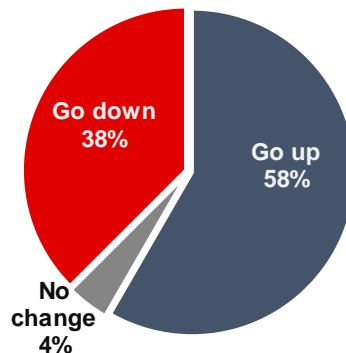


October 16, 2019

Q3 EARNINGS PREVIEW

“Forgive me IBNR, it’s been seven years since my last confession”

Estimated YoY EPS change (% of companies)



Q3 earnings: According to analyst consensus, two-thirds of the 26 companies in the Inside P&C Select are forecast to report YoY increases, aided by modest cats and mild investment tailwinds. However, looking past the quarterly noise, 2020 estimates have been trending lower despite bullishness on pricing. We expect a tension between the good news on pricing versus the emerging bad news on loss costs and investment income. Essentially, to what extent is the faster running by companies being offset by a faster pace on the treadmill, requiring more effort just to stay still? That is the question.

Pricing and loss costs: Two trends appear likely to continue on Q3 earnings calls. First, companies will likely be upbeat on price increases that continue to accelerate and spread to more lines and geographies. However, this will likely be accompanied by an increased atmosphere of confessionals on the loss cost pressures driving rate. For example, one major data point we have on Q3 already is Travelers comments of a “tort environment that came in even above our expectations”. The nature of the insurance business is that pricing follows pain. The nature of executive incentives is that the disclosure of pain often follows the disclosure of better pricing.

International cats: Catastrophe losses are once again on the agenda, with the focus on the international losses from Typhoon Faxai and Hurricane Dorian (inc. some US losses). The pre-announced numbers yesterday (Ren Re and Everest Re) and last week (Axis and Arch) exceed the actual cat losses incurred in Q3:18 (see table below). However, it is worth noting the comparison is distorted by the fact Jebi losses for some companies developed unfavourably since Q3:18.

Investments: As insurance rates continue to see momentum, investment income continues to see emerging headwinds. The yield on the 10-year US Treasury fell to near all-time lows in September, falling in the third quarter to 1.68% from around 2% in the second quarter. Though executives have been sanguine to date as buoyant equity markets have continued to boost NII, we expect more focus on the emerging ROE headwind in Q3.

Brokers: Expectations on both growth and margin expansions are elevated following stellar performance in the recent quarters. Analysts are expecting organic growth to exceed 5% at Aon, Willis Towers Watson and AJ Gallagher. MMC’s report on 10/29 will be highly watched as the firm continues to absorb near-term JLT headwinds.

INSIDE P&C RESEARCH

Gavin Davis, Director of Reserach
gavin.davis@insidepandc.com
(212) 224 3328

James Thaler, CFA, Senior Analyst
james.thaler@insidepandc.com
(212) 224 3336

Dan Lukpanov, CFA, Research Analyst
dan.lukpanov@insidepandc.com
(212) 224 3326

Gianluca Casapietra, Research Analyst
gianluca.casapietra@insidepandc.com
(212) 224 3495

Index	QTD	YTD
Large Cap	(3.1)%	23.9%
Regional	(0.5)%	12.3%
Specialty	(3.0)%	24.8%
Personal	(2.7)%	18.5%
Bermuda	(3.2)%	34.2%
Florida	(4.1)%	(20.1)%
Brokers	(1.4)%	25.9%
IPC Select	(2.9)%	11.4%
S&P 500	0.6%	19.5%
S&P Fin.	0.1%	17.7%

Source: S&P Global, Inside P&C

First up: RLI, Progressive, and BB&T offer early reads

First to get the ball rolling will be **Progressive** in personal lines this morning, rounding out its Q3 report with its monthly report for September. This will be followed by the first data point on the commercial market from **RLI** this evening.

Given RLI's niche businesses and narrow focus, we expect a more meaningful read on the broader market to begin in earnest next week when Travelers reports, and on the more dislocated specialty markets from **WR Berkley**.
























































The following week will see earnings come thick and fast with over 60 percent of the Inside P&C Select firms scheduled to report.

Also this week, **BB&T** reports this Thursday, and its insurance unit should provide early clues on the state of the insurance broking business, with expectations elevated in relation to both growth and margins. Recall, the broker's record organic growth of 11.6% last quarter set the tone for the brokers that followed with solid growth figures.

EXHIBIT: P&C EARNINGS CALENDAR

Source: S&P Global, NASDAQ, Inside P&C

 - before market opens  - after market closes

mon	tue	wed	thu	fri
14-Oct	15-Oct	16-Oct	17-Oct	18-Oct
		Progressive  RLI 	BB&T 	
21-Oct	22-Oct	23-Oct	24-Oct	25-Oct
	Travelers  WR Berkley 	Employers Holdings  Scor 	AJ Gallagher  Cincinnati  Erie  Old Republic 	Aon 
28-Oct	29-Oct	30-Oct	31-Oct	1-Nov
CNA  Brown & Brown  Everest  Mercury 	MMC  AFG  Allstate  Arch  Axis  Chubb  Markel  RenRe  Watford Re 	Blue Capital  Donegal  Hanover  Mapfre  NatGen  Selective  United Insurance 	State Auto  Willis Towers Watson  Amerisafe  Heritage  Kinsale  Swiss Re 	AIG  Argo* Greenlight*
4-Nov	5-Nov	6-Nov	7-Nov	8-Nov - 15 Nov
Hartford  Kemper 	Alleghany  HCI  Third Point 	United Fire  Horace Mann  Intact  James River  Zurich 	Munich Re  RSA  Aviva* Maiden*	Beazley (8-Nov)  Berkshire (9-Nov)  Talanx (11-Nov)  Kingstone (11-Nov)  Prosight*

*CapIQ or Nasdaq algorithm-based estimated date

2/3 P&C carriers expected to grow earnings YoY

According to analyst consensus, two-thirds of the 26 companies in the Inside P&C Select with at least three EPS estimates are forecast to report YoY EPS increases.

EXHIBIT: SUMMARY OF YOY EPS CHANGE EXPECTATIONS

Source: S&P Global, Inside P&C

Company	Peer group	Q3-18 EPS	Q3-19E cons.	% chg	Est. #
AFG	Specialty	\$2.19	\$2.01	↓ -8%	7
AIG	Large Commercial	-\$0.34	\$1.06	↑ NM	18
Alleghany	Other	-\$1.07	\$7.82	↑ NM	4
Allstate	Personal	\$2.16	\$2.33	↑ 8%	16
Arch	Bermuda	\$0.61	\$0.66	↑ 7%	13
AXIS	Bermuda	\$1.09	\$0.94	↓ -14%	10
Berkshire Hathaway	Other	\$4186.05	\$4404.06	↑ 5%	3
Chubb	Large Commercial	\$2.41	\$2.60	↑ 8%	19
Cincinnati	Regionals	\$0.84	\$0.84	↓ -1%	8
CNA	Large Commercial	\$1.17	\$0.97	↓ -17%	4
Everest Re	Bermuda	\$4.09	\$3.34	↓ -18%	10
Hanover	Regionals	\$1.97	\$2.04	↑ 3%	5
Hartford	Large Commercial	\$1.15	\$1.22	↑ 6%	16
Heritage	Florida	\$0.65	\$0.30	↓ -54%	4
Kemper	Personal	\$1.60	\$1.45	↓ -9%	5
Markel	Specialty	\$5.20	\$8.04	↑ 55%	5
Mercury	Personal	\$1.11	\$1.02	↓ -8%	3
National General	Other	\$0.65	\$0.67	↑ 2%	4
Progressive	Personal	\$1.34	\$1.29	↓ -3%	18
RenRe	Bermuda	\$0.73	\$2.47	↑ 238%	10
RLI	Specialty	\$0.46	\$0.51	↑ 10%	5
Selective	Regionals	\$0.99	\$1.06	↑ 7%	8
State Auto	Regionals	\$0.44	\$0.47	↑ 6%	4
Travelers	Large Commercial	\$2.54	\$2.37	↓ -7%	20
United Insurance	Florida	-\$0.35	\$0.11	↑ NM	4
WR Berkley	Specialty	\$0.75	\$0.66	↓ -12%	11

In general, results are expected to improve largely due to the relatively benign US cat-losses in Q3, partly counterbalanced by international losses that are estimated to moderately exceed historical norms. Notable YoY changes are expected at:

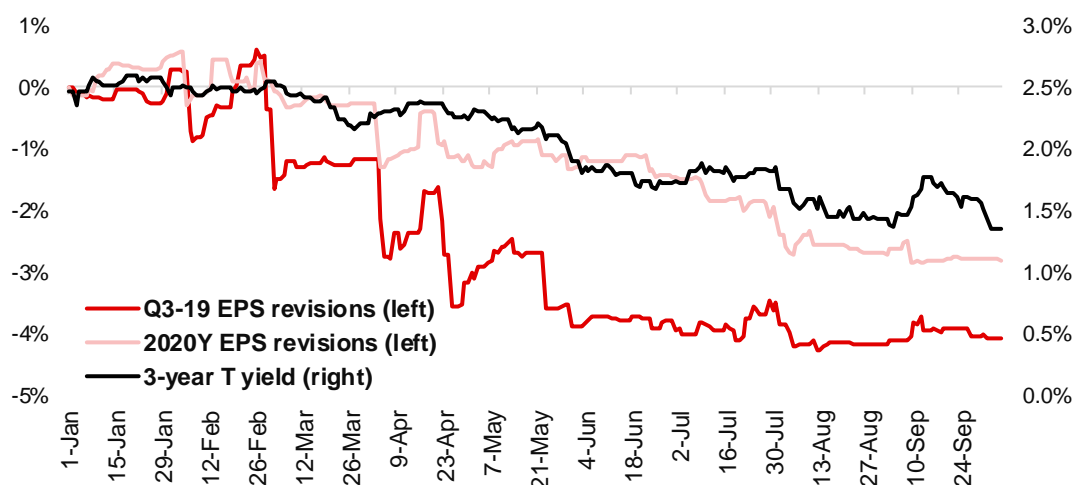
- **AIG** is expected to report improved underwriting results versus Q3:18 when the company recorded cat-related losses of \$1.6bn (22pt on the combined ratio), as well as adverse development from California mudslides.
- **Alleghany** is forecast to recover from unprofitable Q3:18 where the company absorbed \$183mn of cat losses that contributed 19.4pt on the combined ratio of 111.5%.
- **Markel** is expected to improve underwriting bottom-line against breakeven underwriting in the prior period impacted by \$76mn cat losses (6.4pt).
- **RenRe's** EPS was estimated to go up more than three-fold following \$178mn (34.4pt) catastrophe charge in Q3:18. However, its update last night means this estimate will likely reset in the coming days.
- **United Insurance** is estimated to report a profitable quarter following \$34.6mn cat losses (20.2pt) in Q3:18.

EPS estimate revisions trend downwards

Since the start of the year analysts' EPS revisions tilted downward, largely echoing the downtrend of the US interest rates (see chart below). More recently, heading into Q3 in early September analysts briefly revised the estimates upwards reflecting the fixed income yields rebound and the more favourable trajectory of Hurricane Dorian for US carriers. However, the growing optimism was short-lived as the yields reverted to downtrend following disappointing September PMI data from the world's large economies.

EXHIBIT: AVG EPS EST. REVISIONS AND 3-YEAR T-YIELD YTD

Source: S&P Global, Bloomberg, Inside P&C



While declining yields are one of the drivers of EPS revisions, the emergence of loss cost pressures is also likely a factor, focusing attention on whether balance sheet weakness is a greater problem than realized.

Among those calling attention to this issue was **Travelers**. In one of the few significant data points we have as a likely harbinger of Q3 trends, the firm indicated at the Barclays Global Financial Services Conference in September that the tort environment came in even above the company's expectations.

"We got an expectation for an upward trend, but we saw that come in even above what our expectations were and one consequence of that is you get a lengthening of the claim development patterns. This is an issue that continues to persist, and we're going to see the impact of that in the third quarter." – **CEO Alan Schnitzer**

Notably analysts at Bank of America downgraded Travelers to "neutral" following the disclosure, and cut 2019 full year EPS forecast citing reserve strength concerns.

We also note the "fear" driving market correction in many longer-tail lines also speaks to a higher probability of potential negative surprises for some names, and the balance of those two countervailing forces remains to be seen.

Pricing acceleration is the base case

As always, pricing will be a major focus on company conference calls. With rates gaining momentum in Q1, sustaining through Q2 and further bullish outlooks vocalized throughout conference calls in both quarters, the baseline scenario for Q3 pricing momentum is acceleration. As usual, we expect a widespread of views on the market in terms of bullishness, typically explained easily by mix.

We expect a continuation of recent themes, with wholesale pricing better than retail, and more dislocation in large and complex risks where the reduction of line sizes has made programs harder to place.

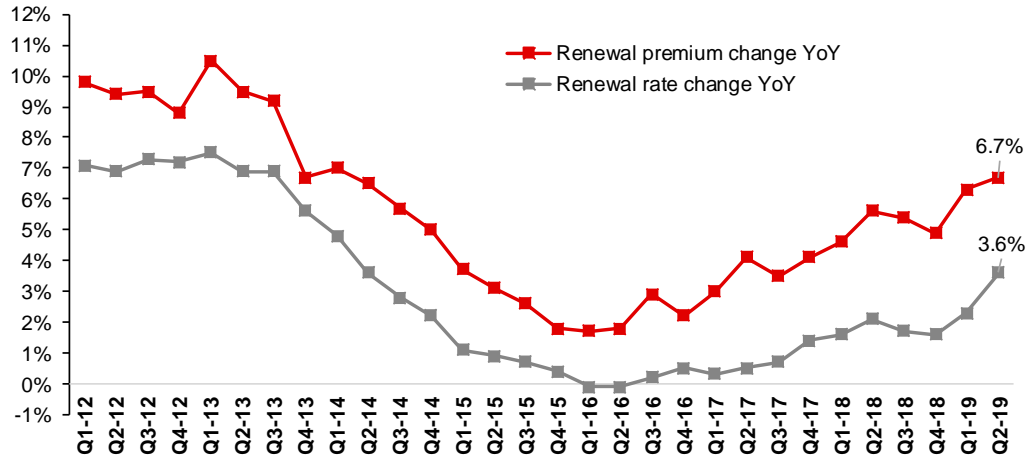
EXHIBIT: Q2 PRICING COMMENTARY FROM LEADING CARRIERS

Source: S&P Global, Inside P&C

AIG	<p>"Rate increases accelerated in the second quarter, in some cases, materially. I've seen a number of market cycles and each one has different characteristics. I would <u>describe this market as one where there is more underwriting discipline and rigor around the deployment of capacity rather than a major decline in capacity</u>. That discipline seems to be playing out through the pricing models and underwriting processes that are recognizing increased loss cost frequency, the tort environment and other emerging risks. To me, that means that tort is based on facts rather than emotion and is therefore, more sustainable."</p> <p>- CEO Brian Duperreault</p>
CB	<p>"The pricing environment continued to firm through the quarter, and we took advantage of some of the best pricing we've seen in years. The rate of increase of prices accelerated, while at the same time, it's spread to more classes of business and more classes of risk. Overall, where rates are moving, they are firming broadly with varying degrees to almost all short and long tail classes. In my judgment, given some of the market dislocation we've observed, including a reset of risk appetite on the part of some, <u>this firming trends is sustainable and will likely to continue to accelerate and spread</u>. It is income and loss reserve-driven not capital-driven."</p> <p>- CEO Evan Greenberg</p>
TRV	<p>"In Buisness Insurance, we increased renewal rate change and renewal premium change both year-over-year and sequentially in each of our product lines other than workers' compensation."</p> <p>- CEO Alan Schnitzer</p>
HIG	<p>"I would note that loss trends in certain lines needed increased pricings to achieve acceptable returns and in part, informed our judgments on the acquired reserves and the 2019 accident year loss picks. The team is focused on capturing the benefit of improving pricing, terms and conditions, particularly in international where results in recent years have been poor."</p> <p>- CEO Jerome Swift</p>
WRB	<p>"Long story short, it's the same old story. Yes, as we've discussed, we have better data and we have better analytics. But the fact is, this industry responds to pain. And there is a growing amount of pain. That is what's driving the change in behavior. And <u>there is a growing amount of evidence that pain is going to increase or build from here</u>, which undoubtedly will drive the market to tighten further."</p> <p>- CEO Rob Berkley</p>

EXHIBIT: TRAVELERS DOMESTIC BUSINESS INSURANCE PRICING

Source: S&P Global, Inside P&C



Despite the bullishness from carriers, brokers have so far been more circumspect.

As we pointed out last quarter, the brokers are caught between a soft and a hard place in terms of the multiple stakeholders they have to manage in their disclosures.

On the one hand, a hardening market is, all else equal, good for insurance broker earnings (and therefore stock prices).

On the other, brokers represent clients and need to push back as hard on pricing as possible, and therefore need to maintain a certain level of control in public messaging.

Conference call transcripts are widely consumed by multiple stakeholders. Clients are unlikely to be happy about gleeful pricing commentary, junior brokers are likely to take any sign of surrender as permission to cave, and underwriters at carriers likely to take any hot takes as ammunition for negotiations.

EXHIBIT: Q2 PRICING COMMENTARY FROM LEADING BROKERS

Source: S&P Global, Inside P&C

AON	"The impact from pricing was modest for the quarter and for the first half of the year." - CEO Gregory Case
AJG	"While I am pleased that we have a bit of a tailwind, I would not get extra bullish on the rate environment." - CEO Patrick Gallagher
BRO	"There's still a lot of capital that needs to get put to work and therefore we do not believe there's going to be large swings in pricing in the near future." - CEO Powell Brown
MMC	"Ultimately, we can't predict the mid to longterm outlook for pricing, but the current conditions are firmer almost across the board." - CEO Daniel Glaser
WLTW	"This is a better environment than we've had for a while." - CEO John Haley

Heading into Q3 earnings, pricing expectations are high. Insurance executives Q2 bullish commentaries and those in-between the quarterly reports has been indicative of a continued upward momentum.

For example, CEO of General Insurance at AIG Peter Zaffino speaking at AIG's conference call in early August (AIG is typically one of the latest P&C reporters in a quarter) noted that the momentum has likely continued into Q3.

Similarly, WR Berkley and Hanover Insurance executives shared further optimism around pricing speaking at [KBW conference](#) in early September.

EXHIBIT: IN-BETWEEN EARNINGS PRICING COMMENTARY

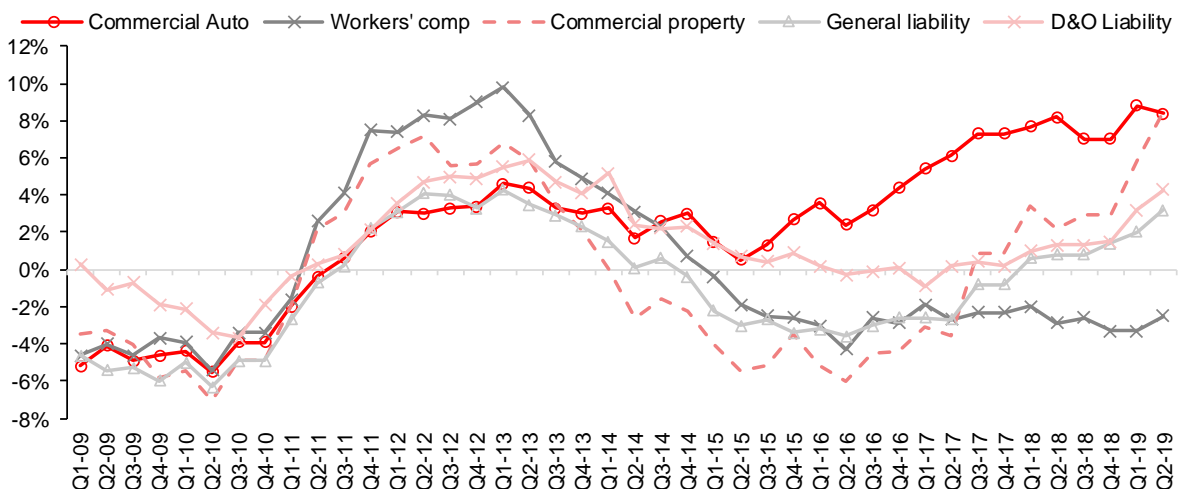
Source: S&P Global, Inside P&C

AIG	"It's too early. But I would expect just based on sort of qualitative commentary that the third quarter, early reactions are similar to what we've seen in the second quarter." - CEO of General Insurance Peter Zaffino
WRB	"There is a growing amount of evidence that would lead us to believe that the momentum is building." - CEO Rob Berkley
THG	"We are optimistic about the current environment. I think the combination of some continued underwriting improvements, along with the rates that are available today in the marketplace, we feel very good about at least the short-term trajectory of the firm" - CEO John Roche

Another data point came from CIAB whose highly watched survey suggested significant pockets of the market are the hardest they have been for close to two decades.

EXHIBIT: CIAB RATE DISCLOSURES

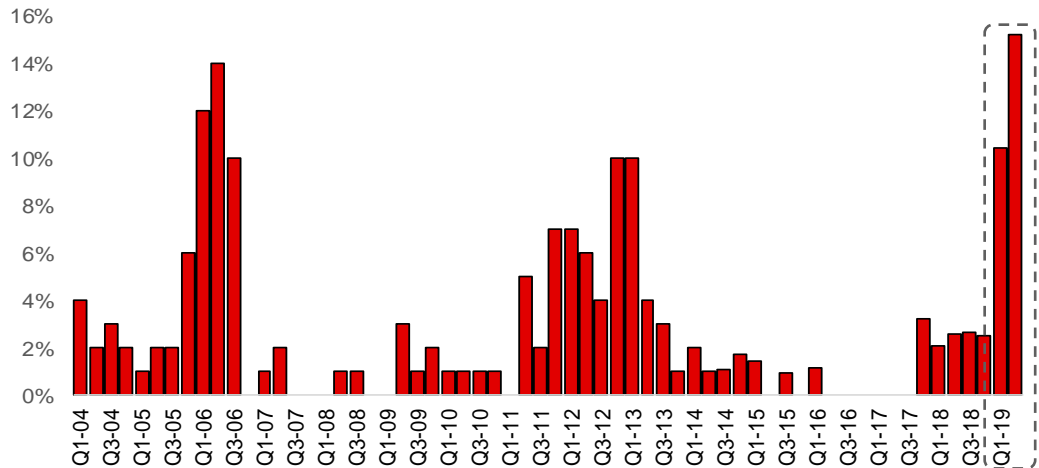
Source: CIAB, Inside P&C



For both medium and large account business, more respondents are indicating a "hard market" of greater than 10% price increase than at any time since 2003. By line, commercial property, umbrella, and medical malpractice are all indicating the biggest percentage of disruption since the early 2000s. (See: [Hard Market Watch: The CIAB edition](#) for background).

EXHIBIT: LARGE ACCOUNTS: PERCENTAGE OF RESPONDENTS INDICATING +10% PRICE INCREASES

Source: CIAB, Inside P&C



Loss costs: The faster treadmill

Despite the bullishness on pricing, we expect some of this will be tempered by an increased atmosphere of confessionals. The nature of this business means that pricing follows pain. The disclosure, however, often reverses that flow, with the good news on pricing coming first, and the bad news on loss trend coming only once the “cover” of pricing momentum provides an offset.

This has been signalled from Travelers in its bearish commentary on the tort environment indicated above, and we expect it will not be alone in this regard. And given the companies superior data capabilities, we expect this to be a leading indicator of trends many will see further down the line.

In many ways, the increasing loss cost trend and emerging ROE pressures from lower investment yields mean insurers must run faster just to stay still on a faster moving treadmill.

International cat losses in focus again

Catastrophe losses are once again on the agenda, with focus on the international losses from Typhoon Faxai and Hurricane Dorian (inc. some US losses)..

The pre-announced numbers from yesterday (Ren Re and Everest Re) and last week (Axis and Arch) exceed the actual cat losses incurred in Q3:18 (see table below). However, it is worth noting the comparison is distorted by the fact Jebi losses for some companies developed unfavorably since Q3:18.

EXHIBIT: PRE-DISCLOSED Q3 CAT LOSSES (BASED ON P/T LOSSES)

Source: Company reports, S&P Global, Inside P&C

	Axis				Arch			
	Q3:17	Q3:18	Q3:19E		Q3:17	Q3:18	Q3:19E	
	Actual	Actual	Lower	Upper	Actual	Actual	Lower	Upper
Cat losses, P/T (\$mn.)	616.8	92.0	150.0	175.0	347.8	58.2	65.0	75.0
Per share, P/T	7.40	1.09	1.78	2.07	0.86	0.14	0.16	0.18
Points on the combined	61.4pt	7.5pt	13.2pt	15.4pt	27.6pt	4.5pt	5.0pt	5.8pt
% of common equity	13.2%	2.0%	3.1%	3.6%	4.3%	0.7%	0.6%	0.7%

	RenRe			Everest Re		
	Q3:17	Q3:18	Q3:19E	Q3:17	Q3:18	Q3:19E
	Actual	Actual	Approx.	Actual	Actual	Approx.
Cat losses, P/T (\$mn.)	615.1	151.9	155.0	1370.2	240.0	280.0
Per share, P/T	15.54	3.83	3.56	33.52	5.92	6.93
Points on the combined	156.0pt	34.4pt	33.0pt	85.7pt	13.9pt	16.2pt
% of common equity	15.5%	3.6%	3.0%	17.3%	2.9%	3.2%

Relative to 2017 and 2018, the 2019 US wind season has been more subdued, featuring 13 storms to 2018's 15, but with storms of more moderated intensity and less significant land falling impacts.

In 2018, Hurricanes Michael and Florence combined for \$15bn losses versus the average Dorian estimate of \$5bn, with most of Dorian's losses concentrated in the Caribbean.

For US-focussed carriers without international or reinsurance exposure, cat losses are likely to be relatively benign.

Internationally, Typhoon Faxai that tore through Tokyo in early September was the largest catastrophe in the quarter. The estimated insured losses varied from \$3-7bn by AIR to \$5-9bn by RMS. Everest released cat loss numbers on Tuesday--\$160m for Faxai and \$120m for Dorian—that pegged Faxai as a \$9bn loss event.

Japanese carriers MS&AD Insurance Group and Sompo Japan Nipponkoa are each expecting to take around \$1bn of losses from the typhoon.

Beyond cat losses, we remain watchful for any commentary on rising attritional property losses and large individual risk losses that have become increasingly prevalent in market chatter.

EXHIBIT: Q3 CAT SUMMARY

Source: Aon Benfield, Inside P&C and other public sources

Dates	Catastrophes	Location	Insured loss est.
United States			
07/02-07/04	Powerful storms	Plains, Midwest, Northeast	\$100mn+
07/04-07/05	Earthquakes	California	Up to \$50mn
07/04-07/05	Thunderstorms	Rockies, Plains	\$575mn+
07/07-07/08	Heavy rainfall	Maryland, Washington DC, Virginia	\$150mn
07-13-07/17	Hurricane Barry	Southeast, Midwest, Mid-At., Northeast	\$300mn
07/17-07/18	Thunderstorms	Rockies, Midwest	Up to \$200mn
07/17-07/23	Severe thunderstorms	Midwest, Northeast, Mid-Atlantic	\$100mn+
07/26-07/30	Severe thunderstorms	Midwest, Northeast	\$100mn+
08/04-08/05	Severe thunderstorms	Midwest	\$510mn
08/06-08/07	Convective storms	Plains, Midwest	\$110mn
08/06	Torrential rainfall	Maryland	Millions
08/10-08/11	Severe thunderstorms	Rockies, Plains	\$425mn
08/13-08/16	Severe thunderstorms	Rockies, Plains, Midwest	\$250mn+
08/17-08/18	Hail	Midwest, Northeast	\$100mn+
08/25-08/26	Hail, winds	Rockies, Plains, Midwest, Southeast	\$100mn+
09/04-09/06	Hurricane Dorian	Southeast, Mid-Atlantic	Up to \$600mn
09/10-09/12	Severe thunderstorms	Rockies, Plains, Midwest	\$240mn
09/17-09/20	Tropical Storm Imelda	Plains, Southeast	Up to \$1bn
09/27-09/28	Severe thunderstorms	Plains, Midwest	Up to 100mn
International significant cats			
08/09-08/11	Typhoon Lekima	China	\$1bn
08/31-09/07	Hurricane Dorian	Caribbean, Bahamas	\$5bn
09/08-09/09	Typhoon Faxai	Japan	up to \$9bn
09/11-09/15	Torrential rain	Spain	\$300mn

Investments: Another emerging ROE headwind

As insurance rates continue to see momentum, investment income continues to see emerging headwinds and has received greater attention from insurance executives. The yield on the 10-year US Treasury fell to near all-time lows in September, falling in the third quarter to 1.68% from around 2% in the second quarter.

Indeed, the growing shortfall of investment income has been cited among executives as one reason the current insurance rate cycle should have legs as carriers compensate for the sustained low yield environment.

While less interest rate sensitive than banks and life insurance peers, P&C companies nonetheless face headwinds. With portfolio durations in the range of 3-4 years, companies in our coverage universe are less likely to see a major immediate impact to earnings, but could be looking at a soft patch on the investment side as lower yields earn through in the coming quarters and years ahead.

On Q2 conference calls P&C executives seemed calm about the developments in the bond market. Perhaps most notable episode was Travelers pointing to the gap between maturing and new money yields, and cutting NII guidance

EXHIBIT: Q2 INVESTMENT INCOME COMMENTARY

Source: S&P Global, Inside P&C

CB	<p>"Despite the negative impact of lower rates, we expect net investment income to grow moderately due to our growth in invested assets and strong cash flow. Although market yields have declined significantly in recent months, we will remain conservative in our investment strategy and do not contemplate any significant shift in asset allocation."</p> <p>- CFO Philip Bancroft</p>
TRV	<p>"In the fourth quarter of last year, we were reinvesting at book yields comfortably above money running off. We were above in this first quarter, but less so, but obviously in the second quarter, we slipped below and rates were at the lowest point in that cycle. I can tell you that the gap, as we measure it, is in excess of 50 basis points and can run higher than that."</p> <p>- CFO Daniel Frey</p>
ALL	<p>"I'll just remind everyone that back in 2016, the 10-year hit a 1.37%. It's hovering a little bit above 2% right now. And in the periods that ensued past that we were still able to return good returns in the portfolio."</p> <p>- CIO John Dugenske</p>

The relative tranquility with which P&C executives has been addressing the subject is understandable. As we showed in "[Making interest rates grate again](#)", investment income, despite making up for ~60-70% of P&C earnings, historically contributed much less into the volatility of earnings, falling short of underwriting and other non-insurance profits in our earnings growth contribution analysis (see chart below).

Additionally, to some extent, investment income is an "input" to pricing, and as the 2011-2014 pricing cycle showed, an increasingly rational P&C market can adjust its earnings model to offset weaker NII from higher underwriting income.

However, market commentaries in-between the quarters were more mixed and some industry CFOs shared concerns about the implications of the low interest rate environment (see table below).

EXHIBIT: P&C EARNINGS GROWTH CONTRIBUTION ANALYSIS

Source: Company reports, S&P Global, Inside P&C

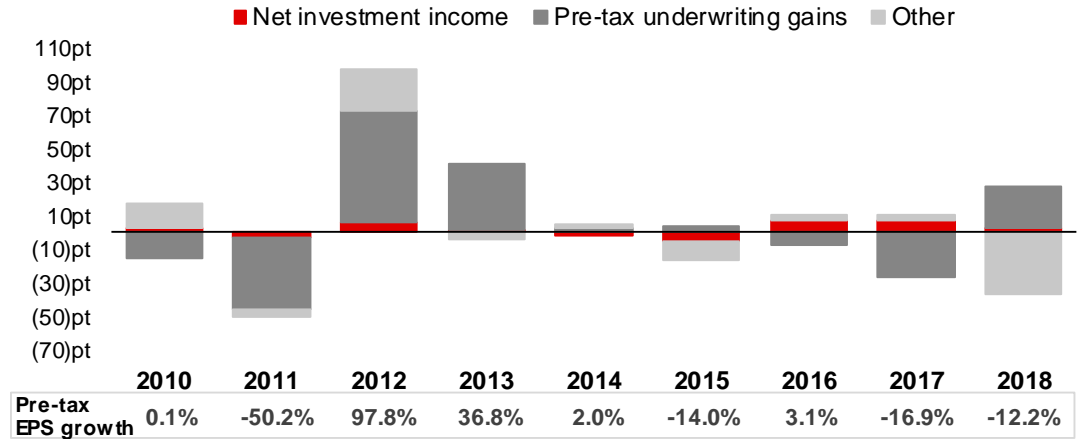


EXHIBIT: IN-BETWEEN EARNINGS INVESTMENT INCOME COMMENTARY

Source: S&P Global, Inside P&C

ARGO	<p>"This is one of those things that keeps me awake at night because it's really challenging. And let me do just simple math, we run a 3-year duration. That means you've got 12 quarters worth of assets, but 3 years later you're going to have to turn the thing over. So every quarter, you've got 8.5% of your portfolio rolling off, reinvesting at fixed rate, 1.5 plus 75 plus 100. It depends on what sort of credit ratio you want to take. In our core bond portfolio, we maintain a pretty conservative risk profile. So factor that math into the net investment income, and we're just going to start to see an impact again pretty quickly, which is disappointing because we -- I felt like we've come out of that trough and we were seeing some momentum there. "</p> <p>– CFO Jay Bullock</p>
SIGI	<p>"We love this interest rate environment because it forces companies to underwrite. Big decrease in rates puts pressure on overall income performance in our sector, so you have to look at the overall portfolio between investments and underwriting to achieve your target returns and I think that is good for the industry in terms of discipline from the underwriting, risk selection and pricing perspective".</p> <p>- CFO Mark Wilcox</p>

The Federal Reserve cut its benchmark interest rate in July and September, and with traders projecting another rate cut in October at 65% probability, the much discussed lower-for-longer scenario of recent years looks to play out.

For those insurers with greater exposure to equities, US stock markets will likely contribute minimally to earnings after the S&P rose a modest 1.2%, with a similar increase in Q2 providing some modest tailwinds to alternative income (largely booked on a one quarter lag).

Note that despite the theoretical offset of better pricing to offset investment income, this can come at a lag as pricing is often done incrementally to not shock clients into shopping the account. Additionally, there is a risk of some marginal push towards self-insurance rather than simply accepting price increases.

Brokers: Will results support high expectations?

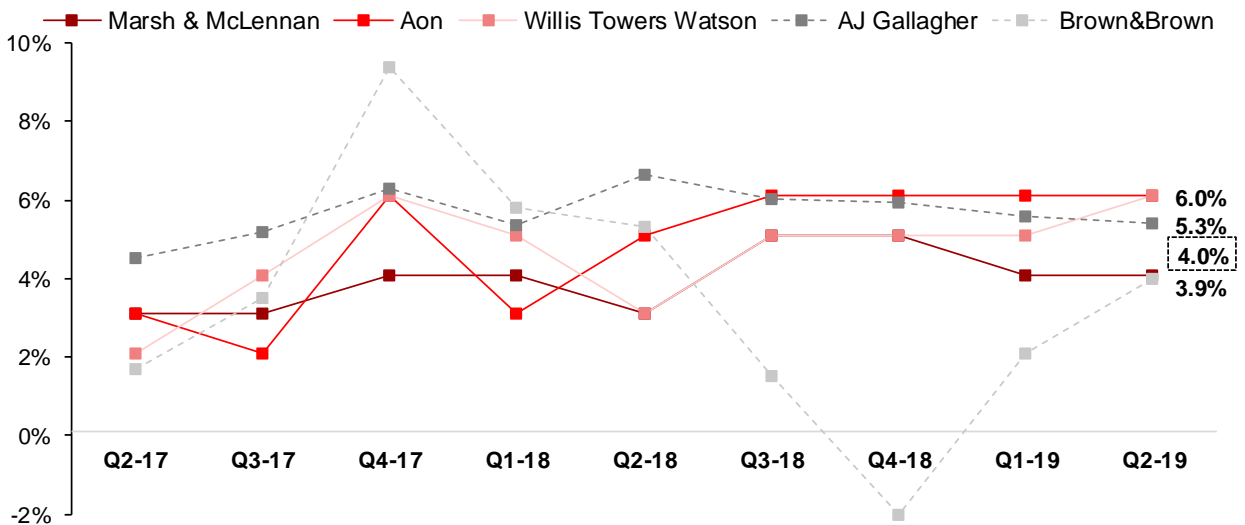
The insurance intermediaries are once again tasked to hit a high bar as market expectations on both growth and margin expansions are elevated following the stellar performance in the recent quarters.

Analysts are expecting organic growth to exceed 5% at Aon, Willis Towers Watson and AJ Gallagher. A slower growth of around 3% is expected from Brown & Brown as the broker continues facing headwinds in National Programs segment due to underperformance of the lender-placed business.

Marsh & McLennan is also expected to trail the peers on growth as the JLT-related revenue-leakage will likely continue hurting the YoY comparison, particularly on reinsurance. Recall, Guy Carpenter saw an organic contraction of 11% last quarter.

EXHIBIT: ORGANIC GROWTH

Source: Company reports, S&P Global, Inside P&C



Elsewhere, the results of margin expansion ambitions will also be topical, with particular focus on the initiatives at Willis Towers Watson in its efforts to catch up with the peers.

BB&T Insurance Holdings results that are set to release this Thursday will be highly scrutinized for an early read on P&C market conditions.

This research report was written by Insider Publishing's Research team which includes Gavin Davis, Gianluca Casapietra, Dan Lukpanov and James Thaler.

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