Inside P&C by The Insurance Insider

July 30, 2019

REINSURANCE: A DECLARATION OF DEPENDENCE

Mercury and NatGen highlight challenges of companies dependent on reinsurance facing higher implied cost of capital

In a flood of earnings announcements Monday, one of the most interesting takeaways were two data points on reinsurance buying that highlights the capital market linkages contributing to a shifting operating environment across P&C. Both **Mercury General** and **National General** have benefitted from an extremely indulgent reinsurance market in recent years. Ironically, both companies put in place their expiring structures almost immediately prior to the HIM hurricane season in July 2017.

For **Mercury General**, the company has benefitted from the ability to buy down its excess of loss (XoL) cat protection to a net retention of just $10mn (or ~0.3pts on the combined). This has shielded the company from significant earnings volatility through a period of higher frequency cat losses - a non-trivial benefit given the firm has failed to cover its dividend from operating earnings since 2011. However, as we explore below, the experience of going through the top of its XoL program in 2018, and possible rating agency pressure, has forced a difficult trade off. The company has traded more top-end balance sheet protection, for higher earnings volatility, and exposure to post-event financing surge-pricing.

For **National General**, the company was previously able to cede a significant percentage of its homeowners' insurance book for a 42% ceding commission representing an override benefit to expenses. However, following significant gross cat losses in 2017 and 2018, the company's two year program has re-priced with a 6.5% lower ceding commission and a new annual structure increasing the frequency of re-pricing events. Back of the envelope math on ~10-15% of premium levered ~2x on common equity implies over 0.5pts of drag on the total combined ratio, and close to 1pt of post-tax ROE impact, all else equal.

In short, both have benefitted from soft reinsurance pricing as a form of capital, and represent interesting and visible data points of a phenomenon undoubtedly playing out across P&C. Though transfer mechanisms from **retro → reinsurance → primary markets** can take time to play out, and has not really been cited as a factor to date, ultimately capital restraints and a higher blended cost of capital must force a reaction in primary.

The unavoidable conclusion is that the cost of capital for P&C is going up as volatility is re-priced. For many quality companies and net underwriters, this will be a trivial change. However, those who have most heavily depended on reinsurance and retro either as a source of cheap capital, financial engineering, or arbitrage opportunity, will face tougher choices ahead.

Quick Hits:

- **Arch's reserve releases drop 41%**
- **Mercury General: 29% EPS Miss and cat restructure**
- **Everest Re: Light cats and NII boost earnings**
- **Donegal: Personal lines remain a drag**

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Index	QTD	YTD
Large Cap	3.0%	24.9%
Regional	(0.2)%	11.4%
Specialty	3.0%	22.8%
Personal	0.5%	23.3%
Bermuda	3.4%	29.5%
Florida	(12.1)%	(27.1)%
IPC Select	(1.2)%	9.2%
S&P 500	2.7%	20.5%
S&P Fin.	2.9%	19.3%

Source: S&P Global, Inside P&C

REINSURANCE: A DECLARATION OF DEPENDENCE

- ***Reinsurance dependence highlighted by MCY and NGHC renewals.***
- ***Mercury General swaps more top-end balance sheet protection for more earnings volatility and no reinstatement.***
- ***National General homeowners' Q/S ceding commission cut 6.5% following 2017 and 2018 losses.***

In a flood of earnings announcements Monday, one of the most interesting takeaways were two data points on reinsurance buying that highlights the capital market linkages contributing to a shifting operating environment across P&C.

Both **Mercury General** and **National General** have benefitted from an extremely indulgent reinsurance market in recent years. Ironically, both companies put in place their expiring structure almost immediately prior to the HIM hurricane season in July 2017.

First **Mercury General**.

The company confirmed on its Q2 call that it had almost trebled its reinsurance limit to $589mn from $205mn on its prior program that expired at 1 July.

Mercury said total reinsurance costs were down slightly at $38mn versus $40mn YoY. The company gave limited details, with more expected when it files its 10-Q. However key details given include.

- First, the prior program had a pre-paid reinstatement, which was responsible for $18mn of the prior spend. The new program appears not to have a reinstatement, so the total spend is really $38mn versus an expiring $22mn for the first event limit.
- Second, the new program has an increased retention from $10mn to $40mn. Management said the pricing on the layer from $10mn to $40mn was "just too high" and "did not make economic sense". (Indeed, we're curious who *wrote* the expiring layer that must have been repeatedly tagged, and on what terms).

The combination of these two changes (more on top, but higher retention) makes the risk-adjusted pricing difficult to compare but like-for like layers are understood to have priced up significantly based on prior private conversations with reinsurance market sources.

Note, the re-structured program essentially provides more balance sheet protection against large catastrophe losses. Recall, the company went through the top on its XoL program in 2018, while an increased focus on wildfire risk specifically in its home state of California by multiple stakeholders including investors, regulators, and rating agencies has likely pressured the company to rethink its enterprise risk management priorities.

However, against that, the removal of the reinstatement and the increased retention significantly increases other types of risk.

One simple way of thinking about this is that the company has traded more top-end balance sheet protection for higher earnings volatility.

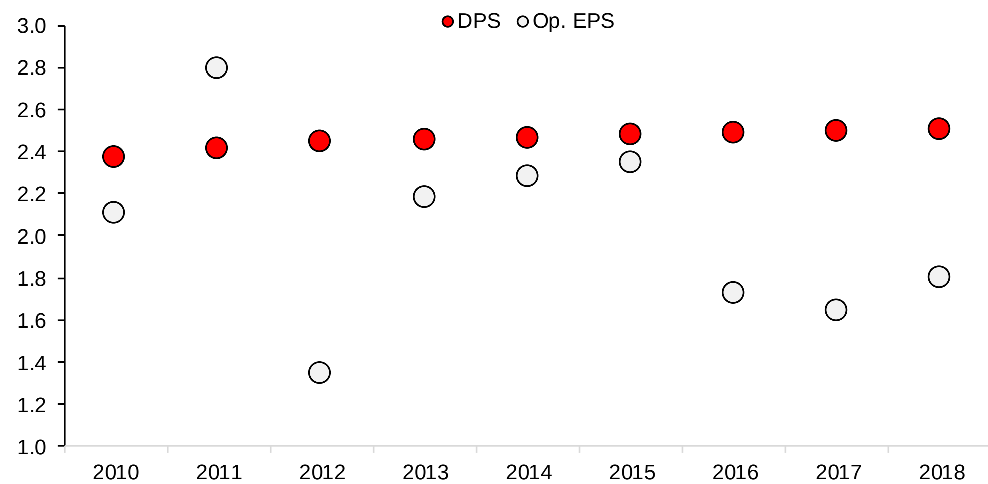
This is non-trivial. The carrier's earnings have been repeatedly protected by its low cat XoL retention since it was lowered ahead of hurricane season in 2017, including multiple hurricane and wildfire losses with gross losses in excess of $10mn.

Even so, the company has not covered its dividend with operating earnings since 2011 (See chart below).

Retaining more earnings volatility net is likely to add additional strain on its ability to find its dividend out of earnings rather than excess capital, though earnings power will not be increased due to the purchase of more limit. E.g. the savings from the dropped bottom layer and reinstatement are being reinvested in the increased top-end protection.

EXHIBIT: MERCURY ANNUAL DPS AGAINST OPERATING EPS

Source: S&P Global, Inside P&C



Additionally, the lack of a pre-paid reinstatement exposes the company to increased risk around post-event risk-financing surge pricing. Given the recent wildfire losses and conditions that appear conducive to elevated risk of events this year, again, this is again non-trivial risk.

In fact, the company's maneuver highlights the challenges of trying to increase risk-management programs without the flexibility of being able to comfortably trade some margin and ROE for more protection without making significant trade-offs on other priorities (e.g. around dividend funding).

Recall, the company saw its AM Best FSR downgraded from A+ to A in December last year, with the agency hinting at concerns around the level of exposure to catastrophic losses and the level of its reinsurance protections.

> *AM Best: "This geographic concentration risk factor, which has gradually become more pronounced over the past several years, was underscored by its record fire losses in 2017 and 2018 and adverse auto bodily injury loss cost trends in California… While Mercury's current reinsurance program has thus far demonstrated sufficient capacity to absorb the fire-*

> *<u>related events, Mercury remains somewhat exposed</u> to additional catastrophe events through the end of June 2019, given that the first layer of reinstated limit on its reinsurance treaty has been exhausted."*

It seems a reasonable interpretation that the increased reinsurance purchase is at least in part due to pressure from its rating agencies (and other external stakeholders like investors and regulators), though the experience of blowing through the top and a re-assessment of wildfire risk was likely enough to sharpen the firm's focus on the issue anyway from an enterprise risk management perspective.

<u>Net take:</u>

The simple unavoidable interpretation is that the combination of increased reinsurance cost and increased exposure to multiple events forced a difficult trade-off on the company.

Protecting the balance sheet is job #1, and in that sense the firm's decision makes sense.

But the trade-off results in increased earnings volatility that will add risk to the firm's ability to fund its dividend from earnings, while the dropped reinstatement adds risk of exposure to post-event risk-financing surge pricing.

These are both <u>non-trivial</u> risks. We expect investors will likely not immediately price in this risk (small cap, underfollowed name), though expect it will manifest over time as risk tends to.

National General: homeowners' Q/S prices up

Meanwhile, NatGen also disclosed the updated details for its two quota shares covering its home and auto business.

Recall, reinsurance is a "*must-have*" for Nat Gen, not a "*nice to have*", in our view.

Nat Gen's annualized H2 gross premiums represent leverage on tangible common equity of 3.8x (and 2.9x on total tangible equity including the company's $450mn of preferreds).

Other sources of capital flexibility appear constrained. Debt and preferred to total capital is at 36%.

And the firm could face some challenges tapping capital markets giving ongoing issues around securities issued by related-party companies AmTrust and Maiden (e.g. de-listing and not paying preferred dividends).

As such, the firm's capital management options may be somewhat constrained. Recall, the last equity issuance was done at an ~8% discount in late 2018.

With that as context, most interesting, to us was the **homeowners' quota share** renewal, which has a 40% cession rate broadly in line with its prior structures.

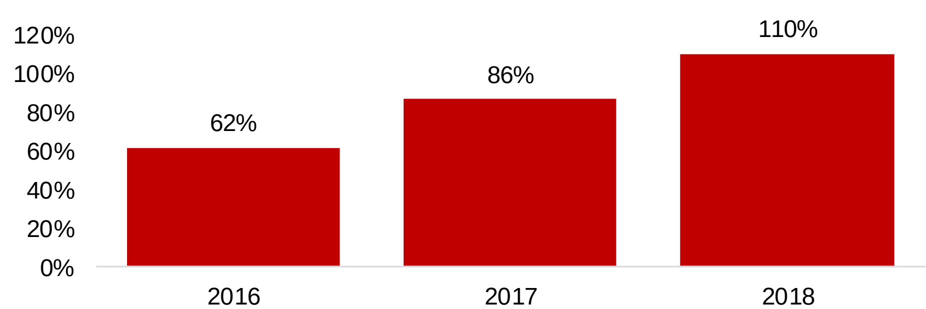
However, in line with sister-publication *The Insurance Insider's* reporting, the treaty moved to an annual structure from a two-year renewal, with the ceding commission dropping 6.5pts to 36%. (Due to a run-off of a prior agreement, the weighted average ceding commission for in-force business is 37.5%).

Recall, the company has repeatedly hit both its Q/S and XoL reinsurance partners with a series of catastrophe losses including 2017 hurricane events, and Hurricane Michael and California wildfires in 2018.

For example, the firm's statutory direct loss ratio in Homeowners multi-peril increased to 86% in 2017 and 110% in 2018.

EXHIBIT: NATGEN HOMEOWNERS' MP DIRECT LOSS RATIO

Source



Prior to 2017 and the inception of the additional reinsurance support, the direct loss ratio had been running around 50% on average since 2014, perhaps explaining the willingness of reinsurers to give up a 42.5% ceding commission.

However, the structure of the deal always looked priced for perfection, with any catastrophes likely to threaten the profitability for reinsurers = priced to a low 90s combined ratio on a cat free year.

From a reinsurance perspective, the economics of the deal appear much improved, but still stretchy. Back of the envelope the deal looks to be priced for a "normal" year combined in the mid-80s.

For NatGen, our (very) back of the envelope for the financial impact looks something like this to us.

Homeowners premiums are 10-15% of the portfolio, translating to around 0.5pts to 1pt of drag on the total combined ratio. With total premium leverage of ~2x common equity, this translates to something like ~0.8-1.5pts of ROE drag, all else equal (e.g. with no pricing offset on underlying, which may ultimately come).

Net take:

For us, the Nat Gen homeowners repricing highlights the risk to companies dependent on reinsurance in a tightening market. Though reinsurance capacity remains plentiful, the ability to arbitrage it as a cheaper form of capital is diminishing, and companies using it as a significant part of their capital structure should face a higher blended cost of capital.

Additionally, it may bring into focus those companies with a low expense ratio that is really due to financial engineering from overriding ceding commissions from reinsurers rather than true operating efficiency.

ARCH'S RESERVE RELEASES DROP 41%

- ***Q2 reserve development falls 2.4 points YoY to 2.7% on the combined following Jebi-related reserve strengthening in Q1***
- ***Reinsurance segment underlying loss ratio improved by 7.3 points to 67.5% from 74.8% YoY***
- ***Acquisition expense ratio of 13.8% is lowest in 17 years***

Arch Capital reported Q2 earnings of $0.77 per share with a positive surprise of 14.9% against analyst estimates and up 30.5% YoY.

The result was driven by:

- **Lower underlying loss ratio** of 52.2% from 55.5% YoY as the ratio improved in all three of Arch's segments.
- **Net investment income increase** of 14.3% to $1.3bn.
- **Lower catastrophe losses** – $7.4mn versus $14.9mn.
- **Expense ratio improvement** to 27.8% from 28.5%.
- Offset by **less favorable reserve development**, particularly in its reinsurance segment ($11.3mn favourable development versus $31.9mn favourable development in the prior year period).

EXHIBIT: ARCH CAPITAL Q2 RESULTS

Source: Company reports, Inside P&C

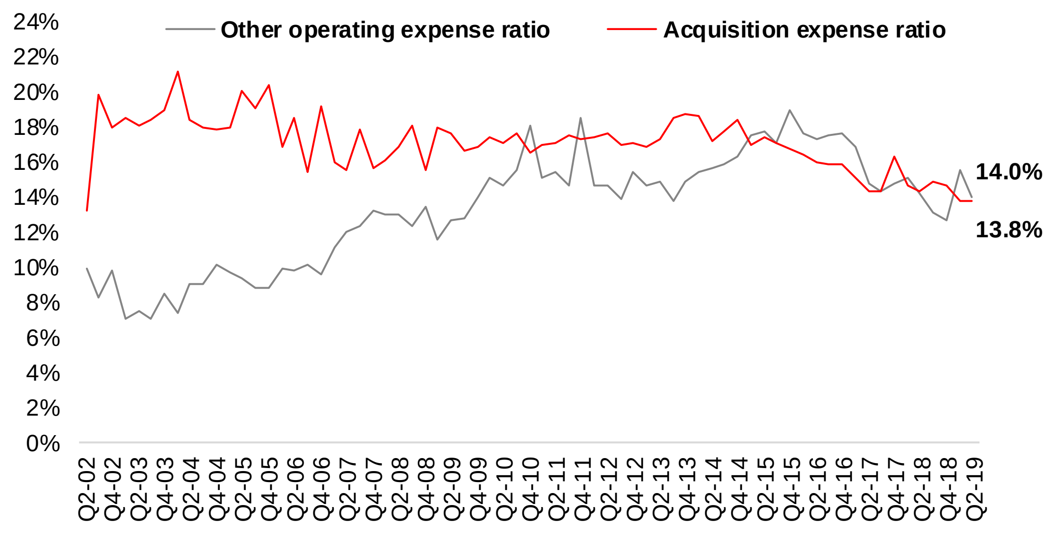
	Arch Capital				EPS beat:	14.9%
$mn, except per share	**Q2-18**	**Q3-18**	**Q4-18**	**Q1-19**	**Q2-19**	**y/y Var**
Operating EPS	$0.59	$0.59	$0.46	$0.67	$0.77	**30.5%**
GWP	$1,591	$1,623	$1,599	$1,980	$1,830	15.0%
NWP	$1,158	$1,182	$1,169	$1,380	$1,326	14.4%
NII	$136	$144	$157	$157	$155	14.3%
Loss and LAE	$726	$699	$828	$719	$768	5.7%
Acquisition expenses	$203	$202	$209	$198	$210	3.6%
Other operating expenses	$176	$161	$166	$201	$199	12.9%
U/W income	$236	$235	$189	$266	$298	26.3%
Cat ratio	*1.3%*	*5.0%*	*9.7%*	*0.6%*	*0.5%*	*-0.8pts*
Prior year	*(5.1%)*	*(6.7%)*	*(6.1%)*	*(3.0%)*	*(2.7%)*	*+2.4pts*
Ex-cat AY loss ratio	*55.5%*	*53.8%*	*53.5%*	*52.1%*	*52.2%*	*-3.3pts*
Loss ratio	51.7%	52.1%	57.1%	49.7%	50.0%	-1.7pts
Acquisition expense ratio	*14.3%*	*14.9%*	*14.6%*	*13.8%*	*13.8%*	*-0.5pts*
Other operating expense ratio	*14.2%*	*13.1%*	*12.7%*	*15.5%*	*14.0%*	*-0.2pts*
Expense ratio	28.5%	28.0%	27.3%	29.3%	27.8%	-0.7pts
Combined ratio	**80.2%**	**80.1%**	**84.4%**	**79.0%**	**77.8%**	**-2.4pts**
BVPS	$20.68	$21.15	$21.52	$23.12	$24.64	6.6% QoQ
Op. ROAE (annualised)	11.6%	11.4%	8.8%	12.3%	13.1%	+1.5pts
Segment highlights						
Insurance AY ex.cat CR	98.5%	100.2%	98.3%	100.2%	99.4%	*+0.9pts*
Reinsurance AY ex.cat CR	100.0%	92.5%	96.2%	92.4%	92.2%	*-7.8pts*

Arch's results will likely be scrutinized on today's earnings call scheduled for 9AM ET on the following themes:

- **Deterioration in reserve releases** will certainly be topical as the market is anticipating details on the development of Typhoon Jebi losses that hit Bermudians in Q1 and may have further adversely developed according to various market reports. Most markets now considering Typhoon Jebi total insured losses to be $15-16bn versus some firms' picked estimates of $8-10bn. Recall, earlier London-based Hiscox issued a profit warning and reported Q2 $40mn reserve strengthening associated with Typhoon Jebi and Hurricane Michael. Arch's Q2 reports available upon earnings release includes no information on Typhoon Jebi creep.
- We expect the significant **reinsurance underlying loss ratio improvement** of 7.3 points to be attributed to smaller non-cat large property claims in Q2:19 versus Q2:18 (as well as Q2:17) when such losses made Arch's reinsurance business unprofitable on the basis of an underlying combined ratio.
- **Rates in cat exposed property pockets** firmed easily into double-digits according to the reports coming from various carriers. Some more data points from Arch are anticipated.
- **Improving expense ratios** in P&C (re)insurance is something that is sticking out in our minds over the last several quarters but seemingly has not been receiving much attention. Arch's reported acquisition expense ratio of 14.0% is the lowest in 68 quarters of the last 17 years. Recall, WR Berkley last week reported lowest quarterly expense ratio in 11 years.

EXHIBIT: ARCH CAPITAL EXPENSE RATIO

Source: Company reports, Inside P&C



MERCURY: 29% EPS MISS AND REINSURANCE RESTRUCTURE

- ***15.9% decrease in operating EPS, driven by underwriting***
- ***Reinsurance renewal raises limit and retention to $589mn and $40mn from $205mn and $10mn respectively***

Earnings highlights:

- 29% operating EPS miss
- Operating EPS down 15.9% to $0.74 per share
- 42% decline in underwriting income
- 98.3% combined, 1.4pt deterioration
- Flat NII growth or +0.7% to $35mn
- Top line NWP growth of 6.6% to $936mn

EXHIBIT: MERCURY Q2:19 EARNINGS RESULTS

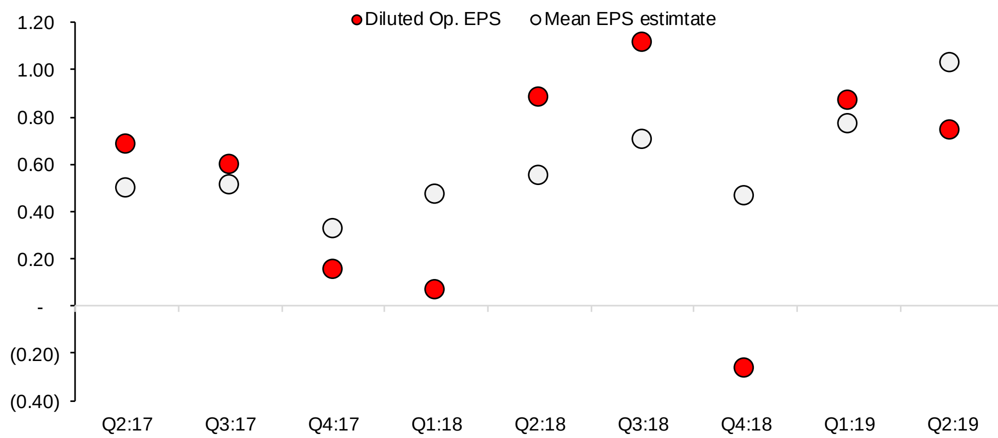
Source: Mercury General, Inside P&C

	MCY Consolidated					
$k	**Q2:18**	**Q3:18**	**Q4:18**	**Q1:19**	**Q2:19**	**VAR**
Operating EPS	**$ 0.88**	**$ 1.11**	**$ (0.26)**	**$ 0.87**	**$ 0.74**	**-15.9%**
NWP	878,418	905,339	850,609	916,448	936,079	6.6%
NII	34,786	38,159	31,383	34,174	35,032	0.7%
Loss and LAE	(605,547)	(614,069)	(724,939)	(630,416)	(656,577)	8.4%
Operating expenses	(202,342)	(206,199)	(201,870)	(215,902)	(217,049)	7.3%
U/W income	26,070	37,867	(58,576)	23,927	15,150	-41.9%
AY ex-cat loss ratio	69.9%	69.3%	75.9%	71.8%	71.8%	2.0pts
Loss ratio	72.6%	71.6%	83.5%	72.4%	73.9%	1.3pts
Expense ratio	24.3%	24.0%	23.3%	24.8%	24.4%	0.2pts
Combined ratio	96.9%	95.6%	106.7%	97.3%	98.3%	1.4pts

The firms 15.9% decline in operating EPS largely stems from its 42% decline in underwriting income.

EXHIBIT: MERCURY GENERAL QUARTERLY EPS BEAT/MISS

Source: S&P Global, Inside P&C

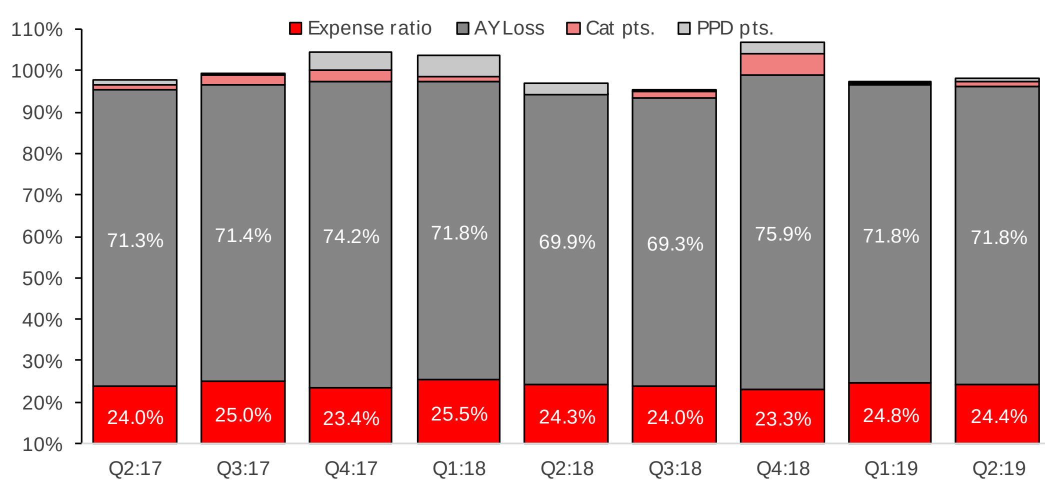


The firm's combined ratio deteriorated 1.4pts to 98.3% YoY. While the firm's underlying loss ratio rose by 2pts to 71.8%, the firm experienced low cats and reserve development when compared to Q2:18. The firm's expense ratio remained flat at 24.4%.

- The heightened combined ratio largely stems from states outside of California, which posted a cumulative combined ratio of 108%. This compared to 92% in the second quarter of 2018.
- The firm's homeowners business also managed an underwriting loss with a combined of 102% in Q2:19 in comparison to 95.3% in 2018. The homeowners business was impacted by increased loss estimates related to CA rainstorms that occurred during the first quarter of 2019.

EXHIBIT: MERCURY GENERAL COMBINED RATIO BREAKDOWN

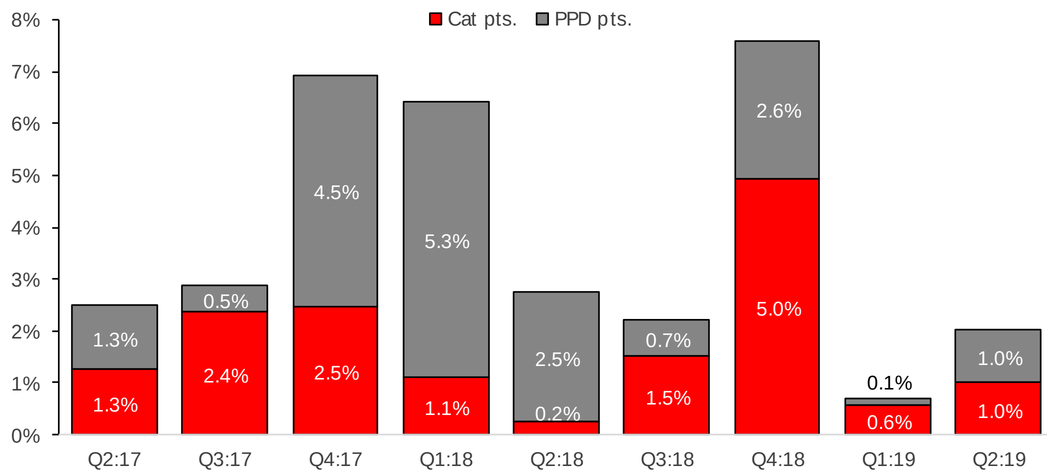
Source: Mercury General, Inside P&C



In Q2:19, catastrophes ($9mn) and reserve development ($9mn) contributed less to the combined than in 2018 ($2mn and $21mn), offsetting the higher underlying loss ratio.

EXHIBIT: MERCURY GENERAL CAT & PPD BREAKDOWN

Source: Mercury General, Inside P&C



On top line, the firm grew written premiums by 6.6% to $936mn. The growth largely stems from price increases while PIF growth remained in the low single digits for its homeowners business, and roughly flat for its personal lines.

EXHIBIT: MERCURY GENERAL PRICING COMMENTS

Source: S&P Global, Inside P&C

Mercury	Personal auto rate 6.9% || Homeowners rate 6.9%

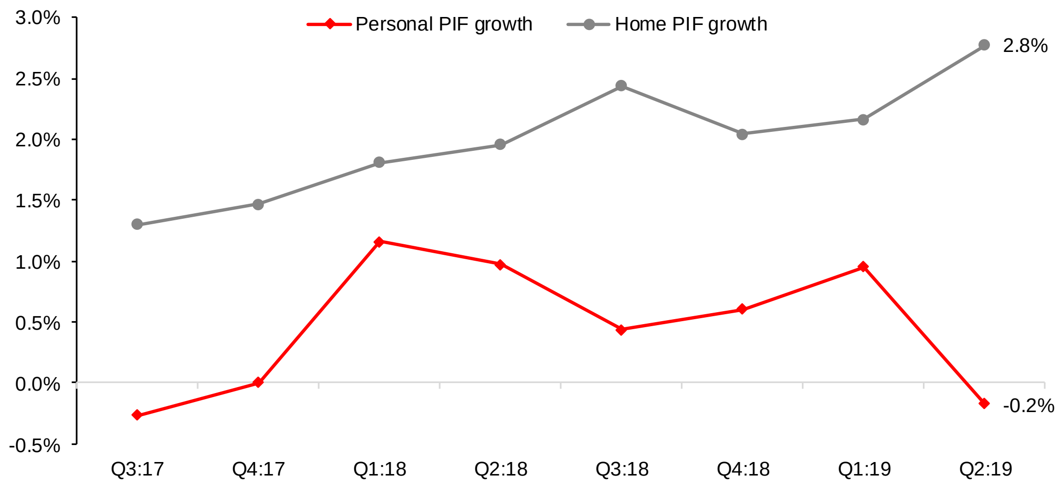
The firm's personal auto segment reflects 2/3 of companywide direct premiums earned. Roughly 32% of the rate increase was earned for the CA auto insurance company, and for the Mercury insurance company roughly 10%.

The homeowners' rate was approved with an implementation month of August, and an additional 6% rate increase in the CA homeowners business was recently filed. The CA homeowners business is approximately 12% of the firm's direct earned premiums.

While the firm's PIF growth continues to accelerate in homeowners, PIF growth in personal lines is struggling to gain momentum. Homeowners grew at 2.8% in Q2:19 to 630k policies, and personal lines shrunk by 0.2% to 1,166k policies.

EXHIBIT: MERCURY GENERAL PIF GROWTH

Source: Mercury General, Inside P&C



As noted in the article above, the firm also restructured its reinsurance program.

CEO Gabriel Tirador on reinsurance: *"We recently completed our catastrophe reinsurance treaty renewal effective July 1, 2019. The total reinsurance limit purchase increased from $205 million in the prior period to $589 million for the July 2019 through June 2020 period. Our retention increased from $10 million to $40 million. Total annual premiums on a new reinsurance program are approximately $38 million. For the prior reinsurance treaty, total premiums were $40 million, including $18 million of reinstatement premiums."*

EVERESTRE Q2: LIGHT CATS AND NII BOOST EARNINGS

- ***Eightfold increase in operating EPS to $7.85***
- ***Result reflects improved combined ratio of 88.2%***
- ***Company cited "strong" property cat renewal***

Everest's strong operating income growth largely stems from a cat light quarter in which it lost $30mn from catastrophes. This pales in comparison to Q2:18's $497mn of catastrophe losses. The firm also boosted its adjusted operating EPS by growing its net investment income by 26.7% to $179mn.

EXHIBIT: EVEREST RE Q2:19 EARNINGS RESULTS

Source: EverestRe, Inside P&C

	RE Consolidated					
$mn	**Q2:18**	**Q3:18**	**Q4:18**	**Q1:19**	**Q2:19**	**VAR**
Operating EPS.	**$ 0.98**	**$ 4.09**	**$ (5.89)**	**$ 6.91**	**$ 7.85**	**701.0%**
GWP	2,066.5	2,198.7	2,278.4	2,127.1	2,166.7	4.8%
NWP	1,746.4	1,938.8	2,057.1	1,851.7	1,784.0	2.2%
NII	141.3	161.4	140.2	141.0	179.0	26.7%
Loss and LAE	1,341.3	1,251.9	2,001.1	1,048.6	1,094.6	-18.4%
Operating expenses	476.5	479.3	480.8	488.5	525.8	10.3%
U/W income	(88.0)	0.3	(630.9)	195.7	196.9	NM
AY ex-cat loss ratio	54.3%	58.5%	60.0%	59.2%	59.6%	5.3pts
Loss ratio	77.5%	72.3%	108.1%	60.5%	60.2%	(17.3)pts
Expense ratio	27.6%	27.7%	26.0%	28.2%	29.0%	1.4pts
Combined ratio	105.1%	100.0%	134.1%	88.7%	89.2%	(15.9)pts

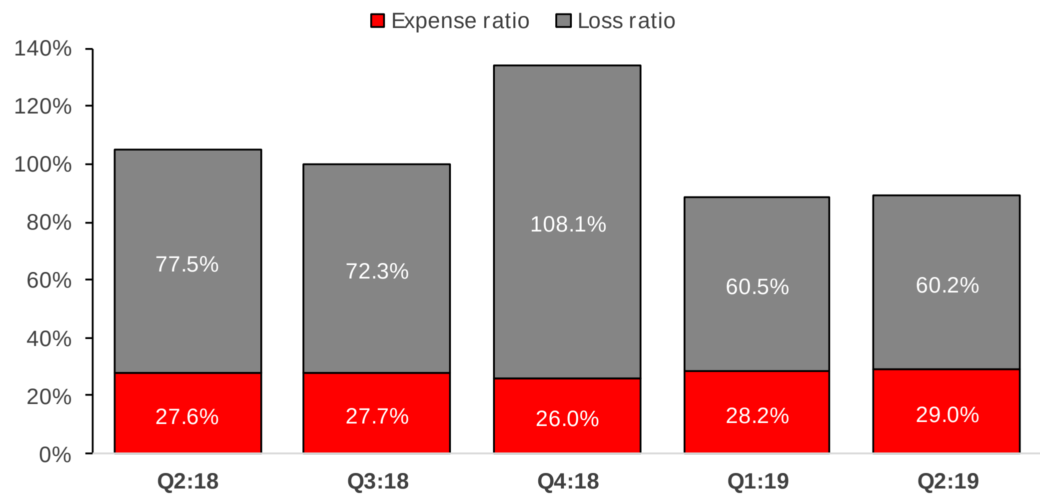
Even while both the firm's underlying loss ratio and expense ratio deteriorated by 5.3pts and 1.4pts respectively, the firm was able to shed 15.9pts off it's combined, leaving the firm with a headline 89.2% result.

Reserve releases amounting to 1.1pts benefitted the firm's combined ratio, but in Q2:18 the firm experienced 5.6pts worth of favorable development.

In 2018, cat losses contributed 28.8pts to the combined, while in 2019 only 1.7pts.

EXHIBIT: EVEREST COMBINED RATIO BREAKDOWN

Source: EverestRe, Inside P&C



CEO Dominic Addesso commentary: *"Everest delivered outstanding results for the quarter, with a 16.1% annualized net income return on equity, driven by both solid underwriting and investment performance. With nearly $9 billion in common equity and strong franchises in both reinsurance and insurance, our ability to adjust the mix of business to optimize our portfolio was again evident this quarter, as Everest added top line in insurance and casualty reinsurance along with a strong property cat renewal to take advantage of the improved market conditions."*

DONEGAL: PERSONAL LINES REMAINS A DRAG

- ***Growth in operating EPS of $0.15 per share to $0.13***
- ***14.9% growth in net investment income***
- ***102% combined ratio, 3.6pt improvement***
- ***Rate increases ex-Workers Comp of 4.6%***

Donegal's EPS growth stems from improved underwriting results, and NII growth. The firm's underwriting performance benefited from a 3.4pt drop in its loss ratio to 69.7%, and a 0.5pt improvement in its expense ratio to 31.3%. All in, the firm still reported an underwriting loss with a combined ratio of 102%, albeit down 3.6pts in comparison to Q2:18.

The 3.4pt improvement to the loss ratio stems from lower weather related losses of $17mn, a 0.5pt improvement, and 1.5pts of favorable reserve development in its workers comp line of business.

EXHIBIT: DONEGAL Q2:19 EARNINGS RESUTLS

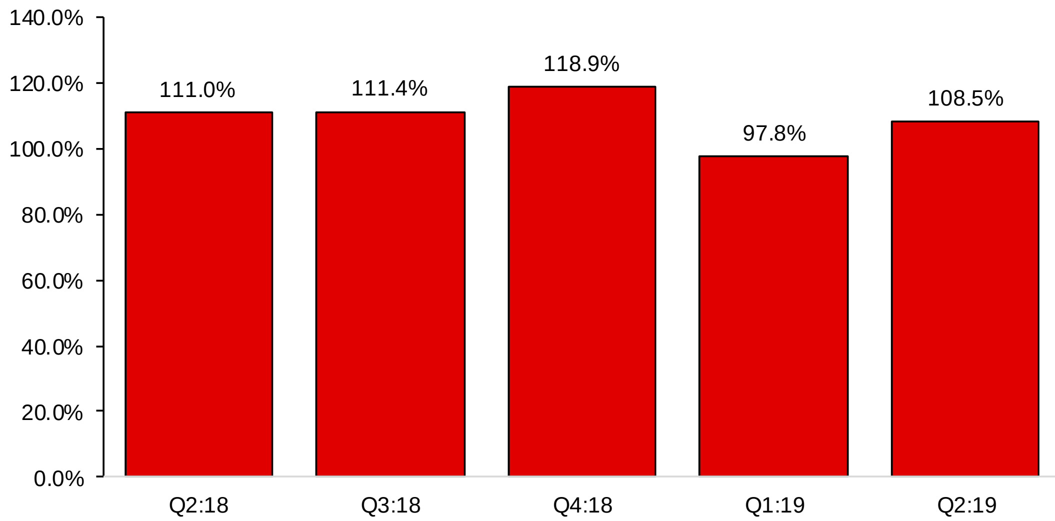
Source: Donegal, Inside P&C

	DGICA Consolidated					
$k	**Q2:18**	**Q3:18**	**Q4:18**	**Q1:19**	**Q2:19**	**VAR**
Operating EPS.	**$ (0.02)**	**$ (0.03)**	**$ (0.30)**	**$ 0.26**	**$ 0.13**	**NM**
NWP	195,949	184,518	168,293	199,915	197,803	0.9%
NII	6,342	6,620	7,567	7,049	7,290	14.9%
Ex-cat loss ratio	63.6%	63.7%	70.3%	60.4%	60.7%	(2.9)pts
Loss ratio	73.1%	75.0%	77.0%	65.5%	69.7%	(3.4)pts
Expense ratio	31.8%	29.6%	32.5%	32.6%	31.3%	(0.5)pts
Combined ratio	105.6%	105.2%	110.5%	99.3%	102.0%	(3.6)pts
Personal lines CR	111.0%	111.4%	118.9%	97.8%	108.5%	(2.5)pts
Commercial CR	97.3%	97.5%	101.3%	96.4%	92.9%	(4.4)pts

The firm's underwriting loss largely stems from its personal lines business with had a 108.5% combined ratio in Q2:18, down 2.5pts from Q2:18. This compares to the firms commercial lines combined ratio of 92.9%. The firm continues to run-off its unprofitable personal lines business which saw negative NWP growth of 10%. The firm grew its commercial lines business by 13.5%.

EXHIBIT: DONEGAL PERSONAL LINES COMBINED RATIO

Source: company reports, Inside P&C



CEO Kevin Burke commentary: *"We continue to shift our overall mix of business to a higher proportion of commercial business, where we see greater opportunities for profitable growth for the foreseeable future. Net premiums written within our commercial segment grew 13.5% for the second quarter of 2019 and comprised approximately 52.3% of our total writings. We attribute this growth to new commercial accounts our insurance subsidiaries have written throughout their operating regions, a continuation of renewal premium increases that averaged 2.1% and lower reinsurance premiums. Renewal premium increases, excluding workers' compensation, averaged 4.6% for the second quarter of 2019. Our commercial multi-peril and workers' compensation lines generated profitable results, and we have continued to implement commercial automobile rate increases to improve results in that line."*

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