

An Introduction to Demotech, Inc.



DRAGONFLY:
300 MILLION YEARS OLD



T-REX:
EXTINCT

Nature knows size and survival are independent.

Demotech, Inc. had to prove that to the insurance industry.

- In 1989 Demotech filled a gap left by the legacy rating agencies to become the first company to review and rate independent regional and specialty insurers.
- Today Demotech reviews, rates and monitors on a quarterly basis 400 insurers operating throughout the U.S., District of Columbia and Commonwealth of Puerto Rico. These insurers write virtually every line of P&C insurance reported to the NAIC.

Our Business Model

Demotech's business model is to support financially stable insurers that are currently unrated or underrated by others. We do not review or follow insurers if we have concluded they have mediocre, or worse, financial stability.

Our Philosophy

Demotech encourages carriers to focus on long-term solvency. This perspective encourages carriers to establish loss and loss adjustment expense reserves at an adequate level.

With adequate being a higher standard than reasonable, this philosophy also enhances the quality of reported earnings.

Many publicly traded insurers report chronic adverse loss and loss adjustment expense development at a level that does not impact solvency yet impacts the quality of their reported earnings.

Regional and Specialty Insurers Are Under-appreciated. Demotech Understands Them.

- Regional and Specialty Insurers focus on their niche. They may be state, regional or coverage specialists.
- For year-end 2015, P&C carriers reporting to the NAIC, in excess of 2,600 insurers, with 25% by count writing 90% of the premium.

Regional and Specialty Insurers Are Under-appreciated. Demotech Understands Them.

- Maintain consistent underwriting discipline – even if the cost is loss of marketshare.
- Publish transparent financial statements.
- Purchase conservative reinsurance programs from well-respected reinsurers, protecting surplus yet foregoing potential profitability so as to retain the financial stability, flexibility, and consistency required by their insureds, producers, regulators and boards.

Regional and Specialty Insurers Are Under-appreciated. Demotech Understands Them.

- **Maintain stable relationships with agents and core customers.**
- **Succeed in their niches because they understand them. They thrive by serving sectors that their agents, underwriters, customer service, and claims personnel understand.**

Assignment of FSRs

- Demotech recognizes that the assignment of ratings is a complex and multi-faceted process.
- Although concepts, whether diversification or economic modeling, sound quantitative, they can be supplemented by subjective, qualitative biases rather than objective evaluation criteria.

- To the extent possible, Demotech foregoes the utilization of subjective criteria, such as size, geographical or product line diversification.
- By employing long-tenured, experienced insurance professionals, Demotech possesses the capacity and capability to present insights and observations that the inexperienced cannot offer.

Our Primary Analysts

- **Joseph L. Petrelli, ACAS, ASA, MAAA, FCA (MBA)**
President
 - **Sharon M. Romano Petrelli, CPCU, AIAF, CCP, ARC**
Vice President and Co-founder
 - **Barry J. Koestler II, CFA**
Chief Ratings Officer
 - **Robert M. Warren, CPA, CPCU**
Client Services Manager
- Average Number of Years of Insurance Experience: 35
 - Average Number of Years at Demotech Inc.: 25*
- *Incorporated in 1985, the maximum tenure at Demotech is 31 years.

Preliminary FSRs

- Demotech prepares Preliminary Financial Stability Ratings® based upon our interpretation of historical public financial information.
- Finalization is interactive.
- Requires a review of quality (reinsurers) and quantity (applicability) of reinsurance

- Access to management and the consultants or employees who prepare critical financial documents such as SAO, audit, property catastrophe reinsurance models, investment guidelines and advisory services, etc.
- Enterprise Risk Management program and other corporate submissions and information.
- Demotech publishes Comparative Financial Observations™ on carriers that elect not to finalize their PFSRs.

An Independent Analysis

In February 2011, Florida State University's College of Business, Risk Management and Insurance undertook an independent analysis comparing Demotech FSRs with insurer ratings issued by A. M. Best, Standard and Poor's, Moody's and Fitch.

The study reviewed thousands of insurer ratings issued over a nine year period. The results were released in *A Comprehensive Examination of Insurer Financial Strength Ratings*.

The authors concluded that:

- 1. Demotech serves the need of another unique group of insurers, namely those that are geographically focused.*
- 2. Comparisons of Demotech ratings to other agencies show relative consistency in the factors that drive Demotech ratings compared to agencies such as A. M. Best, Moody's, Standard and Poor's, and Fitch.*
- 3. There is also general consistency in the firms that each agency would categorize as financially secure.*

- 4. These results have important public policy implications for insurers, regulators and consumers as they work to better understand the ratings process. Of particular importance to most is the comparability of Demotech ratings to other agencies.*
- 5. Given that lenders often have requirements related to the use of rated insurers and some states require ratings to operate in a state, the results suggest that Demotech serves an important service within the ratings community and plays a very important role in the insurance market.*

Questions?

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