NAIC National Association of Insurance Commissioners & The Center for Insurance Policy and Research

Capital Markets Special Report

The **NAIC's Capital Markets Bureau** monitors developments in the capital markets globally and analyzes their potential impact on the investment portfolios of US insurance companies. A list of archived Capital Markets Bureau Special Reports is available via the **index**

Insurance Company Holdings of Equities: A Detailed Review

Insurance companies are significant holders of equities in their investment portfolios — with equities (common stock and preferred stock) totaling $610.8 billion (or 11.4% of total cash and invested assets) at year-end 2012 — second only to bonds, which were 68.4% of total cash and invested assets. Excluding affiliated equity investments, unaffiliated equities constituted $258.8 billion in investments (or 4.9% of total cash and invested assets) at year-end 2012. This special report provides insight into the insurance industry's common and preferred stock holdings and considers stock exposure trends. In addition, the basics of common and preferred stocks, including valuation methods and risk measurement, are briefly discussed in the appendix to the report.

U.S. Insurance Industry Year-end 2012 Common Stock Holdings

As of year-end 2012, the U.S. insurance industry held $589.6 billion of total common stock holdings, 40.7% of which were unaffiliated investments. Property/casualty (P/C) insurers held the most unaffiliated common stock investments at $191.7 billion (or 79.9% of total industry unaffiliated common stock holdings). Life insurers were the second-largest investors in common stock with $27.9 billion (or 11.6% of total industry unaffiliated common stock holdings). In terms of the mix of affiliated versus unaffiliated investments, fraternal insurers had the highest percentage of unaffiliated common stock holdings (84.0%) while life companies had the lowest (19.4%). Life companies tend to hold less common stock, as fixed-income investments tend to fit better with their yield- and spread-oriented products. P/C companies held 12.2% of their total cash and invested assets in unaffiliated common stock versus only 0.8% for life companies, because stocks provide better liquidity to match P/C insurers' shorter-term liabilities. Table 1 summarizes our findings.

Table 1: 2012 Common Stock Holdings by Insurer Type

Book Adjusted Carrying Value (In US$ billions)	P/C	Life	Health	Fraternal	Title	Industry Total
Affiliated	$ 214.8	$ 115.9	$ 17.6	$ 0.5	$ 1.0	$ 349.8
Unaffiliated	$ 191.7	$ 27.9	$ 17.4	$ 2.4	$ 0.4	$ 239.9
Total	**$ 406.6**	**$ 143.8**	**$ 34.9**	**$ 2.9**	**$ 1.5**	**$ 589.6**
Total as a % of Industry	69.0%	24.4%	5.9%	0.5%	0.2%	100.0%
Affiliated	52.8%	80.6%	50.3%	16.0%	71.1%	59.3%
Unaffiliated	47.2%	19.4%	49.7%	84.0%	28.9%	40.7%
Unaffiliated as a % of C&IA*	12.2%	0.8%	10.7%	2.2%	5.1%	4.5%

*C&IA = Cash & Invested Assets

On average, going back to 2003, insurers have held more affiliated common stock than unaffiliated common stock in their investment portfolio, as shown in Table 2. Unaffiliated holdings grew 22.3% from 2004 to 2006, with unaffiliated common stock peaking at 46.5% of total common stock in 2006 for the time period analyzed. There was a dramatic 33.3% decrease in unaffiliated common stock holdings from 2007 to 2008 due to the financial crisis, as compared to the S&P 500's negative 38.5% return (excluding dividends). Adjusting for unaffiliated common stock net acquisitions of $5.8 billion in 2008, the adjusted BACV decline was 35.8%, closer to the S&P 500's 38.5% decline. Affiliated common stock, however, dropped only 2.6% for the same time period, as these were subsidiaries and mostly non-publically traded common stock holdings that were valued according to *Statement of Statutory Accounting Principles (SSAP) No. 97—Investments in Subsidiary, Controlled and Affiliated Investments*, which provides guidelines for valuing subsidiary, controlled and affiliated common stock holdings. Overall, unaffiliated common stock bottomed at 36.1% of total common stock holdings in 2008 (during the time period analyzed), but has since increased to 40.7% of total industry common stock holdings as of year-end 2012; however, this is still below the peak of 46.5% in 2006.

Table 2: U.S. Insurance Industry Common Stock Holdings 2003-2012

Book Adjusted Carrying Value (In US$ billions)	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
Affiliated	$ 349.8	$ 332.6	$ 323.6	$ 319.3	$ 277.9	$ 285.3	$ 269.2	$ 252.9	$ 243.5	$ 225.1
Unaffiliated	$ 239.9	$ 216.4	$ 199.2	$ 187.1	$ 157.1	$ 235.5	$ 234.1	$ 202.8	$ 191.4	$ 169.0
Total	**$ 589.6**	**$ 549.0**	**$ 522.8**	**$ 506.4**	**$ 435.0**	**$ 520.8**	**$ 503.3**	**$ 455.7**	**$ 434.9**	**$ 394.0**
Affiliated	59.3%	60.6%	61.9%	63.1%	63.9%	54.8%	53.5%	55.5%	56.0%	57.1%
Unaffiliated	40.7%	39.4%	38.1%	36.9%	36.1%	45.2%	46.5%	44.5%	44.0%	42.9%
Unaffiliated as a % of C&IA	4.5%	4.2%	4.0%	3.9%	3.4%	5.0%	5.2%	4.7%	4.7%	4.4%

Because large insurers (those with cash and invested assets greater than $10 billion) tend to own many subsidiaries, affiliated common stock was 61.1% of their total common stock holdings as compared to 38.0% for the smallest insurers (less than $250 million in cash and invested assets). As shown in Table 3, the largest investors of common stock as a percentage of cash and invested assets were the insurers with $1 billion to $2.5 billion in cash and invested assets, at 14.4%.

Table 3: Total Common Stock Holdings by Size of Insurers

Book Adjusted Carrying Value (In US$ billions)	>$10 billion	$5 billion to $10 billion	$2.5 billion to $5 billion	$1 billion to $2.5 billion	$500 million to $1 billion	$250 million to $500 million	<$250 million	Industry Total
Affiliated	$ 233.7	$ 32.0	$ 28.5	$ 30.7	$ 11.2	$ 7.3	$ 6.4	$ 349.8
Unaffiliated	$ 148.8	$ 22.9	$ 17.1	$ 22.7	$ 10.3	$ 7.5	$ 10.5	$ 239.9
Total	**$ 382.4**	**$ 55.0**	**$ 45.6**	**$ 53.5**	**$ 21.5**	**$ 14.8**	**$ 16.9**	**$ 589.6**
% of Industry	64.9%	9.3%	7.7%	9.1%	3.6%	2.5%	2.9%	100.0%
Affiliated	61.1%	58.3%	62.5%	57.5%	52.1%	49.1%	38.0%	59.3%
Unaffiliated	38.9%	41.7%	37.5%	42.5%	47.9%	50.9%	62.0%	40.7%
Total as a % of C&IA	**10.2%**	**13.2%**	**13.3%**	**14.4%**	**13.3%**	**11.8%**	**9.8%**	**11.1%**

Unaffiliated Common Stock Holdings

For the remaining analysis, the report will focus solely on unaffiliated common stock.

As shown in Table 4, within unaffiliated common stock holdings as of year-end 2012, the overwhelming majority consisted of direct common stock investments. Note that this was the case for each of the five industry types except for health companies, whose largest unaffiliated common stock holdings consisted mostly of mutual funds.

Table 4: 2012 Unaffiliated Common Stock Holdings by Insurer Type

Book Adjusted Carrying Value (In US$ billions)	P/C	Life	Health	Fraternal	Title	Industry Total
Common Stock	$ 179.1	$ 23.9	$ 7.2	$ 2.3	$ 0.4	$ 212.8
Mutual Funds	$ 12.6	$ 4.0	$ 10.2	$ 0.2	$ 0.0	$ 27.0
Total	**$ 191.7**	**$ 27.9**	**$ 17.4**	**$ 2.4**	**$ 0.4**	**$ 239.9**
% of Industry	79.9%	11.6%	7.2%	1.0%	0.2%	100.0%
Common Stock	93.4%	85.6%	41.4%	92.6%	91.2%	88.7%
Mutual Funds	6.6%	14.4%	58.6%	7.4%	8.8%	11.3%

Insurance industry allocations to mutual funds over the past 10 years increased from a low of 7.4% of total unaffiliated common stock investments in 2004 to 11.3% as of year-end 2012, as shown in Table 5. According to the Investment Company Institute (ICI), the U.S. mutual fund industry—which includes mutual funds, exchange-traded funds, closed-end funds and unit investment trusts—had $14.7 trillion in assets as of year-end 2012, representing a significant increase from $7.8 trillion in 2003. Looking at only the mutual fund portion, which totaled $13 trillion in assets, 45.5% (or $5.9 trillion) was invested in equities. The advantages of owning mutual funds include diversification, lower transaction costs and management fees (economies of scale due to larger size of funds) and flexibility. There are an abundance of mutual funds to choose from, varying by investment style (e.g., large cap, mid cap, small cap, country, emerging market, etc.).

Table 5: Unaffiliated Common Stock Holdings 2004-2012

Book Adjusted Carrying Value (In US$ billions)	2012	2011	2010	2009	2008	2007	2006	2005	2004
Common Stock	$ 212.8	$ 192.6	$ 176.9	$ 166.9	$ 139.6	$ 214.2	$ 212.8	$ 187.2	$ 177.2
Mutual Funds	$ 27.0	$ 23.8	$ 22.3	$ 20.2	$ 17.5	$ 21.3	$ 21.4	$ 15.6	$ 14.2
Total	**$ 239.9**	**$ 216.4**	**$ 199.2**	**$ 187.1**	**$ 157.1**	**$ 235.5**	**$ 234.1**	**$ 202.8**	**$ 191.4**
Growth (%)	10.8%	8.6%	6.5%	19.1%	-33.3%	0.6%	15.4%	6.0%	
Common Stock	88.7%	89.0%	88.8%	89.2%	88.9%	90.9%	90.9%	92.3%	92.6%
Mutual Funds	11.3%	11.0%	11.2%	10.8%	11.1%	9.1%	9.1%	7.7%	7.4%

Smaller insurers (i.e., those with total cash and invested assets of less than $250 million) tend to hold relatively more mutual funds as a percentage of their common stock investments versus the larger insurers. The largest insurers (i.e., those with total cash and invested assets of more than $10 billion) have almost all of their common stock investments made directly in common stocks (96.2%), as shown in Table 6, versus 67.3% for insurers with total cash and invested assets of less than $250 million.

Table 6: 2012 Unaffiliated Common Stock Holdings by Insurer Size

Book Adjusted Carrying Value (In US$ billions)	>$10 billion	$5 billion to $10 billion	$2.5 billion to $5 billion	$1 billion to $2.5 billion	$500 million to $1 billion	$250 million to $500 million	<$250 million	Industry Total
Common Stock	$ 143.1	$ 20.5	$ 13.2	$ 16.9	$ 7.3	$ 4.8	$ 7.1	$ 212.8
Mutual Funds	$ 5.7	$ 2.4	$ 3.9	$ 5.9	$ 3.0	$ 2.7	$ 3.4	$ 27.0
Total	**$ 148.8**	**$ 22.9**	**$ 17.1**	**$ 22.7**	**$ 10.3**	**$ 7.5**	**$ 10.5**	**$ 239.9**
% of Industry	62.0%	9.6%	7.1%	9.5%	4.3%	3.1%	4.4%	100.0%
Common Stock	96.2%	89.5%	77.3%	74.2%	70.7%	63.6%	67.3%	88.7%
Mutual Funds	3.8%	10.5%	22.7%	25.8%	29.3%	36.4%	32.7%	11.3%

Table 7 shows the industry's acquisitions and dispositions of unaffiliated equities from 2010 through 2012. Overall, the industry net disposed of equities in 2010 but net acquired equities in both 2011 and 2012 with a recovery in the stock market. The industry net acquired $18.7 billion in 2011 but only $2.7 billion in 2012, likely due in part to lingering uncertainties from 2011. These uncertainties included the Eurozone crisis, Greece and Spain's debt problems, and the weak U.S. and European economies. The S&P 500 Index's annual returns (excluding dividends) were negative 38.5% in 2008 during the financial crisis and began to recover in 2009, with a positive return of 23.5%. It continued its recovery in 2010 with a positive 12.8% return, was flat in 2011 and gained another 13.4% in 2012.

Table 7: Insurers' Acquisitions & Dispositions of Unaffiliated Common Stock and Preferred Stock

	2012			2011			2010		
In US$ billions	Acquisitions	Dispositions	Net	Acquisitions	Dispositions	Net	Acquisitions	Dispositions	Net
Common Stock	$ 35.8	$ 33.3	$ 2.5	$ 52.4	$ 29.1	$ 23.4	$ 33.8	$ 34.3	$ (0.5)
Preferred Stock	$ 3.3	$ 3.1	$ 0.2	$ 5.1	$ 9.8	$ (4.7)	$ 2.7	$ 4.8	$ (2.2)
Total	**$ 39.1**	**$ 36.4**	**$ 2.7**	**$ 57.5**	**$ 38.8**	**$ 18.7**	**$ 36.4**	**$ 39.1**	**$ (2.7)**

As of year-end 2012, 76% of the insurance industry's unaffiliated common stock holdings were "large cap," or stocks with market capitalization of greater than $10 billion (as shown in Table 8). Large cap stocks are typically considered higher in quality, more liquid (i.e., higher trading volume), less volatile and pay higher dividends.

*Table 8: 2012 Unaffiliated Common Stock by Insurer Type and Market Cap Breakdown**

Book Adjusted Carrying Value (In US$ billions)	P/C	Life	Health	Fraternal	Title	Total Industry
Large Cap	$ 145.0	$ 11.4	$ 3.8	$ 1.3	$ 0.2	$ 161.7
Mid Cap	$ 18.0	$ 3.8	$ 1.7	$ 0.7	$ 0.0	$ 24.1
Small Cap	$ 2.4	$ 1.5	$ 0.3	$ 0.1	$ 0.0	$ 4.3
ETFs and Other Funds	$ 4.7	$ 1.6	$ 0.7	$ 0.1	$ 0.1	$ 7.3
Non-Traded Stock (incl. FHLB)	$ 9.0	$ 5.6	$ 0.6	$ 0.0	$ 0.0	$ 15.3
Total	**$ 179.1**	**$ 23.9**	**$ 7.2**	**$ 2.3**	**$ 0.4**	**$ 212.8**
Large Cap	81.0%	47.7%	52.8%	59.3%	41.4%	76.0%
Mid Cap	10.0%	15.7%	23.2%	29.7%	10.8%	11.3%
Small Cap	1.4%	6.3%	4.6%	3.7%	0.5%	2.0%
ETFs and Other Funds	2.6%	6.8%	10.4%	5.6%	36.5%	3.4%
Non-Traded Stock (incl. FHLB)	5.0%	23.5%	9.0%	1.7%	10.8%	7.2%

** Large Cap is >$10 billion, Mid Cap is $1-10 billion, and Small Cap is less than $1 billion*

U.S. Insurance Industry Common Equity Valuation Ratios

There are many stock valuation methods, but the various ratios listed below are the simplest and most common, and effectively are snapshots of how the market values a stock. These ratios are useful for peer comparisons or comparing market values. Table 9 summarizes various common stock valuation ratios for the insurance industry's common stock holdings, as compared to the S&P 500 as a market index. Overall, the data shows that insurers tend to hold high-quality, "blue chip" large cap stocks that tend to be more profitable and, thus, pay out more dividend income.

Table 9: Historical Ratios and Dividend Yield

	2012 Insurer average	S&P 500 Index 2012	2011	2010	2009	2008	2007	2006
Price to Earnings (P/E)	15.9	17.1	14.9	16.3	20.7	70.9	21.5	17.4
Price to Sales (P/S)	2.6	1.3	1.2	1.3	1.2	0.9	1.4	1.5
Price to Book Value (P/BV)	4.6	2.1	2.1	2.2	2.2	2.0	2.8	2.8
S&P 500 Dividend Yield	2.5%	2.1%	2.1%	1.8%	2.0%	3.2%	2.0%	1.8%
10-Year Treasury Yield		1.8%	2.8%	3.2%	3.3%	3.7%	4.6%	4.8%

Price to Earnings (P/E) Ratio: As of year-end 2012, the P/E ratio of the insurance industry's common stock holdings was 15.9X, slightly lower than the S&P 500's P/E of 17.1X. The top 30 common stock holdings for the industry totaled $106 billion in book/adjusted carrying value (BACV), nearly half of total unaffiliated common stock holdings. These stocks, on average, had lower P/Es than the year-end 2012 insurer average of 15.9X — including banks, energy, and industrial companies that tend to command P/Es in the high single digits to low teens. The lower P/E reflects slower growth rates in earnings, as these are large companies that are typically in low growth industries.

Price to Sales (P/S) Ratio: In 2012, the P/S ratio of the insurance industry's common stock investments was 2.6X, twice as high as the S&P 500's 1.3X. Some of the large blue chip companies tend to have higher profitability and, therefore, command a higher price for each sale made.

Price to Book Value (P/BV) Ratio: In 2012, the P/BV ratio of the insurance industry's common stock holdings of 4.6X was more than twice the S&P 500's, as insurers generally hold more blue chip companies that have lower book value due to some assets that are carried at low historical costs. Companies such as IBM (10X) and Coca Cola (4.9X) are examples.

Dividend yield versus 10-year treasury yield: In 2012, the 10-year Treasury yield dropped below the common stock dividend yield for the first time since 1957. A major reason is the low interest-rate policy of the Federal Reserve, whereby the Fed funds rate reached historical lows, such as 0.09% as of Dec. 31, 2012. The weighted average dividend yield for the insurance industry's common stock holdings was 2.5%, higher than the S&P 500 dividend yield of 2.1% in 2012. This is due, in part, to insurance companies' more conservative investment philosophy, which typically focuses on holding higher-quality companies that usually pay higher dividends.

U.S. Insurance Industry Common Equity Risk Factors

Equity investors must consider various risk factors that could impact their investment portfolio before investing in a particular stock, so as to maximize risk/return profile. These factors include liquidity, leverage and volatility:

Liquidity: For insurers' year-end 2012 common stock holdings, the market value weighted average transaction volume (average daily shares traded divided by total shares outstanding) was 0.58%, which was higher than the combined New York Stock Exchange (NYSE) and National Association of Securities Dealers Automated Quotations' (NASDAQ) liquidity of 0.41%, according to Securities Industry and Financial Markets Association (SIFMA) data using average daily dollar traded volume divided by total market capitalization of listed stocks.

Current Ratio*:* For 2012, the current ratio for the insurance industry's common stock holdings was 1.23X. A ratio greater than 1X is favorable, indicating current assets are greater than current liabilities. This also means that the company has the ability to pay off short-term debt and liabilities in full.

Credit Rating of Senior Unsecured Debt*:* For the U.S. insurance industry's common stock holdings, 76.2% of their corresponding senior unsecured debt was rated investment grade as of year-end 2012. S&P assigned investment grade credit ratings to 77% of the S&P 500 companies, and speculative grade ratings to 11% as of year-end 2012 (the remaining were not rated by S&P). In market capitalization terms, investment grade companies represented 87% of the S&P 500's market capitalization, as per the latest available S&P 500 Credit Profile report with market capitalization breakdowns, dated as of Jan. 31, 2012. If ETFs, other funds, and non-rated issuers of stock were excluded from our calculations, 94.4% of the unaffiliated common stock exposure would have been issued by investment grade entities.

Table 10 shows the credit ratings of the senior unsecured bonds issued by companies for which insurers held common stock as of year-end 2012. If ETFs, other funds and non-rated issuers of stock were excluded from the total, 72.6% of insurer common stock holdings were in companies who issued long-term senior unsecured debt that is rated A- or higher (or NAIC 1 designation).

Table 10: YE 2012 Credit Ratings of Issuers of Unaffiliated Common Stock

BACV (In US$ Billions)		Rating	%
$	7.3	AAA	3.4%
$	19.8	AA+/AA/AA-	9.3%
$	97.5	A+/A/A-	45.8%
$	37.5	BBB+/BBB/BBB-	17.6%
$	6.0	BB+/BB/BB-	2.8%
$	3.2	B+/B/B-	1.5%
$	0.3	CCC+ and below	0.1%
$	7.3	ETFs and Other Funds	3.4%
$	33.9	Non-Rated Issuers of Stock	16.0%
$	**212.8**		**100.0%**

Table 11: NAIC Designation Equivalents of Issuers of Unaffiliated Common Stock

NAIC Designation	2012 Year End BACV (In US$ Billions)		%
1	$	124.7	58.6%
2	$	37.5	17.6%
3	$	6.0	2.8%
4	$	3.2	1.5%
5	$	0.3	0.1%
6	$	0.0	0.0%
ETFs, Other Funds and Non-Rated Issuers of Stock	$	41.3	19.4%
	$	**212.8**	**100.0%**

Debt to Equity Ratios*:* As of year-end 2012, the S&P 500's total debt to equity ratio was 1.4X, higher than the insurance industry's common stock investments' debt to equity ratio of 1.15X. This indicates that the insurance industry is investing in the equity of companies that are less leveraged than the market.

BETA*:* The two-year weighted beta for the insurance industry's common stock holdings is 0.992 as of year-end 2012. This is essentially the same risk as the market or the S&P 500 Index (whose beta is assumed to be 1.00). That is to say, if the market (as measured by the S&P 500) increases by 1% in value, so will the value of the insurer's unaffiliated common stock holdings. With respect to the five major insurer types' common stock holdings, the beta remains in a relatively tight range around the market beta of 1.00, as seen in Table 12.

Table 12: BETA by Insurer Type							
	P/C	Life	Health	Fraternal	Title	Industry	Market
BETA	0.986	1.020	1.040	1.060	0.902	0.992	1.000

Common Stock Industry Breakdown

Table 13 shows no significant deviation of insurers' common stock sector breakdowns from the S&P 500's breakdown as of year-end 2012, except for the financial and technology sectors. With respect to the insurance industry, the consumer non-cyclical sector is the largest, at 24.5% of the total, followed by financials, at 21.7%. Consumer non-cyclical industries include agriculture, food and beverages, biotechnology, healthcare products and services, pharmaceuticals, cosmetic/personal care, household products and commercial services. Insurers held 11.7% of unaffiliated common stocks in technology in 2012, versus 19% for the S&P 500. The underweight in technology is comforting, given the riskier and more volatile nature of the sector. Conversely, insurers held 21.7% of their common stock in the financial sector, while the S&P 500 contained 15.6%. Typically, financials are considered relatively stable, except during the financial crisis, and generally have higher credit ratings and are more liquid.

Table 13: Unaffiliated Common Stock Sector Breakdowns

Book Adjusted Carrying Value (In US$ billions)		2012 BACV	% of Total	S&P 500 %
Basic Materials	$	8.6	4.0%	3.6%
Communications	$	12.4	5.8%	3.1%
Consumer, Cyclical	$	12.7	6.0%	11.6%
Consumer, Non-cyclical	$	52.1	24.5%	22.6%
Diversified	$	0.2	0.1%	0.0%
Energy	$	18.4	8.6%	11.0%
Financial	$	46.1	21.7%	15.6%
Industrial	$	15.0	7.0%	10.1%
Technology	$	24.9	11.7%	19.0%
Utilities	$	3.0	1.4%	3.4%
N/A	$	19.5	9.2%	0.0%
Total	**$**	**212.8**	**100.0%**	**100.0%**

Year-end 2012 U.S. Insurance Industry Preferred Stock Holdings

As of year-end 2012, insurers owned $21.2 billion of preferred stock, 89% of which was unaffiliated (see Table 14). Unaffiliated preferred stocks totaled $18.9 billion and represented 0.4% of cash and invested assets at year-end 2012. Over the past 10 years, unaffiliated preferred stock holdings peaked in 2007 at $81.2 billion in BACV terms, or 1.7% of total cash and invested assets. In 2003, preferred stocks totaled $45.8 billion, twice as much as in 2012, with unaffiliated at $32.3 billion. Before 2009, hybrid bonds were reported in the annual financial statements as preferred stock; they are currently reported as debt. As of year-end 2012, the insurance industry owned $20.8 billion of hybrid bonds.

Table 14: Preferred Stock Holdings by Insurer Type

Book Adjusted Carrying Value (In US$ billions)	P/C	Life	Health	Fraternal	Title	Industry Total
Affiliated	$ 1.1	$ 1.1	$ 0.1	$ -	$ 0.1	$ 2.3
Unaffiliated	$ 11.0	$ 6.8	$ 0.4	$ 0.5	$ 0.2	$ 18.9
Total	**$ 12.1**	**$ 7.8**	**$ 0.4**	**$ 0.5**	**$ 0.3**	**$ 21.2**
% of Industry	57.2%	37.0%	2.1%	2.5%	1.3%	100.0%
Affiliated	9.4%	13.7%	16.1%	0.0%	18.9%	11.0%
Unaffiliated	90.6%	86.3%	83.9%	100.0%	81.1%	89.0%
Unaffiliated as a % of C&IA	0.7%	0.2%	0.2%	0.5%	2.7%	0.4%

Table 15 shows that, for unaffiliated preferred stock holdings, perpetual maturity preferred stocks represented 85.2% of the total while fixed maturities were 14.8%. Life and fraternal insurers held relatively more fixed maturity preferred stock than the rest of the industry, at 29.6% and 33.9%, respectively.

Table 15: Unaffiliated Preferred Stock by Insurer and Maturity Type

In US$ Billions	P/C	Life	Health	Fraternal	Title	Industry Total
Fixed Maturity	$ 0.5	$ 2.0	$ 0.1	$ 0.2	$ 0.0	$ 2.8
Perpetual	$ 10.5	$ 4.8	$ 0.3	$ 0.3	$ 0.2	$ 16.1
Total	**$ 11.0**	**$ 6.8**	**$ 0.4**	**$ 0.5**	**$ 0.2**	**$ 18.9**
% of Industry	58.3%	35.8%	1.9%	2.8%	1.2%	100.0%
Fixed Maturity	5.0%	29.6%	16.8%	33.9%	0.2%	14.8%
Perpetual	95.0%	70.4%	83.2%	66.1%	99.8%	85.2%

Conclusion

As of year-end 2012, insurance companies invested 11.4% of cash and invested assets (or $610.8 billion) in common and preferred stock, which, for the most part, has been unchanged since 2003. P/C companies are responsible for the majority of the exposure, holding 69% of total common stock and 80% of total unaffiliated common stock for the insurance industry. Insurers have increased their acquisitions of common stocks in recent years, which, in turn, have increased their unaffiliated common stock exposure as a percentage of cash and invested assets to 4.5% as of year-end 2012, closer to the past 10 years' average of 4.4% after reaching lows during the financial crisis of 2008. In addition, insurers held 76% of their unaffiliated common stocks in large cap companies (i.e., those with market caps of greater than $10 billion), as these are generally high-quality, more liquid, dividend paying, investment grade rated and less risky companies. This is reflected in the higher dividend yields and lower P/E ratio of insurers' unaffiliated common stock holdings when compared to the S&P 500 Index.

Stock investments represent attractive opportunities for insurers, particularly in the current low interest-rate environment as they are increasingly interested in seeking higher yielding alternatives to bonds. Equities generally offer higher long-term returns, dividend yields that are currently higher than the 10-year Treasury bond yield, better liquidity, a hedge against inflation, portfolio diversification and tax efficiency.

The Capital Markets Bureau will continue to monitor events in the equities market and report as deemed appropriate.

Appendix

Definition of Common Stock and Preferred Stock

Common Stock

Common stock represents a claim on a corporation's assets and earnings. Investors in stocks (common or preferred shares) effectively become an owner in the company, whether public or private.The method by which shareholders receive earnings is through cash dividends that are paid on a quarterly, semiannual or annual basis. As a company owner, an investor has limited liability — meaning that, if the company enters into bankruptcy, the maximum loss a stock investor can incur is the initial investment in the shares of the company; claimants (such as the company's debt holders) have no claims to the stock owner's personal assets or the institutional investors' assets. In terms of seniority, the common stock holder would be the last in line to receive any proceeds in the event of a company's liquidation. Furthermore, common stock dividends are not certain. When a company's earnings decline or are negative, the company may reduce or eliminate dividends to common shareholders, but it will continue to pay bondholders as contractual claims, and it may continue to pay preferred shareholders if able. Common stock shareholders are typically entitled to one vote per share; they vote on routine matters, such as the election of board members, declaration of dividends or selection of a new auditor, as well as on special events, such as mergers. The dividends common stockholders can receive are unlimited and can grow as the company's earnings grow, if declared by the company's board of directors.

Preferred Stock

Preferred stock is a class of ownership in a corporation that has a higher claim on assets and earnings than common stock. Preferred stock generally has a fixed dividend that must be paid out before dividends to common stockholders, and the shares usually do not have voting rights. However, some preferred shareholders might gain voting rights if the dividends are in arrears for a certain time. Although preferred stock has some characteristics similar to bonds and are at times viewed as fixed income, preferred shareholders do not have a contractual claim and cannot declare a default. There is also less upside for owning preferred stock compared to common stock: preferred stock dividends are fixed, as opposed to unlimited for common stockholders. In addition, in the event of a company's liquidation, preferred stockholders would receive any remaining proceeds only after payment to bondholders and other company creditors.

Valuation Methods

Common stock market valuation ratios include:

- **Price to Earnings (P/E) Ratio**: This is the ratio of price per share to earnings per share. In general, high P/E stocks are usually higher earning, growth companies. They may also be cyclical companies at the bottom of a cycle where earnings are low but are expected to improve as the economic up-cycle starts. P/E is static in time, and it does not objectively consider future earning streams. P/E ratios cannot be negative, as, for example, a $10 stock price divided by a $1.00 loss is a negative 10 P/E ratio.
- **Enterprise Value to Earnings before Interest, Taxes, Depreciation and Amortization (EV/EBITDA) Ratio**: This is the ratio of enterprise value (EV) to earnings before interest, taxes, depreciation and amortization (EBITDA) charges, where depreciation and amortization are non-cash costs. This is basically a ratio of debt plus equity to the cash flow generated by the business to which debt and equity holders have a claim.

- **Price to Sales (P/S) Ratio**: This is the ratio of price per share to sales per share of the company. This is sometimes used for companies that have no earnings and are at the bottom of an economic cycle, where the P/E ratio cannot be used.
- **Price to Book Value (P/BV) Ratio**: This is the price per book value (or net worth) of the company.

Some of the ratios are more useful in certain industries than others. For example, the P/BV ratio is commonly used for banks, because capital or book value is easier to compare across different banks, and eliminates distortions caused by varying leverage/debt levels. A bank stock can look cheap on a P/E basis, but is generally more risky due to its greater percentage of earnings from higher leverage or debt. The EV/EBITDA ratio is commonly used for cable/satellite companies. EV is the company's debt plus equity, while EBITDA is essentially cash flow generated; so, the EV/EBITDA ratio measures the amount of cash flow the company can generate using its debt and capital. Cable/satellite companies typically have large upfront capital expenditures to build infrastructure, thereby creating large non-cash depreciation and amortization charges that result in lower net income earnings; therefore, a P/E ratio would not be an appropriate measure for these types of companies. The value of a stock might also be estimated by multiplying its average historical ratio by the estimated future results, such as earnings, EBITDA, sales or book value.

Risks of Investing in Equities

Common equity risk factors include:

- **Liquidity**:Thisis calculated by dividing the average daily trading volume for the common stock by the total common shares outstanding. This formula is one way to assess stock liquidity. Note that liquidity is often not just "calculated" via a mathematical formula; it is influenced by many factors, such as bid/ask spreads, the number of stockholders, dollar size of the outstanding market, etc. For more detail, please see the Capital Markets Bureau's previously published special report titled, "U.S. Insurance Company Asset Liquidity," dated March 6, 2013.
- **BETA**: This is a measure of the volatility of a security or a portfolio in comparison to the market as a whole (for example, in comparison to the S&P 500). Beta is calculated using regression analysis. A beta of one indicates that the security's price will move with the market. A beta of less than one means that the security's price is less volatile than the market; a beta of more than one indicates that the security's price is more volatile than the market.

The following three risk factors are debt-related risk measures, but equity investors also consider them in their valuation; for example, higher debt companies typically have a lower average P/E multiple.

- **Debt/Equity Ratio**: This is also known as default risk, gearing or leverage. Debt includes short-term and long-term debt, and equity consists of share capital and retained earnings.
- **Current Ratio**: This is a liquidity ratio that measures a company's ability to pay short-term obligations. A ratio of less than one could mean the company will be unable to pay off its obligations if they come due immediately. The formula = (Current Assets)/(Current Liabilities).
- **Credit Rating of Senior Unsecured Debt**: Typically, the higher a company's long-term senior unsecured debt rating, the less likely the firm is expected to default on its debt obligations. Long-term debt that is rated BBB- or Baa3 and higher by Standard & Poor's and Moody's Investors Service, respectively, are considered investment grade. NAIC 1 and NAIC 2 designations effectively map to investment grade ratings.

August 2, 2013								
Major Insurer Share Prices			**Change %**			**Prior**		
		Close	**Week**	**QTD**	**YTD**	**Week**	**Quarter**	**Year**
Life	Aflac	$62.26	1.9	7.1	17.7	$61.09	$58.12	$52.89
	Ameriprise	91.21	3.4	12.8	46.1	88.18	80.88	62.45
	Genworth	13.29	0.2	16.5	77.4	13.27	11.41	7.49
	Lincoln	44.24	6.5	21.3	71.7	41.55	36.47	25.77
	MetLife	50.80	3.8	11.0	55.1	48.93	45.76	32.76
	Principal	44.37	3.2	18.5	56.3	42.99	37.45	28.38
	Protective	44.51	2.5	15.9	56.3	43.42	38.41	28.47
	Prudential	82.41	4.1	12.8	55.2	79.16	73.03	53.09
	UNUM	32.54	3.0	10.8	57.0	31.58	29.37	20.73
PC	ACE	$91.95	(0.4)	2.8	15.7	$92.33	$89.48	$79.50
	Axis Capital	43.45	(5.1)	(5.1)	26.1	45.77	45.78	34.46
	Allstate	52.15	1.2	8.4	30.2	51.52	48.12	40.05
	Arch Capital	54.34	(0.4)	5.7	24.0	54.55	51.41	43.82
	Cincinnati	49.74	1.3	8.3	27.7	49.12	45.92	38.95
	Chubb	87.07	(0.2)	2.9	16.1	87.23	84.65	75.01
	Everest Re	135.29	2.8	5.5	23.4	131.61	128.26	109.67
	Progressive	26.20	0.8	3.1	24.7	26.00	25.42	21.01
	Travelers	84.00	0.5	5.1	17.4	83.60	79.92	71.53
	WR Berkley	43.16	1.0	5.6	14.8	42.75	40.86	37.59
	XL	31.95	(0.8)	5.4	28.1	32.22	30.32	24.94
Other	AON	$69.08	2.3	7.4	24.7	$67.53	$64.35	$55.41
	AIG	48.33	3.8	8.1	37.0	46.54	44.70	35.28
	Assurant	54.83	3.3	7.7	59.0	53.09	50.91	34.48
	Fidelity National	25.14	1.5	5.6	6.6	24.77	23.81	23.58
	Hartford	32.03	2.1	3.6	43.1	31.36	30.92	22.39
	Marsh	42.49	1.2	6.4	23.9	41.99	39.92	34.30
Health	Aetna	$63.56	(1.8)	0.0	37.7	$64.70	$63.54	$46.17
	Cigna	77.30	(0.3)	6.6	45.1	77.57	72.49	53.29
	Humana	89.89	0.2	6.5	31.4	89.74	84.38	68.43
	United	72.26	0.1	10.4	33.5	72.21	65.48	54.12
	WellPoint	86.08	1.5	5.2	41.7	84.79	81.84	60.73
Monoline	Assured	$22.41	(0.9)	1.6	58.7	$22.61	$22.06	$14.12
	MBIA	13.97	3.8	5.0	76.4	13.46	13.31	7.92
	MGIC	8.04	7.2	32.5	197.8	7.50	6.07	2.70
	Radian	14.59	4.4	25.6	137.2	13.98	11.62	6.15
	XL Capital	31.95	(0.8)	5.4	28.1	32.22	30.32	24.94

August 2, 2013							
Major Market Variables		**Change %**			**Prior**		
	Close	**Week**	**QTD**	**YTD**	**Week**	**Quarter**	**Year**
Dow Jones Ind	15,658.36	0.6	5.0	19.5	15,558.83	14,909.60	13,099.80
S&P 500	1,709.67	1.1	6.4	20.2	1,691.65	1,606.28	1,422.10
S&P Financial	280.43	0.8	7.0	26.8	278.07	262.06	221.17
S&P Insurance	264.44	1.6	7.2	32.4	260.18	246.78	199.67
US Dollar $		**Change %**			**Prior**		
/ Euro	$1.33	0.0	2.0	0.6	$1.33	$1.30	$1.32
/ Crude Oil bbl	106.71	1.9	10.5	16.5	104.70	96.53	91.62
/ Gold oz	1,310.60	(0.8)	6.3	(21.7)	1,321.50	1,233.50	1,673.70
Treasury Ylds %	**%**	**Change bp**			**%**	**%**	**%**
1 Year	0.11	(0.01)	(0.04)	(0.04)	0.11	0.15	0.14
10 Year	2.60	0.04	0.11	0.84	2.56	2.49	1.76
30 Year	3.69	0.07	0.19	0.74	3.62	3.50	2.95
Corp Credit Spreads -bp		**Change %**			**Prior**		
CDX.IG	32.64	(0.8)	(18.5)	(42.8)	32.90	40.05	57.04

August 2, 2013 Major Insurer Bond Yields				Weekly Change					YTD
				Price			Spread over UST		Spread
	Company	Coupon	Maturity	Current	Change	Yield	B.P.	Change	Change
Life	Aflac	8.500%	5/15/2019	$130.24	$0.13	2.79%	114	(3)	(13)
	Ameriprise	5.300%	3/15/2020	$114.84	($0.13)	2.82%	89	(1)	(29)
	Genworth	6.515%	5/15/2018	$113.39	($0.53)	3.46%	213	13	(177)
	Lincoln National	8.750%	7/15/2019	$130.31	$0.01	3.09%	141	(2)	(43)
	MassMutual	8.875%	6/15/2039	$147.44	($0.89)	5.43%	189	(1)	(59)
	MetLife	4.750%	2/15/2021	$110.15	$0.17	3.22%	106	(3)	(2)
	New York Life	6.750%	11/15/2039	$123.82	($1.86)	5.09%	155	6	(8)
	Northwestern Mutual	6.063%	3/15/2040	$115.03	($0.88)	5.03%	145	(1)	0
	Pacific Life	9.250%	6/15/2039	$135.65	($3.81)	6.41%	286	17	(45)
	Principal	6.050%	10/15/2036	$116.71	$0.07	4.84%	142	(9)	(40)
	Prudential	4.500%	11/15/2020	$108.23	$0.11	3.22%	112	(3)	(29)
	TIAA	6.850%	12/15/2039	$123.29	($1.42)	5.21%	166	2	(4)
P&C	ACE INA	5.900%	6/15/2019	$119.62	($0.03)	2.30%	62	(2)	(15)
	Allstate	7.450%	5/15/2019	$126.96	($0.09)	2.42%	73	0	(38)
	American Financial	9.875%	6/15/2019	$131.00	($0.10)	3.90%	216	(2)	(96)
	Berkshire Hathaway	5.400%	5/15/2018	$116.26	($0.01)	1.83%	52	(0)	(11)
	Travelers	3.900%	11/15/2020	$106.99	($0.33)	2.82%	71	4	6
	XL Group	6.250%	5/15/2027	$112.17	($0.96)	5.01%	213	10	(29)
Other	AON	5.000%	9/15/2020	$110.10	$0.15	3.40%	131	(3)	(1)
	AIG	5.850%	1/15/2018	$114.37	$0.37	2.42%	125	(8)	5
	Hartford	5.500%	3/15/2020	$112.92	($0.06)	3.32%	135	(3)	(38)
	Marsh	9.250%	4/15/2019	$130.99	($0.22)	3.24%	156	2	(41)
	Nationwide	9.375%	8/15/2039	$138.69	($2.36)	6.32%	279	11	(42)
Health	Aetna	3.950%	9/15/2020	$104.59	($0.36)	3.22%	115	3	(4)
	CIGNA	5.125%	6/15/2020	$110.80	($0.20)	3.35%	132	2	(12)
	United Healthcare	3.875%	10/15/2020	$105.22	$0.06	3.06%	102	0	6
	Wellpoint	4.350%	8/15/2020	$107.20	$0.22	3.20%	116	(4)	(22)

Questions and comments are always welcome. Please contact the Capital Markets Bureau at **CapitalMarkets@naic.org**.