



2008 Property-Casualty Insurance Market: Opportunities & Competitive Challenges For Independent Insurance Agents & Brokers

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[See the "About the Data" explanation in Section VI. for information about how this data is compiled.]

Table of Contents

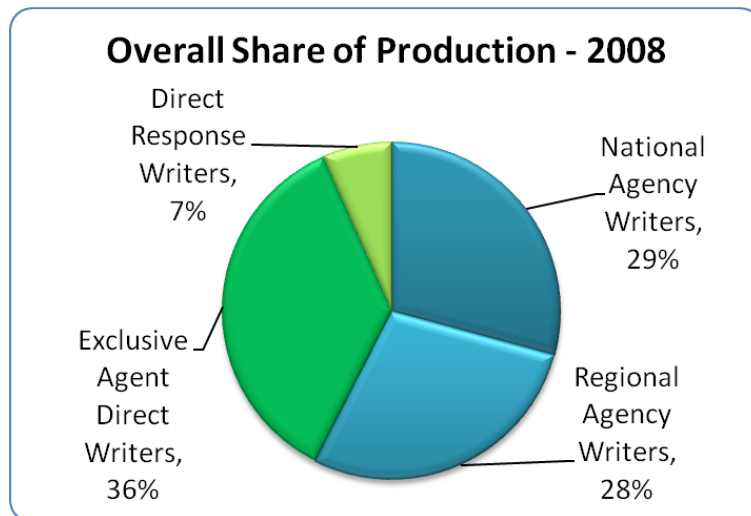
I. Market Conditions 2
II. Commercial Lines 4
Largest Gains 6
State by State Market Share Results 8
III. Personal Lines 10
Largest Gains 12
State by State Market Share Results 14
Private Passenger Automobile 16
Homeowners 20
IV. Company Expense Comparisons 23
2008 By-Company Private Passenger Auto Operating Ratios 24
V. Conclusions & Considerations 25
VI. About the Data 29

I. Market Conditions

Continued soft pricing and a very soft economy were the hallmarks of 2008 for the property-casualty insurance industry. With 2009 looking soft again, the industry may face small or flat premium growth for five years in a row. With the recession, demand declined for all sorts of insurance coverage—save for small gains in homeowners premiums.

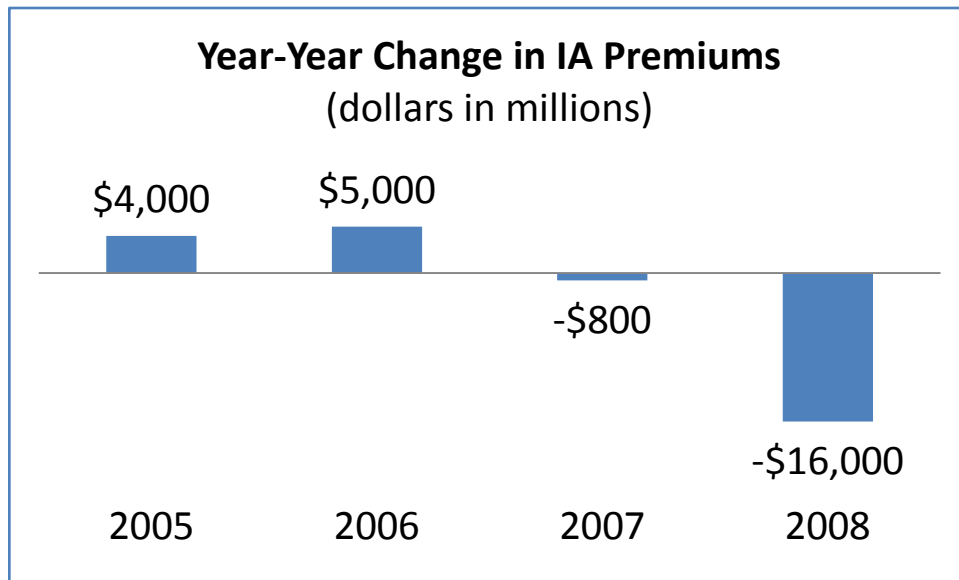
The overall property-casualty insurance market dropped about 3% in 2008, according to data provided to IIABA by A.M. Best Co. Total direct written premiums were \$474.5 billion, vs. \$490.0 billion in 2007.

The results from 2008 continue a streak of pricing weakness. The property-casualty market had been flat in 2007, and grew only about two percent in each of the two prior years. (Year-to-date results for 2009 indicate continuing weak pricing.)



Independent insurance agents and brokers (collectively “IAs”) produced \$272.7 billion of the total \$474.5 billion property-casualty market in 2008—meaning they generated about \$6 of every \$10 written in overall premiums. But the IA overall share of the total P&C premium pie slid by one percentage point, to 57%, in 2008. (IAs wrote \$288.8 billion of a total \$490.0 billion market in 2007.)

With the overall market shrinkage, regional and national independent agency companies together wound up writing \$16 billion less in P&C premium in 2008, on the heels of writing \$800 million less in 2007. IAs previously had gained \$5 billion and \$4 billion in 2006 and 2005, respectively.



It is important to note that even small percentage movements in market share can translate into hundreds of millions of premium dollars moving in or out of a particular distribution channel, or to or from a specific insurer.

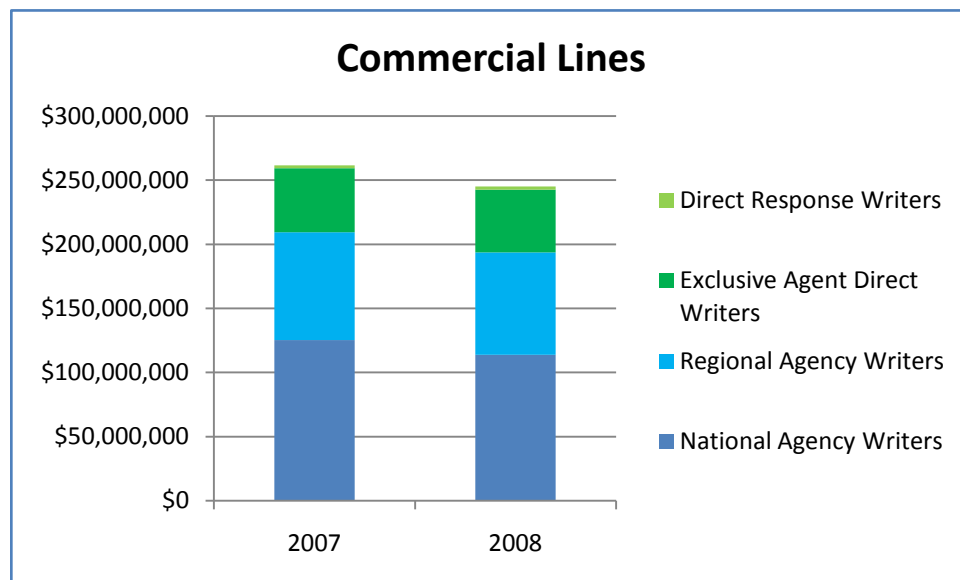
II. Commercial Lines

Mired in a soft market, the overall commercial lines property-casualty insurance market continued to decline in premium volume in 2008, dropping by 9.4% to \$245.0 billion. This was down from direct written premiums of \$261.4 billion in 2007 and \$261.6 billion in 2006.

In fact, the commercial market had been slowing for years, but growth was replaced by declining premiums in 2008. The slowing economy affected commercial lines writers in several ways:

- Lower payroll levels, along with the commensurate return of workers compensation premium.
- Smaller inventories and vehicle fleets.
- Reduced retailing, construction, manufacturing and transportation operations.

Independent agent and broker production declined by about 8% from 2007, while overall carriers' production decreased by only 1%, shifting market share away from independents slightly. Independents still dominate by writing nearly \$8 of every \$10 in commercial premiums. That equates to about \$194 billion in premiums in 2008, down from \$209.4 billion the prior year.

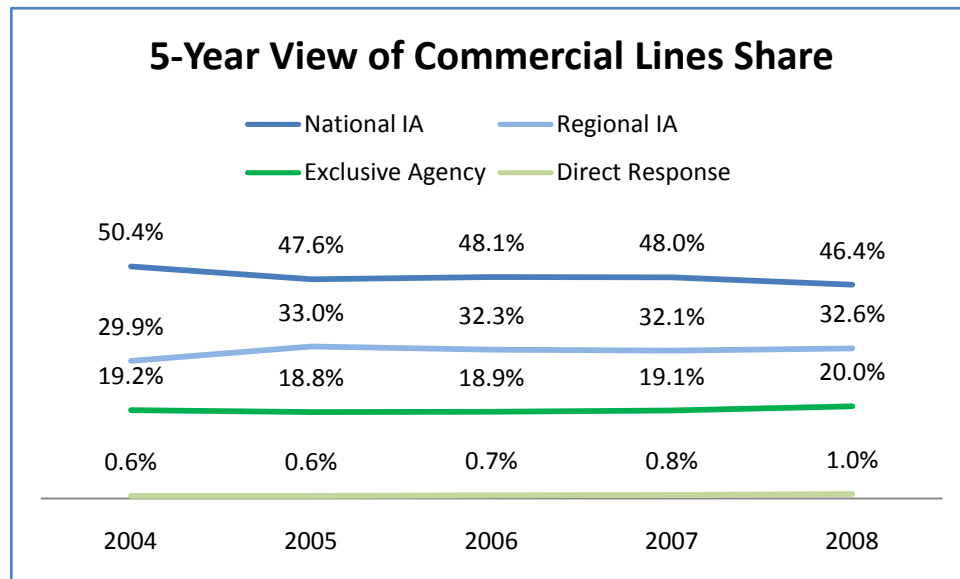


IAs had booked increased premium in each of the prior three years: \$5.5 billion in 2006, \$2.5 billion in 2005, and \$7.6 billion in 2004.

Shift to Regional IAs & Direct Writers

In 2008, regional IA carriers wrote \$79.9 billion in commercial business, down from \$84.0 billion in 2007. Their share of the overall market stood at 32.6% in 2008, up 1.5 points of share over 2007.

Meanwhile, national IA companies wrote \$113.7 billion in premium, down from \$125.4 billion in 2007. Their share of 2008 premium was 46.4%, down 1.6 points from the year prior.



Captive agency carriers also had a decrease in commercial premium (\$49.9 billion in 2008, down by \$850 million), but their market share of 20% of all commercial lines jumped by nearly a full percentage point over 2007 because they decreased more slowly than the independent agents.

Direct response was the only distribution channel that grew premiums in commercial lines, writing \$2.4 billion, up from \$2.2 billion in 2007. Its share of the overall commercial market increased by 18%, but from a tiny base of only about 1%.

Commercial Auto

In commercial automobile, the overall market dropped by 7% in 2008, to premiums of \$26.9 billion, following a decline of 4% the prior year.

Independent agents and brokers wrote 83.7% of commercial auto premium in 2008, down 0.6 points of share over 2007. Of that drop, however, national IA carriers were up by 0.5 points and regional IAs were down 1.6 points. Captive agency companies picked up about 4 points of share, but still only write about 16% of the commercial auto market.

Workers Comp

With the recession and soft market prevailing, the overall workers compensation market dropped by 13% in 2008, to \$44.5 billion, which followed a 4.5% drop the prior year. IA carriers wrote 81.6% of the comp market in 2008, down from 82.5% in 2007.

Largest Gains

These national and regional independent agency carriers experienced percentage growth in overall commercial lines market share in 2008¹ (among carriers with at least \$1 billion in direct premium written):

<u>Independent Agency Carrier</u>	<u>% Growth</u>
Westfield Group	17.2%
Bank of America Group	17.0%
Mortgage Guaranty	16.6%
Assurant Solutions	16.2%
Tokio Marine US Group	15.4%
HCC Insurance Group	12.6%
White Mountains Insurance	12.2%
Argo Group	11.8%
Hanover	11.7%
Allianz	11.5%
Great American	10.1%
Berkshire Hathaway (less GEICO)	8.7%
Erie Insurance Group	5.1%
Harleysville	3.8%
Chubb	3.8%
Selective	3.6%
Cincinnati	3.6%
Travelers	3.3%
Auto-Owners	2.0%
Liberty Mutual Agency Cos	1.6%
Hartford	1.4%
CNA	0.2%

The major independent agency carriers were essentially flat in commercial lines market share in 2008, including Liberty Mutual Agency Companies, Hartford, CNA, Swiss Reinsurance and Drive, while others dropped slightly, including Zurich, QBE Americas Group and W. R. Berkley. Largely due to shifts in how business was allocated, AIG (sans direct response) dropped in market share by 20% from 2007 to 2008.

¹ Note it is easier for carriers with smaller books in this line to show big percentage changes in market share because they are working from a smaller premium base.

Competitors

Major carrier competitors to the independent agent channel experienced the following percentage changes in their 2008 commercial lines market share:

<u>Captive Agency</u>	<u>% Growth</u>
Munich Re/American Mod	16.7%
Farmers (less Foremost)	9.2%
Liberty Mutual Direct Cos	8.7%
Allstate Direct Cos	8.3%
State Farm Group	7.6%
Nationwide Direct Cos	3.3%

The direct-response category gained 18% in their commercial lines market share, but these carriers start with a relatively small overall share. AIG Direct, the leader in direct-response commercial market share, was up by 20%, and USAA was up 16%.

State-by-State Market Share Results

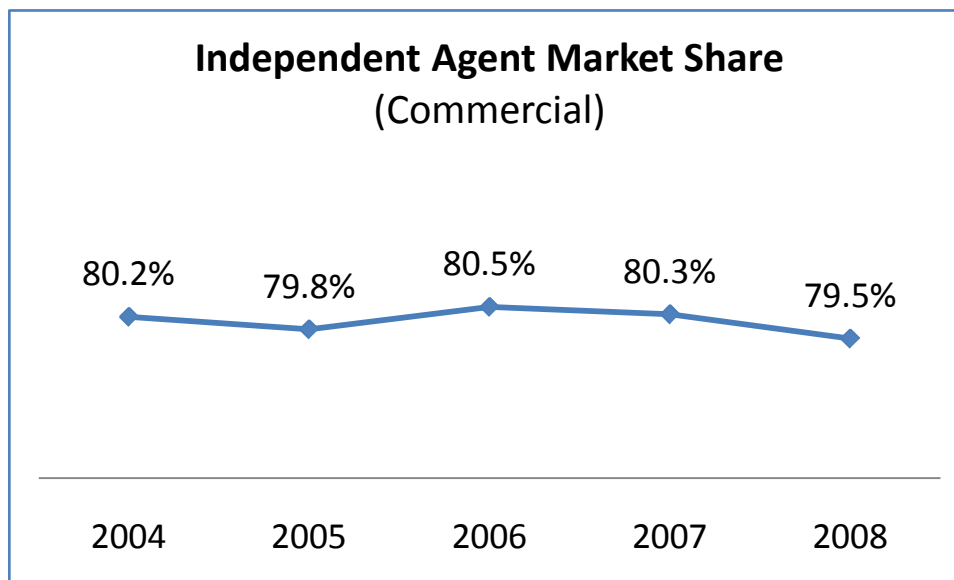
Around the U.S., and in most states, independent agents and brokers continue to dominate the commercial lines market and have generally retained their market share.

The IA channel commercial lines market share in all the states (plus the District of Columbia) broke down as follows over the last five years:

Number of States with IA Share by Range (Commercial Lines)					
Share	2004	2005	2006	2007	2008
Over 90%	1	0	0	0	0
85-90%	4	6	5	5	4
80-85%	16	15	19	18	15
75-80%	18	20	19	21	24
70-75%	5	4	2	4	3
65-70%	3	1	2	2	4
60-65%	3	5	4	1	1
55-60%	1	0	0	0	0

Average IA Share

The average independent agent market share around the states was 79.5% in 2008, down slightly over the last two periods but staying relatively consistent over time. Captive agency and direct response writers appear to have picked up the difference, increasing from 18.8% to 19.7% since 2006, as noted earlier, because their volumes decreased less than agent volumes.



Independent agents and brokers produced more than 85% of commercial lines in 2008 in each of four markets: Hawaii, Maine, Massachusetts, and West Virginia.

States with 5 largest gains/losses in IA commercial market share			
	<u>Gains</u>		<u>Losses</u>
Oregon	2.68	Wyoming	-2.95
Idaho	2.54	Oklahoma	-2.34
Dist. of Columbia	1.83	South Carolina	-2.17
Utah	1.61	Connecticut	-2.01
Minnesota	1.08	West Virginia	-1.96

III. Personal Lines

By late in 2008 and early 2009, the magnitude of rate decreases in most key commercial lines had begun to diminish, but remained in negative territory. On the other hand, personal lines (auto and home) were seeing small increases on individual policies (low to mid-single digits). Nevertheless, whatever modest gains the industry earned from higher rates were more than offset by economic weakness cutting into the demand for most types of insurance.

The weak economy is having a disproportionately large impact on commercial insurers, due to rising unemployment (slicing payrolls and eroding the exposure base for workers compensation premiums) and reduced construction, manufacturing, transportation and retailing activity. Conversely, in personal lines the market overall was essentially flat; direct written premiums ended 2008 at \$229.5 billion, up slightly from \$228.6 billion in 2009.

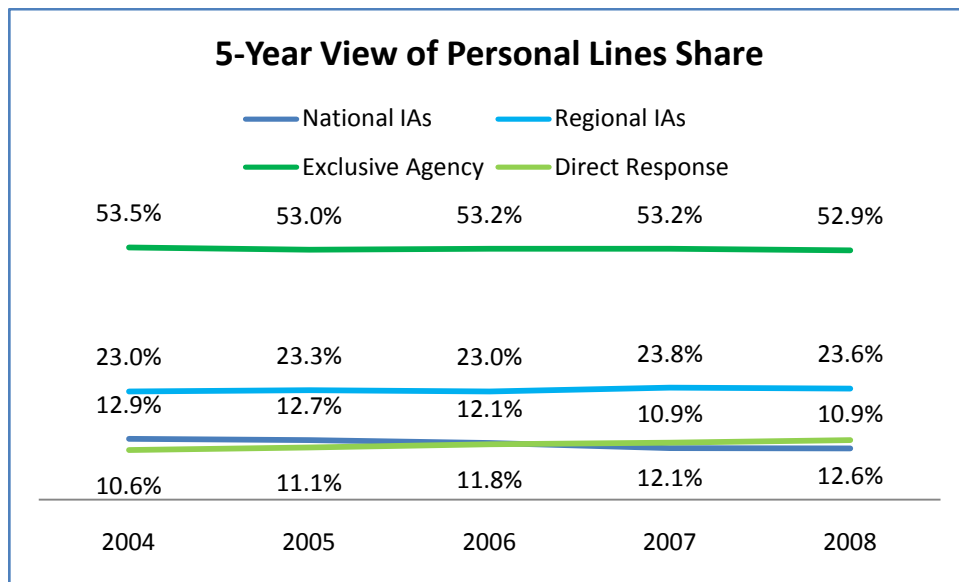
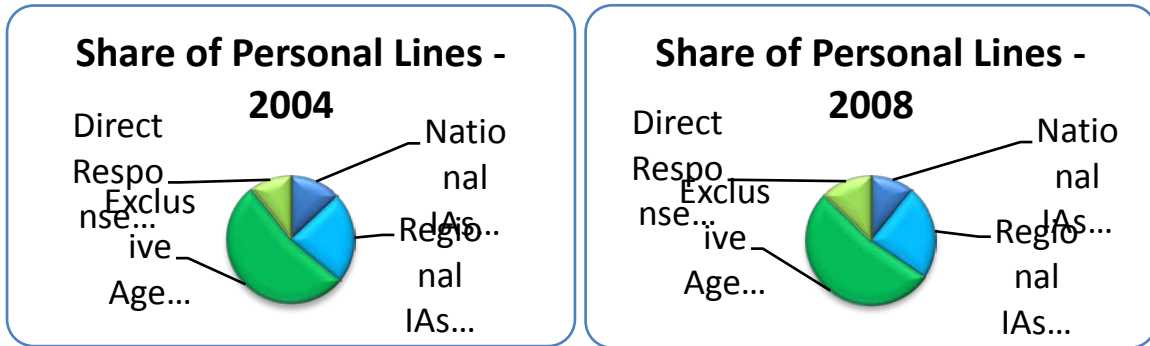
Regional IA carriers decreased only slightly, from \$54.3 billion to \$54.1 billion, or 23.6% of the market. National IA carriers were flat at \$25.0 billion, or 10.9% of the market.

Captive carriers continue to dominate the market with the majority of business, though they were also down slightly, to \$121.4 billion, or 52.9% of the personal lines market, from \$121.7 billion, or 53.2%, in 2007.

The real change was in direct response, which added \$1.4 billion of personal lines premium, to \$29.1 billion (12.6% of the market), up from \$27.7 billion. That's a 4.3% gain in share over 2007 for the direct channel.

**Five-Year Look:
Overall Personal Lines Market Share**

These small changes in direct premiums written become more apparent when viewed over five years. The charts below show a gain in direct response, with a loss by national agency writers. Other channels are unchanged in share.



As the chart above shows:

- Captive agent carriers continue to hold a consistent share of just over half the market.
- Direct-response writers continue to increase share, reaching a two percentage point increase over the last five years, adding about \$1.3 billion in direct premiums written during the flat year of 2008. The direct-response channel surpassed national IA companies in 2007 and added to the gap this year.
- Over the four-year period from 2005 to 2008, the IA channel has lost one-and-a-half points in share, which has gone to the direct-response writers.

Largest Gains

While many of the major national IA companies were down slightly in market share, the following national IA companies with premiums of at least \$100 million in personal lines realized percentage growth in their market share in 2008² over the prior year:

<u>National IA Carrier</u>	<u>% Growth</u>
Unitrin	8.2%
White Mountains	3.6%
Travelers	1.8%
Foremost	0.5%
Harleysville	0.5%
Allianz of America	0.1%

The following regional IA companies saw percentage growth in their personal lines market share in 2008² over the prior year:

<u>Regional IA Carrier</u>	<u>% Growth</u>
Central	10.6%
State Auto	4.2%
Donegal	3.4%
Enumclaw	3.1%
Liberty Mutual Agency Cos.	2.8%
Safeway	2.7%
Nationwide Agency Cos.	2.2%
Auto-Owners	1.9%
Pekin	1.7%
Erie	1.0%

On the flipside, the national and regional independent agency carriers below with more than \$100 million in personal lines premium each were down by 5% or more in market share in 2008²:

<u>National/Regional IA Carrier</u>	<u>% Growth</u>
Affirmative	-14.3%
Infinity	-13.2%
United Automobile	-11.7%
Safety	-8.6%
Bank of America Group	-8.1%
Mercury	-7.7%
GMAC	-7.5%
QBE Americas Group	-6.7%
Commerce	-6.3%
AIG (less direct-response)	-5.0%
Arbella	-5.0%

² Note it is easier for carriers with smaller books in this line to show big percentage changes in market share because they are working from a smaller premium base.

Competitors

The main carrier competitors to independent agents and brokers experienced the following percentage changes in personal lines market share in 2008 over the prior year:

<u>Major Direct-Response Competitors</u>	<u>% Growth</u>
AIG Direct	16.2%
GEICO	6.3%
Progressive Direct	5.5%
USAA	3.0%
Amica Mutual	-0.7%
21 st Century	-13.0%

AIG Direct's large increase and 21st Century's large decrease result from the former's acquisition of the latter. The other companies in the above list showed performance comparable to the previous year.

<u>Major Captive Agency Competitors</u>	<u>% Growth</u>
Ameriprise	16.9%
Wawanesa	2.7%
Safe Auto	2.7%
Liberty Mutual Direct	1.6%
Alfa Insurance	1.2%
Shelter	1.1%
Farmers (less Foremost)	0.7%
State Farm	0.1%
Nationwide Direct Cos.	-2.1%
American Family	-2.8%
Allstate	-3.7%

State-by-State Market Share Results

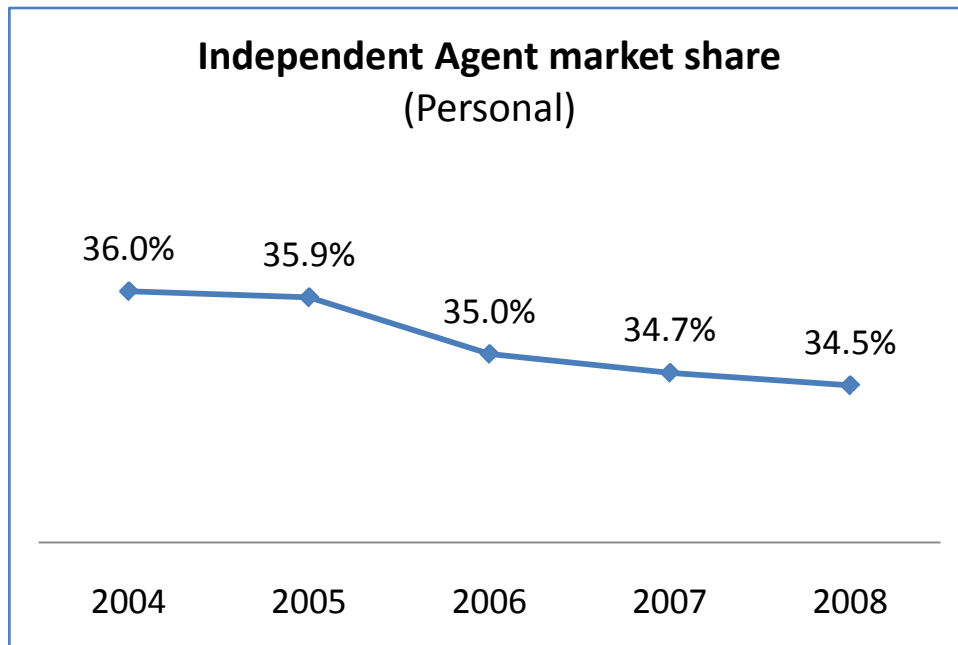
The personal lines market share held by independent agents and brokers varies widely by state, around a national average of 35%. The share in 2008 ranged from a low in Alaska (about 17%) to a commanding 83% in Massachusetts. In the latter state, the share has continued to drift down since 2006 as regulatory changes in the auto insurance market challenged independent agents and brokers with fresh competition.

The IA channel held relatively strong state market shares in 2008 around the rest of New England, traditionally an independent agent stronghold: Maine (56.2%, up from 55.6% in 2007), Vermont (51.4%, unchanged), Connecticut (50.0% vs. 50.7%), Rhode Island (46.4% vs. 47.4%) and New Hampshire (44.6%, unchanged).

In other relatively stronger states for market share in personal lines for independent agents and brokers, Ohio came in at 45.6%; South Dakota, 45.8%; and Pennsylvania, 45.4%.

The independent agency personal lines market share for all of the states (plus the District of Columbia) broke down this way for the last five years:

Number of States with IA Share by Range (Personal Lines)					
Share	2004	2005	2006	2007	2008
Over 50%	5	4	4	4	3
45-50%	4	6	3	4	5
40-45%	9	6	7	7	6
35-40%	4	6	5	4	6
30-35%	11	10	9	12	11
Under 30%	18	19	23	20	20



In personal lines, the national average independent agency system market share was 34.5% in 2008, showing a downward trend since 2004. As noted in IIABA's earlier market share reports, independent agents have an attractive opportunity in this huge consumer market:

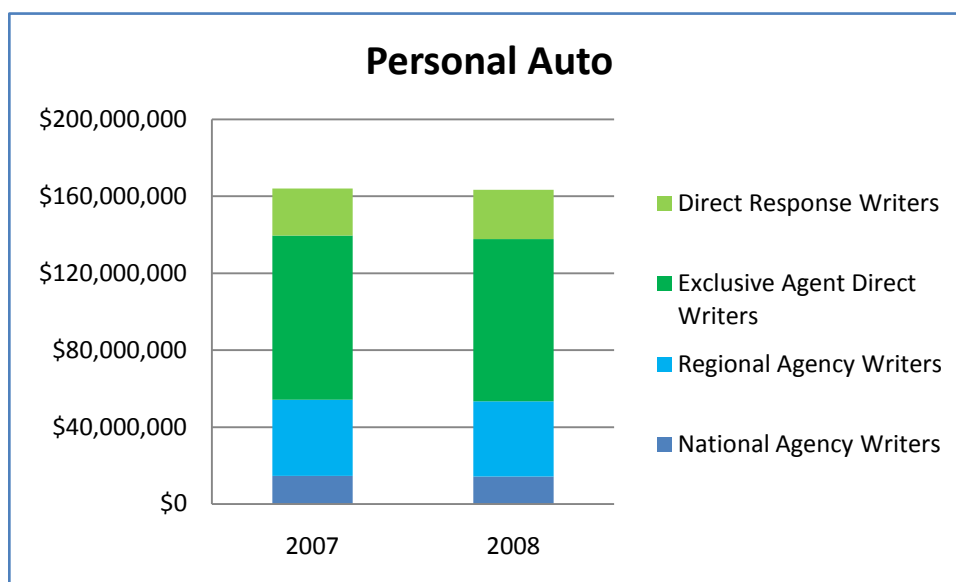
- In 22 states, independent agents and brokers were able to grow market share, even while the distribution channel's national average decreased slightly.
- While prices are soft, this \$229 billion market continues to expand.
- Many new independent agencies are being launched, according to IIABA's *2008 Agency Universe Study*, and many of these smaller firms are likely to be aggressively seeking personal lines.
- Particularly in the face of commercial lines weakness, many larger agencies are seeking growth through increased sales of personal lines.
- While it is difficult to compete with direct-response writers for advertising and marketing expenditures, many independent agents have been successful doing it by applying focus, customized service and sales power to personal lines. They are able to do this by using the latest efficient technologies such as Real Time, along with the Internet, email marketing and the Social Web, and Trusted Choice®, the national consumer brand for independent insurance agents and brokers. There is a lot of market share on the table (relative to commercial lines) that IAs can go after. Moreover, reduced commercial lines premiums are squeezing agents who rely heavily on that side of the business. IAs are seeking customers in all lines.

Private-Passenger Automobile

It's no wonder the airwaves, the mailbox and the Internet are teeming with messages on buying car insurance. The personal automobile insurance segment alone represented a premium opportunity equivalent to 71% of all personal lines and 34% of the *entire* property-casualty market in 2008.

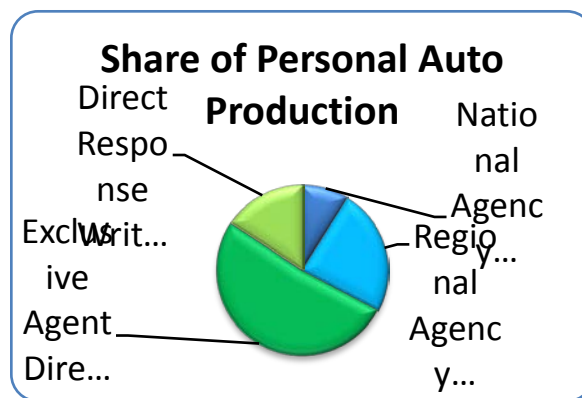
But carriers continued to battle a tough pricing environment in 2008. Premiums for car insurance overall were \$163.4 billion, down slightly from \$163.0 billion.

Regional and national IAs wrote less in premiums and also lost market share, as did captive agency companies. Even in this soft market, direct response actually added \$1.2 billion in premiums, and increased market share by a healthy 5.4%. This growth suggests a combination of factors: advertising for auto insurance continues to pay off as it has for decades; many consumers are very willing to purchase this coverage online; and there is the risk of an accelerating commoditization of this market.



In 2008, captive agency carriers still owned just more than half (51.6%) of the private passenger auto market, with premium of \$84.4 billion, losing 0.4 percentage points of market share from 2007.

Direct-response companies wrote \$25.6 billion, up by more than \$1.2 billion, or 5%, over 2007. With the regional independent

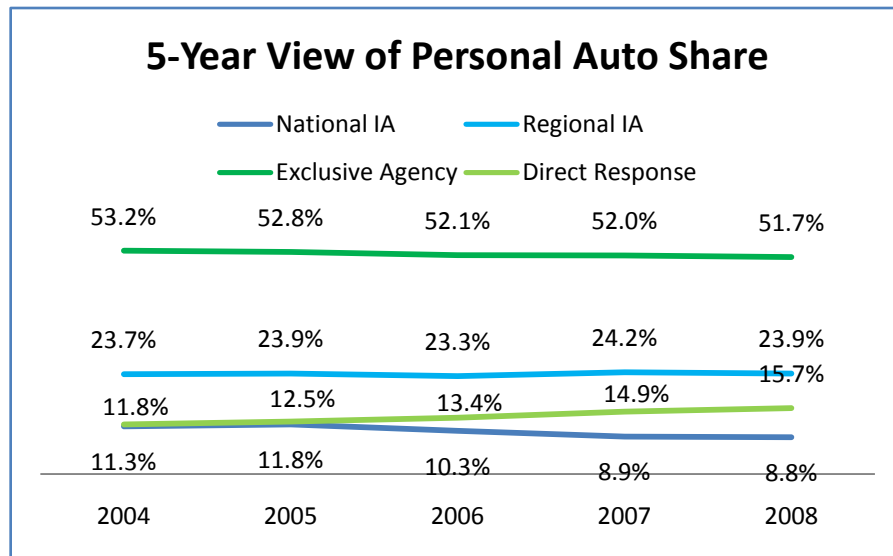


agency companies at \$39.1 billion in premium (a 23.9% share) and national IA companies at \$14.3 billion (8.8%), the IA channel lost a combined 0.4 percentage point of market share in 2008 vs. 2007.

Note that even small movements in share represent huge opportunities won or lost: each market share point in personal auto was the equivalent of \$1.6 billion in premium in 2008.

Five-Year Look: Personal Auto Market Share

Over the five years ending with 2008, this chart shows how captive agency carriers and regional IA companies have been fairly flat. During the same time, direct-response companies have displayed dramatic growth, adding about one third to their share. Their expansion has come at the expense of national IA and exclusive agency companies.



Some national and regional independent agency carriers, however, bucked the trend. Among those with at least \$500 million in direct premium written, companies showing at least a 1% gain in personal auto market share for 2008 vs. 2007 include³:

<u>National/Regional IA Carrier</u>	<u>% Growth</u>
Unitrin	10.4%
Nationwide Agency Cos.	10.1%
White Mountains	5.9%
State Auto	5.3%
Auto-Owners	4.1%
Shelter	2.1%
Erie	1.7%
Travelers	1.6%
Liberty Mutual Agency Cos.	1.3%
Alfa	1.2%

³Note it is easier for carriers with smaller books in this line to show big percentage changes in market share because they are working from a smaller premium base.

Competitors

Among the big direct-response players, GEICO added \$786 million in premium in 2008, booking a total \$12.5 billion for a total market share of 7.7% (an increase of about 7% in share over 2007). USAA grew by \$283 million to \$6.3 billion, giving it 3.8% of the market (up 5% from a year earlier). Progressive Direct grew by \$218 million, to \$3.9 billion in premium, a 2.4% share (up 6%).

Comparable percentage changes in market share in 2008 (over year-prior numbers) for the independent agents' major carrier competitors were as follows:

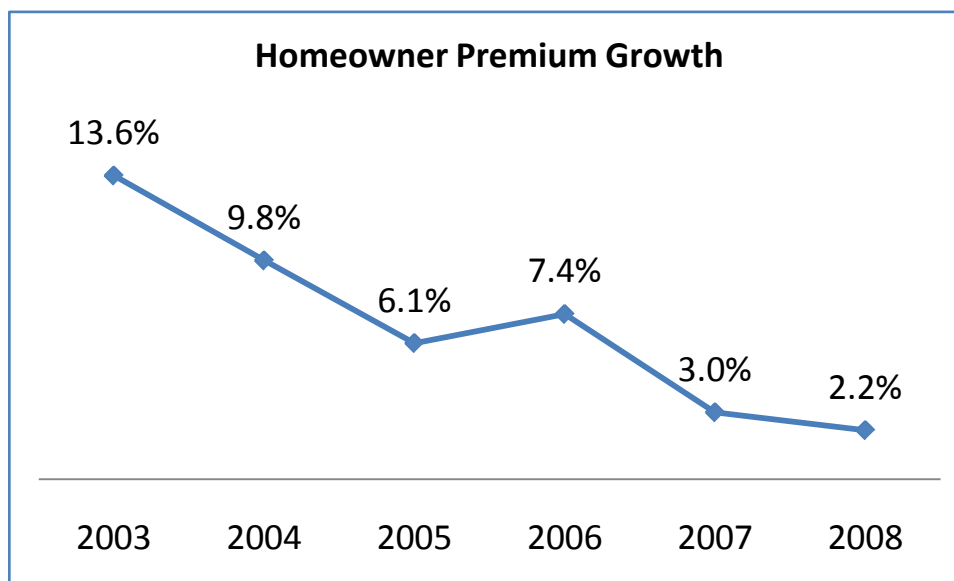
<u>Major Direct-Response Competitors</u>	<u>% Growth</u>
AIG Direct	15.5%
GEICO	7.1%
Progressive Direct	6.2%
USAA	5.1%
Amica Mutual	-0.6%
21 st Century	-12.4%

AIG Direct's large increase and 21st Century's large decrease result from the former's acquisition of the latter. The other companies in the above list showed performance comparable to the previous year.

<u>Major Captive Agency Competitors</u>	<u>% Growth</u>
Ameriprise	20.1%
Liberty Mutual Direct	1.1%
Farmers (less Foremost)	0.1%
State Farm	2.3%
Nationwide Direct Cos.	-4.1%
American Family	-3.0%
Allstate Direct	-3.3%

Homeowners

The homeowners market was the bright spot in premium growth for 2008, though the year continued a trend of slowing growth. The overall home insurance premium market grew to \$63.4 billion in 2008, up by 2% from \$62.0 billion the year prior.



In the case of homeowners insurance, independent agency carriers grew faster than the other channels:

- National independent agency carriers grew by 2.4% (to \$10.2 billion, or a 16.0% share), while regional IA companies increased by 3.1% (\$14.2 billion, or a 22.4% share).
- Combined, IAs wrote \$24.4 billion of the 2008 market, adding more than \$660 million of premium. Their share gained slightly to 38.6% from 38.3% in 2007

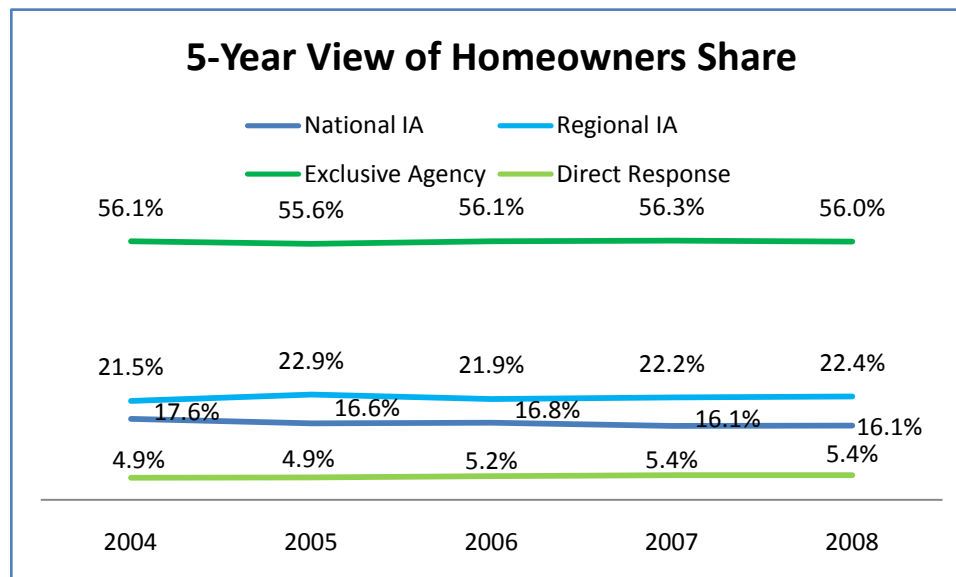
Captive agency writers grew by 1.7% in 2008 over 2007, slower than IA carriers, but they still command 56% of the market, or \$35.5 billion of premium.

The direct-response writers also grew more slowly than IA carriers, at 2.1%. With their main attention clearly focused on the personal auto segment, their market share of homeowners remained at 5.4%, or \$3.4 billion in premium.

Five-Year Look: Homeowners Market Share

This chart shows obviously that there has been relatively little movement in share of the homeowners market.

Direct response has grown somewhat, though much less quickly than in the auto market. National IA companies have slid slightly while regional IA companies have held their own.



Largest IA Gains in Homeowners

National and regional IA carriers (at least \$100 million in homeowners premium) showing the biggest percentage gains in homeowners market share for 2008 include⁴:

AIG (less direct response)	22.6%
Arbella	9.6%
Central	7.2%
Liberty Mutual Agency Cos.	6.8%
Commerce	3.5%
Assurant Solutions	2.3%
Republic	2.2%
Main Street America	1.7%

⁴Note it is easier for carriers with smaller books in this line to show big percentage changes in market share because they are working from a smaller premium base.

Competitors

The larger carrier competitors to IAs in the homeowners line saw these market share gains or losses:

Major Direct-Response Competitors

AIG Direct	18.0%
Amica Mutual	-1.1%
USAA	-1.8%

Major Captive Agent Competitors

Nationwide Direct Cos.	3.2%
Liberty Mutual Direct	2.4%
Farmers Group (less Foremost)	2.2%
State Farm	-2.3%
American Family	-2.9%
Allstate Direct	-4.8%

IV. Company Expense Comparisons

Beyond market share trends, each year we review the expenses incurred by each distribution system. For this comparison, we examine carrier operating ratios for private-passenger auto insurance, as that is the line of business in which all three distribution systems compete in a major way.

We consistently have found over the 14 years in which we have conducted this study that:

1. There are varying degrees of efficiency among companies within each distribution system; and
2. The overall expenses to provide insurance (operating ratios) for efficient carriers often come close to one another—no matter what the channel.

Net operating expense ratios⁵ can be used to compare efficiency across companies and distribution methods. Lower net operating expense ratios reflect more efficient operations.

⁵ Because of the discrepancies in how companies categorize their expenses, we have found that the only way to get a true “apples to apples” comparison is to use operating expense ratios. The operating expense ratio is the combination of the company’s underwriting expense ratio and loss adjustment expense ratio. The underwriting expense ratio includes the commissions/broker fees ratio, other acquisition expense ratio, general expense ratio, and the taxes, licenses and fees ratio.

2008 By-Company Private Passenger Auto Operating Expense Ratios

The following table shows a variety of expense ratios for some of the major carriers in each of the distribution systems. There are varying degrees of efficiency among companies within each channel. Furthermore, the operating ratios for efficient carriers often come close to one another, regardless of the channel.

	National IA	Regional IA	Captive	Direct response
USAA				20.94%
GEICO				28.56%
Affirmative		29.04%		
Auto-Owners		30.05%		
Southern Farm Bureau			30.18%	
Hartford	31.85%			
Progressive Direct				33.00%
Auto Club Enterprises			33.14%	
Progressive Drive (Agency)		34.04%		
Amica Mutual				34.91%
American Family			35.83%	
MetLife Agency Cos.		36.03%		
Main Street America		36.49%		
Liberty Mutual Direct Cos.			36.82%	
Erie		36.88%		
State Farm			37.29%	
Allstate Direct			37.32%	
Safety Group		37.73%		
Infinity		38.21%		
Permanent		38.76%		
GMAC		38.79%		
Commerce Group		38.85%		
State Auto		39.02%		
Cincinnati	39.22%			
Hanover	39.49%			
AIG (less direct response)	39.80%			
Chubb	39.82%			
Farmers (less Foremost)			39.84%	
Nationwide Direct Cos.			41.33%	
AIG Direct-Response				41.96%
Auto Club Group			42.56%	
California State Auto			46.72%	
21 st Century				47.11%

Several independent agency companies posted 2008 operating ratios that compare well against those of major captive agency carriers. In particular, the operating expense ratios of some regional independent agency carriers handily beat those of the largest captive agent writers—and were comparable to those of some large direct companies.

Note USAA's very low ratio above, as the firm enjoys an expense and marketing advantage. Leveraging a major affinity group and extensive word-of-mouth marketing, the firm generates business from military personnel without high advertising outlays.

V. Conclusions & Considerations

The worsening U.S. economy, which has yielded flat overall premium growth for a couple of years, turned negative in 2008. Commercial lines, the portion of the property & casualty market dominated by independent agents and brokers, led the way down with a 9% decline. Personal lines were flat, with both captive companies and independent agents and brokers losing share to direct response carriers, mainly in auto coverage. This report evaluates 2008 data—the most recent year available from A.M. Best Co.—but insurers likely dealt with similar, or worse, conditions in 2009.

There are winners and losers within any property-casualty insurance market—hard or soft—as this report illustrates. Opportunities abound for aggressive and smart firms in each of the three distribution channels.

This annual report consistently has presented data that demonstrates both threats and opportunities for independent agents and brokers. In some pockets around the U.S., independent agents and brokers truly dominate both commercial *and* personal lines. That proves the opportunity exists for IAs in other states to grow.

This year's report mainly covers year-end numbers for 2008 and compares them with recent trailing years.

Expense Differential

The A.M. Best data for 2008 demonstrate that efficient companies are leveraging each type of distribution system—a consistent finding in the 14 years of this market share analysis.

As the data show, well-managed independent agency writers can produce, distribute and service insurance products just as cost-effectively as captive agent writers and direct companies—and, in some cases, even more so.

Generally speaking, across the distribution platform, the obvious differential in expenses with the direct-response channel is savings on commissions, an advantage offset in part by the hefty advertising and marketing bills these firms pay in addition to whatever salary and incentive compensation they pay those in sales positions. Another expense benefit is a single workflow and technology—the same advantage enjoyed by captive agency writers.

However, we believe that workflow and technology advantage is narrowing—witness the thousands of independent agencies around the country increasing their use of policy download and real-time workflow tools. This adoption of a consistent, easier way of doing business is enabling IAs and their carriers to realize cost savings—and, along with other streamlining initiatives, meet or even beat the operating expense efficiency ratios of the large captive carriers.

Further improvements are expected as real-time and download interfaces are used for rating, inquiries and other transactions, which will enable agents to focus on value-added consultation to end users. IA carriers continue to report increased usage, lower expenses and improved business quality. Progress along current trends likely will continue to narrow the gap with captive agency writers and direct writers.

Success Stories

While the overall composition of market share across the major distribution channels remains fairly consistent over time, the averages conceal the success stories.

Many IIABA Best Practices firms continue to earn above-average growth, even while independent agents and brokers are still writing nearly 60% of all property-casualty insurance. Though direct writers are experiencing a high growth rate in mass-market personal lines coverage, especially auto, IAs continue to own competitive advantage in commercial lines coverage. Leveraging their advantages in flexibility, customization, judgment and range of options, they are able to grow coverages to keep pace with their commercial clients' needs in ways that captive and direct writers cannot. They also enjoy a greater ability to cross-sell and up-sell with far broader product sets.

Another significant evolutionary change is growth in start-up independent agencies, observed in the IIABA Future One *2008 Agency Universe Study*. As the report says, "New agencies are concentrated geographically: 33% in the South Atlantic states; 20% in the West South Central states; 11% in the Mountain region, and 10% each in the East North Central and West North Central States. The concentration in the South Atlantic (including Florida) and West South Central (including Louisiana and Texas) suggests that non-independent agency carriers withdrawing from coastal areas may have encouraged formation of new independent agencies." Many of these firms are headed up by younger principals, some of whom earned their selling-skills stripes at captive agencies.

Even as new agencies join the marketplace, older agency owners continue to work through the disposition of their firms as they retire. As has historically been common, some turn over their firms to succeeding generations, others to partners they have groomed. Some are selling their firms, in many cases leading to the growth of large, multi-unit agencies. Such agency sales can disrupt the personal relationships on which much of their business is built, and this likely has led to some of the observed market share losses. Perpetuation planning should be a priority for all agency owners.

Key Battleground

Direct response continues to expand its share of car insurance, now at 16%, and leaving that of national independent agency carriers well behind (now down to 9%). In 2008, while national and regional agency companies and captive writers saw their premiums written decline, direct writers actually *grew* premiums by more than \$1 billion.

The personal auto line represents a fiercely competitive arena, making up one-third of the entire property-casualty pie. Characterized by massive marketing budgets and

economies of scale (particularly seen in GEICO and Progressive), direct writers are successfully slicing off the least complex and most accessible mass-market volumes of the insurance business. Direct response writers also are enjoying success in homeowners as well, though at a less aggressive pace—for now.

Some independent agents and brokers dismiss the rise of direct response in the personal auto space. To some extent this makes sense, as auto has become highly price-competitive, with low switching costs and consequent low retention. There often appears to be little opportunity for the value-add that is the hallmark of the independent agent and broker. But IIABA has been sounding the warning for at least a decade: IAs relinquish or ignore this business at their peril. Many auto insurance purchasers are families with other, varied and opportunity-creating coverage needs such as homeowners, personal umbrellas and add-on coverages. Additionally, about 10% of consumers in the general market also own their own businesses, a potentially lucrative target for small commercial lines—an opportunity accessed by the in-depth needs assessment conducted by an independent agent. Soon, auto insurance may be viewed similarly to the way banks view checking accounts—a method to bring in desirable consumers, uncover their other needs and meet them with more customized (and profitable) product options. Agents who dismiss simple auto insurance may miss out on opportunities to have these important needs-assessment conversations.

It continues to be worth noting that the Independent Agency System still holds a full one-third of the private-passenger auto market. Even as direct response companies have aggressively added share, regional IA carriers have held their own. Independent agents who view personal lines as an important part of their business to be sought and protected will continue to earn incremental business and the benefits of cross-selling.

Strategies for Success

The Independent Agency System continues to prove itself as the value-added distribution anchor of the insurance industry, even in the current difficult economic environment. This decentralized, flexible and knowledgeable distribution network reaches every part of the U.S., providing an experienced, proven channel for carriers needing to access new markets or offer innovative products.

Of course, this does not mean that IAs can rely on the strengths of the Independent Agency System itself to compete successfully. Top-notch firms are hitting on *all* marketing, selling, processing and servicing cylinders—both among prospects and established customers—to grow and deepen policyholder relationships.

The strategies listed below may not surprise most agents—they are the foundations of high-performing agencies and have been validated for years. They include:

- ***Invest in people.*** Make necessary investments in younger generations of employees, and provide flexible and modern work schedules and environments, technology, and perpetuation plans.

- **Build capabilities.** Develop employee expertise as trusted advisors, knowledgeable about risk management, new products and particular industry sectors, as well as the stress businesses are feeling with the economy.
- **Rethink marketing strategies.** Reach out to an entirely new customer segment— younger generations and new families in need of the service and products available, delivered in a way that is appealing to the customer. Consider allocating more marketing dollars to agency Web sites, social media and other e-marketing approaches, such as online Yellow Pages over their print counterparts, and leveraging participation in Trusted Choice®. For example, agencies across the country report sales success with Facebook, LinkedIn and Twitter interactions.
- **Cross-sell.** Leverage property-casualty lines and cross-selling into product areas that build further trust, such as financial services, life insurance and employee benefits. These new lines are a valued path to proactively retain accounts; the more policies per customer, the greater the opportunity for robust, value-added service, and the higher the retention rate.
- **Sell with discipline.** Implement disciplined marketing and sales initiatives that build an ongoing pipeline of prospects.
- **Leverage new workflows.** Innovate with modern workflows and technologies (e.g., real-time communications, policy download, and a paperless work environment) to free up employee time to engage in value-added functions. (Many IAs are expected to encourage CSRs to change workflow behavior with the “21 Day Challenge” beginning in January 2010 by the industry’s Real Time Campaign; see www.getrealttime.org/21DC.)
- **Evaluate carrier partners.** Smart IAs develop strong relationships with regional and national carriers, and those carrier partners tend to be more responsive to their agency plant in implementing technology efficiencies like download and real-time technology.

Independent agents and brokers truly dominate the commercial insurance market, and are defending a strong position in the personal lines space. Given the competitive differentiators that independent agents and brokers bring—the variety of strong carriers that make it easy to do business, personal relationships and breadth of knowledge— along with improved access to technology and the confidence and customization communicated by the Trusted Choice® brand, they have the potential to enjoy robust growth in every state and every product line.

[Note: We invite your comments and questions about this report. Please contact Madelyn Flannagan, IIABA Vice President, Education and Research, at (703) 706-5409 or madelyn.flannagan@iiaba.net.]

VI. About the Data

This is the 14th year in which A.M. Best Co. has provided the Independent Insurance Agents & Brokers of America with year-end industry market share and company expense data for the association to provide an annual assessment of the state of the independent agency system. All data in this report comes from A.M. Best and is printed with its permission. The 2008 calendar-year figures represent the latest year in which segmented data is available from A.M. Best.

The A.M. Best data offers IIABA the most accurate picture of changes in property-casualty insurance distribution because it separates captive agency and direct-response carriers. In addition, as requested by IIABA, the affiliates of groups leveraging various distribution systems are separated and placed by A.M. Best Co. in the appropriate distribution category (wherever the company group uses separate affiliates for this purpose).

Adjusted Numbers

In the charts in this report, previous year market share numbers are the most mature numbers compiled by A.M. Best, and they reflect the same affiliate adjustments in order to provide as accurate comparisons as possible. Careful readers of these IIABA market share reports will note some premium and market share data changes; we use the new numbers for prior years from the latest report, which is 2008. This occurs because carriers report adjustment which can change the market share percentages for prior years.

Rounding

Note that some numbers in the charts may not add to 100% of market share; this is due to rounding of minute numbers.

Further Data Changes/Notes

There were two major changes made to the information provided to IIABA in the last five years to further enhance the accuracy of the numbers. Several company groups from the regional independent agency company category were reallocated to the national independent agency category. A.M. Best requires a company to write in many states and to write multiple lines of business in order to fit into the national agency category. When A.M. Best makes such changes, the changes are made for the prior years as well in order to produce as accurate comparisons as possible. As a result of these changes, readers should use caution in reaching any broad conclusions as to trends affecting either the national agency company or regional agency company sub-segments of the independent agency and broker market.

Some of the groups that were re-allocated to the national agency category include: W.R. Berkley Companies, Cincinnati Insurance Company, EMC, Harleysville, HDI U.S. Group, Markel Corporation, Old Republic General Group, Winterthur Swiss Group, and XL

America Group. A.M. Best separated Progressive's direct business from what is written by its agency group; the Progressive agency companies, however, remained in the regional group because of the limited lines of business being written by those companies. A.M. Best moved the following companies from the national agency category to the regional category: Amerisure, Atlantic Mutual and Utica National.

For this custom study, A.M. Best continues to reclassify the independent agency affiliates that can be identified for selected groups, such as Allstate, Liberty Mutual, MetLife, Nationwide and Farmers.

In all charts, A.M. Best has re-allocated premium volume to the proper distribution category wherever the carrier used separate affiliates for its different distribution methods. In the personal lines, personal auto, and homeowners charts, however, the market shares for the direct-response companies are somewhat understated because the direct business written by The Hartford cannot be separated from the independent agency business written by this company, as it is not written in a separate affiliate. In addition, A.M. Best has not been able to separate out most of AIG's direct auto business (written in the AIG name) from that written through independent agencies, and that business appears in the national agency company category. A.M. Best does separate out AIG's 21st Century business to the direct category, or the direct-response business it acquired from GE Financial Assurance.

This overstatement of independent agency numbers is partially offset by the fact that Allstate's rural independent agency program is still classified as part of its captive agency business. Allstate's other independent agency business, which is written in separate affiliates such as Encompass and Deerbrook, has been placed in the proper distribution system category. In addition, A.M. Best has not been able to separate out Farmers' independent agency business that it writes in eastern states, except for the business written in the Foremost name. This additional Farmers' independent agency business continues to be included in the captive agency category.

IIABA and A.M. Best work together each year to continually refine the data and make adjustments wherever possible. IIABA comments on and uses only the numbers ultimately provided by A.M. Best.