

# Insurance Industry

## Early Read on Japanese Earthquake and Tsunami

**Magnitude:** It is very early, but the effects of the earthquake and tsunami in northern Japan on March 11 could be materially larger than the recent Christchurch earthquake loss (estimated at \$5 billion to \$10 billion). The tsunami will affect several types of insurance coverage areas and the Japanese market has some very large reinsurance programs.

- Japan is a sizable reinsurance market that has been underpriced for years. This means that reinsurers have been selling capacity at relatively low rates and will likely incur a good share of this loss.
- Tsunami exposure is a covered peril. This means that losses related to this event where insurance is in place will be covered.
- Exposed insurance coverages include agriculture, marine, commercial property, and transportation (trains and harbors); these lines of business could incur significant losses. Homeowners' insurance, for the most part, is not handled by the insurance/reinsurance market.
- The northern part of Japan is heavily agricultural. A large Japanese mutual insurer that covers most farms in this area has typically purchased \$7 billion to \$10 billion of reinsurance coverage. The large European reinsurers usually handle most of this program.
- Marine and transportation insurance/reinsurance will likely be another source of significant losses. This includes boats and ships, harbors, railroads, and similar areas affected by the event. Lloyd's of London and Bermuda reinsurers will likely have material exposure, particularly the insurers or syndicates with significant marine books of business.
- Market impact is too early to call. There is a good probability that pricing will go up materially in Japan, particularly as the market has been soft for some time. It is too early to tell if the event could have spillover effects to other property-/marine-oriented reinsurance markets. The magnitude of the loss to the large Europeans reinsurers is a key factor to watch.
- Positive for the brokers. The brokers Aon, Willis, and Marsh should have at least a moderately favorable impact from the event through their reinsurance brokerage subsidiaries. Aon/Benfield has the largest share of the international market (upwards of 40%) and Willis Re and Guy Carpenter have closer to a quarter of the market. However, reinsurance brokerage has the highest impact on Willis (over 20% of earnings) versus closer to 10% for Aon and Marsh. If the impact of the tsunami spills over the other markets, this could be a significant positive for the reinsurance brokers.

### Financial | Insurance Brokers

March 11, 2011

#### Aon Corporation

Stock Rating: **Outperform**  
 Company Profile: **Established Growth**  
 Symbol: AON (NYSE)  
 Price: \$49.91 (52-Wk.: \$35-\$53)

#### Marsh & McLennan Companies, Inc.

Stock Rating: **Market Perform**  
 Company Profile: **Established Growth**  
 Symbol: MMC (NYSE)  
 Price: \$29.20 (52-Wk.: \$20-\$31)

#### Willis Group Holdings Public Limited Company

Stock Rating: **Outperform**  
 Company Profile: **Established Growth**  
 Symbol: WSH (NYSE)  
 Price: \$37.86 (52-Wk.: \$29-\$40)

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Bottom line: The tsunami is another in a string of recent negative catastrophe events for property-oriented reinsurers unless the event is sufficient to change pricing across markets. For now, the potential for higher pricing is a moderate positive for the brokers. Willis likely has the most incremental leverage, although it is also a positive for Aon.

**Insurance Brokers  
Valuation Comparison**

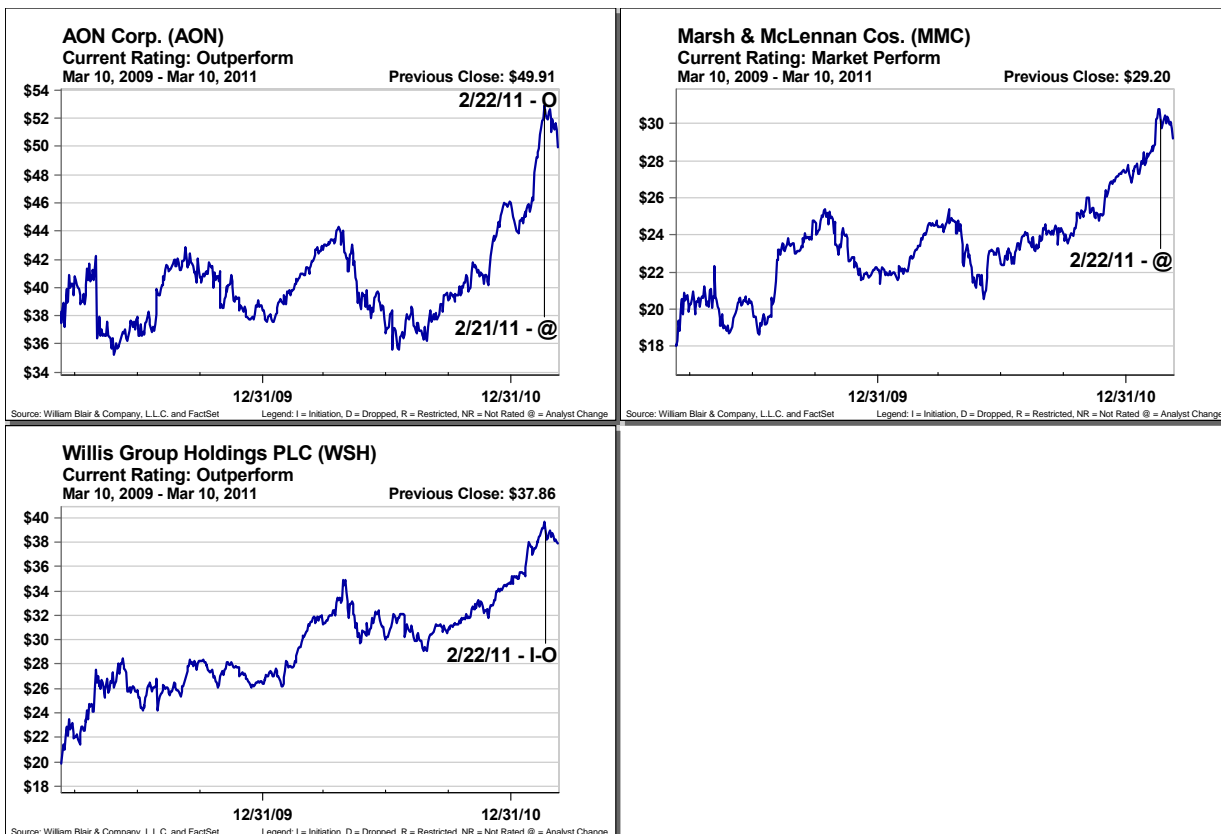
Ticker	Rating	Price	GAAP EPS			GAAP P/E			Cash P/E			EV / EBITDA		
			2010	2011E	2012E	2010	2011E	2012E	2010	2011E	2012E	2010	2011E	2012E
AON	O	49.91	\$3.07	\$3.25	\$3.84	16.3x	15.4x	13.0x	15.1x	13.8x	9.6x	9.9x	7.2x	6.6x
AJG	M	30.46	\$1.41	\$1.50	\$1.75	21.6x	20.3x	17.4x	15.8x	16.1x	14.1x	11.5x	9.9x	8.8x
BRO	M	24.92	\$1.13	\$1.17	\$1.32	22.1x	21.2x	18.9x	16.7x	16.1x	14.6x	11.1x	10.6x	9.6x
MMC	M	29.20	\$1.66	\$1.82	\$2.04	17.6x	16.0x	14.3x	16.9x	15.4x	13.8x	10.1x	9.8x	9.2x
WSH	O	37.86	\$2.69	\$2.80	\$3.55	14.1x	13.5x	10.7x	12.4x	12.3x	10.0x	9.6x	9.4x	8.0x
Average						18.3x	17.3x	14.9x	15.4x	14.7x	12.4x	10.4x	9.4x	8.5x
Median						17.6x	16.0x	14.3x	15.8x	15.4x	13.8x	10.1x	9.8x	8.8x

Source: Company reports, Thomson One, and William Blair & Company L.L.C.

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Outperform (Buy)	65	Outperform (Buy)	9
Market Perform (Hold)	34	Market Perform (Hold)	1
Underperform (Sell)	1	Underperform (Sell)	0

\*Percentage of companies in each rating category that are investment banking clients, defined as companies for which William Blair has received compensation for investment banking services within the past 12 months.

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