Portfolio Review: Understanding Key Reports & Analyses

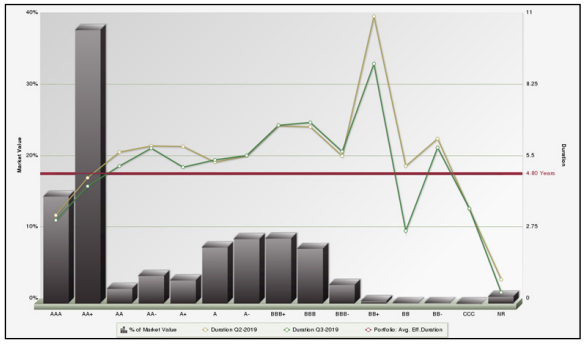
It's typical for insurance companies and government risk pools to receive a quarterly report from their investment manager and/or investment consultant with various charts and analyses reviewing the investment portfolio. Given the vast amount of data that can be provided, it is easy for Boards and Committees to become inundated with information.

To simplify the portfolio review process, insurers and risk pools should focus on better understanding a select group of reports and analyses. Understanding these key reports will maximize the benefits of the portfolio review process; providing a clearer picture of the investment portfolio's structure, overall strengths and potential issues.

Credit Duration

Description:
Credit rating agencies provide the same rating for a given issuer, irrespective of the maturity of its bond. For example, an issuers' two-year bond is given the same credit rating as its ten-year bond, even though predicting the likelihood of repayment becomes more difficult when looking over longer time spans.

Credit Duration analysis combines credit risk and interest rate risk *(aka duration)*. A bond's duration gauges how its price may fluctuate due to interest rate changes.



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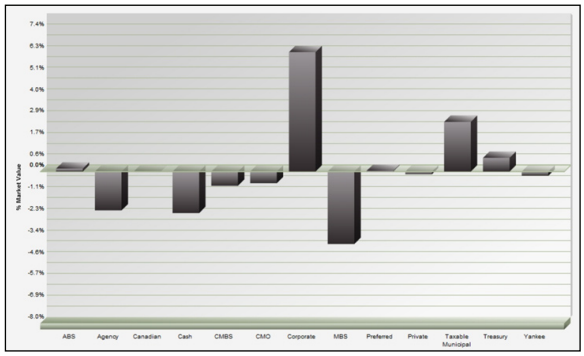
Each vertical bar displays the amount invested in each credit rating. The horizontal line indicates the average portfolio duration. The other line graphs correspond with the duration within a given credit rating.

Importance:
Ideally, the duration for any given credit rating will not vary much from the portfolio's overall duration. However, if duration increases as credit risk increases *(shown through an upward sloping line)*, it can be a sign for problems to come as it relates to the value of the bond portfolio.

Asset Allocation Change

Description:
An Asset Allocation Change report displays how asset allocations within certain sectors have changed from the prior quarter.



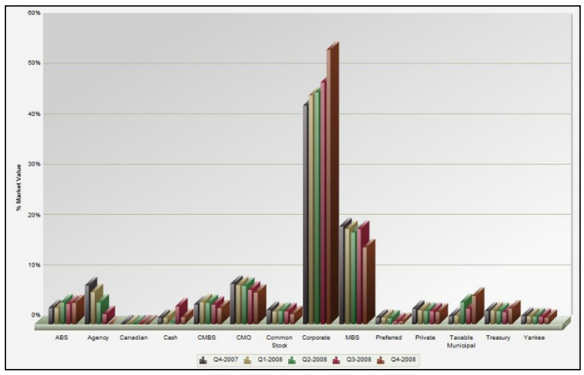
Importance:
This analysis quickly identifies any major changes in the portfolio's asset allocation.

Asset Allocation (%)

Description:
Asset Allocation (%) analyses review the amount the fixed income portfolio, risk asset portfolio and total portfolio (fixed income + risk assets) are invested towards various asset types.

Importance:
Commercial insurers tend to have fixed income portfolios tilted more towards 'spread' sectors and away from lower yielding US Treasuries and Agencies. Due to regulatory restrictions, many government risk pools are heavily allocated towards US Treasuries and Agencies and are limited in their ability to utilize risk assets.

This report allows insurers and risk pools to see trends and changes within the investment portfolio's mix of sectors.



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Typically, allocations are compared across the five most recent quarters.

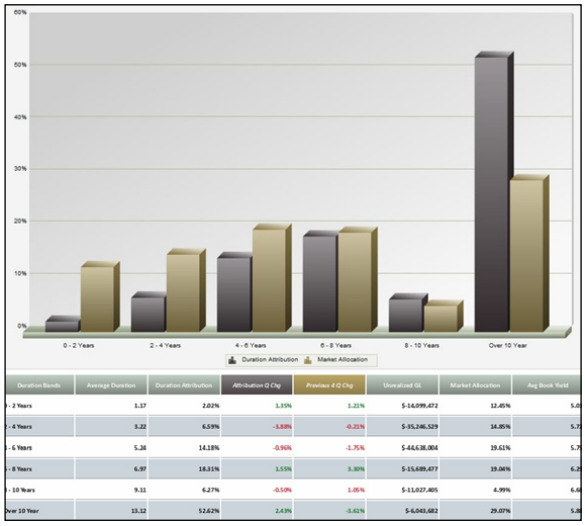
Duration Profile

Description:
A Duration Profile report places the portfolio's bonds into six pre-determined duration buckets *(i.e. 0-2 years, 2-4 years, etc.)* and compares the "Duration Attribution" to the market value *(market allocation)* of each bucket.

Duration Attribution is calculated by multiplying the average duration in a given bucket by the market value and then dividing that result by the multiplication of the portfolio's market value by its average duration.

Importance:
It is easy to identify a portfolio's average duration, but how the average is calculated provides a greater level of detail. For example, a portfolio's average duration may be longer than expected simply due to a small amount of long duration bonds.

Knowing where duration is occurring can provide a better understanding on how sensitive the portfolio may be to changes in the shape of the yield curve.



Duration Bands	Average Duration	Duration Attribution	Attribution Q Chg	Previous 4 Q Chg	Unrealized GL	Market Allocation	Avg Book Yield
- 2 Years	1.17	2.02%	1.15%	1.21%	$-14,099,472	12.45%	5.0
- 4 Years	3.22	6.59%	-3.68%	-0.21%	$-35,246,529	14.85%	5.7
- 6 Years	5.26	14.18%	-0.96%	-1.75%	$-44,638,004	19.61%	5.7
- 8 Years	6.97	18.31%	1.55%	3.30%	$-15,689,477	19.06%	6.2
- 10 Years	9.11	6.27%	-0.50%	1.05%	$-11,027,405	4.99%	6.4
Over 10 Year	15.12	52.62%	2.43%	-3.61%	$-6,043,682	29.07%	5.8

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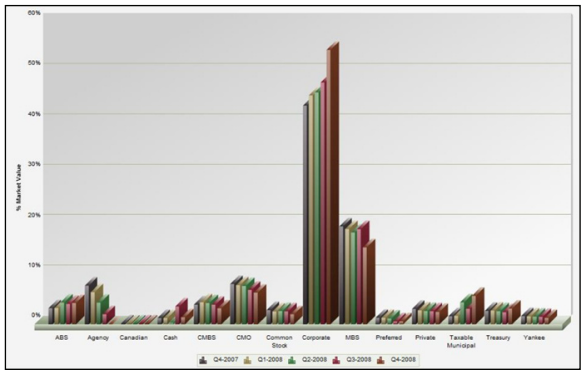
Portfolio Review: Understanding Key Reports & Analyses

Credit Rating Detail

Description:
A Credit Rating Detail analysis displays the percentage of the fixed income portfolio invested in any given detailed credit rating over; typically compared over the last five quarters.

Importance:
One of the most important decisions in fixed income portfolio construction is its exposure to credit risk. This report allows you to see trends in this allocation over the last five quarters.



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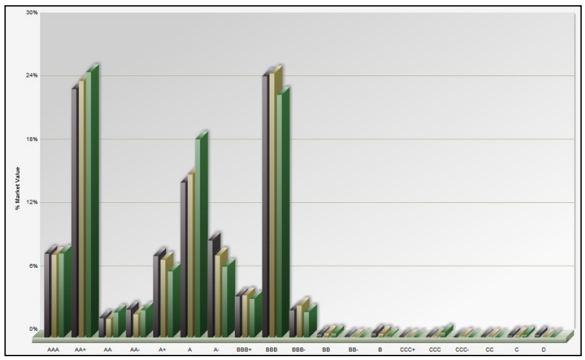
Credit Exposure

Description:
This identifies the ten largest individual securities held in the portfolio, along with their respective market values, allocation percentage, book value, credit rating, duration and maturity. Typically, this report also compares these top ten exposures to the total portfolio.

Importance:
This report provides a glimpse at which bonds are the largest in the portfolio and an initial snapshot of the overall diversification.



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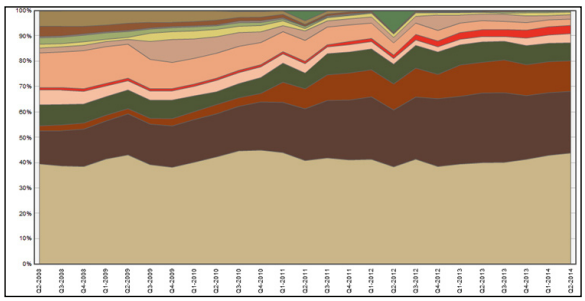
Detailed Historical Asset Allocation Summary

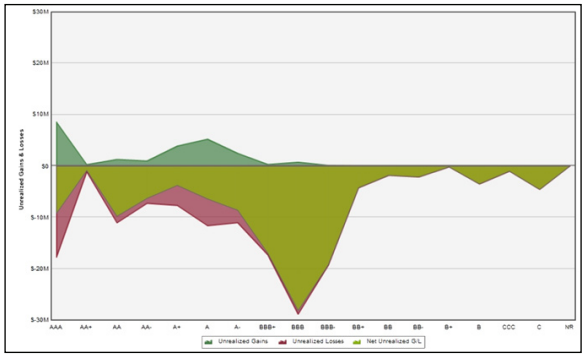
Description:
Most Asset Allocation analyses are over shorter periods of time. This compares a portfolio's asset allocation over five or more years.

Importance:
Insurance companies and government risk pools tend to make changes to their portfolio slowly from quarter to quarter, keeping in mind realized gain or loss limits, etc. Reviewing trends over a longer-term horizon can provide a clearer perspective since small changes over a long period of time can equate to very large changes.



Unrealized Gains and Losses

Description:
An Unrealized Gains and Losses (also known as 'paper losses' as the bond or stock as not been sold yet) report displays all gross unrealized gains and losses, as well as net gains or losses, for bonds in various credit rating categories.



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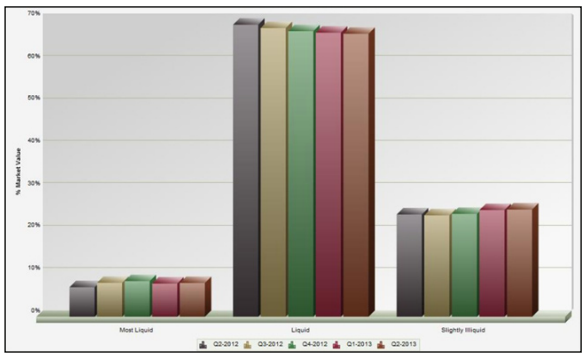
Importance:
To the extent that an insurance company or risk pool may require taking gains or losses, availability to do so may be limited; not only by the portfolio's overall net realized gain or loss position, but by their availability within a given credit rating.

If gains or losses are unusually large for a given credit rating, it may be worthwhile to determine the source.

Implied Portfolio Liquidity

Description:
An Implied Portfolio Liquidity report loosely places certain asset classes in three basic liquidity buckets: Most Liquid, Liquid and Slightly Liquid.

It is important to note this analysis is not designed to make a judgment on specific issues within the asset classes and it does not take into account limitations past possible liquidity (such as imbedded unrealized gain/loss).



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Importance:
Liquidity risk is very difficult to quantify.

This very basic approach is a means to raise the issue and be a starting point for discussions, especially as there are major changes over time or if the portfolio appears to be too liquid or not liquid enough based upon this very initial view.

Potential Impairment Report (OTTI)

Description:
Other than temporary impairment (OTTI) usually occurs when a security's fair market value is below 80% of book value for a consecutive six months or more.

A Potential Impairment Report screens for securities below 90% of book value, color coding the amount of book to market value percentage depending upon how serious the value drop is.

Importance:
This report serves as an 'early warning' for such securities, as it screens for securities that are valued below 90% of book.

OTTI (Watch List <= 90%)

Consolidated FI

3rd Q, 19

0.0 up to 0.5
0.5 up to 0.7
0.7 up to 1.0

Cusip	Issuer	AssetType	Quantity	Book Value	Market Value	MV/BV	Unrealized G/L	Duration	Book Yield	CR
73557*AB	PORT WASHINGTON	Corporate Bond	1,200,000	867,275	517,550	59.7%	-349,725	7.60	6.00	NR
88167AAE	TEVA PHARMACEUTICAL FINANCE NETHERLANDS III BV	Corporate Bond	1,000,000	1,006,555	700,000	69.5%	-306,555	5.78	3.05	BB-
88167AAE	TEVA PHARMACEUTICAL FINANCE NETHERLANDS III BV	Corporate Bond	300,000	301,935	210,000	69.6%	-91,935	5.78	3.05	BB-
674599CF	OCCIDENTAL PETROLEUM CORP	Corporate Bond	380,000	433,300	389,099	89.8%	-44,201	14.95	3.76	BBB-
12669FXB	CWHL 2004-5 B1	non-Agency CMO	400,000	9,861	0	0.0%	-9,861	0.00	5.74	D
02313988	AMBAC FINANCIAL GROUP INC	Preferred Equity	8,207	198,609	160,447	80.8%	-38,162	0.00	0.00	NR
31392GWD	FHW 2003-W1 H	U.S. Agency CMO	500,000	137,248	90,346	65.8%	-46,903	2.77	3.47	CCC
Grand Total:	7		3,788,207	2,954,783	2,067,442	70.0%	($887,340)	7.38	3.84	

% of Portfolio @ BV 0.12%
% of Portfolio @ MV 0.08%

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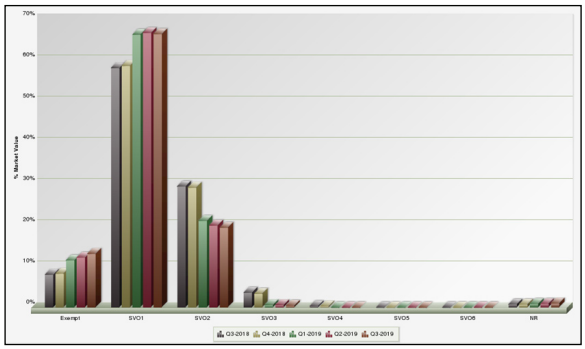
SVO Rating

Description:
The Securities Valuation Office (SVO) of the National Association of Insurance Commissioners (NAIC) requires that US insurer fixed income investments have an SVO credit rating, ranging from 1 to 6.

The SVO has issued a table which shows the equivalent SVO rating for any given ratings from S&P, Moody's or Fitch.

This report uses that table to imply the correct SVO rating for each security in the fixed income portfolio; and then show the percentage of the fixed income portfolio invested in any given SVO rating over the last five quarters.



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Importance:
One of the most important decisions in fixed income portfolio construction is its exposure to credit risk. This report allows you to see trends in this allocation over the last five quarters, as would be seen through the 'eyes' of the SVO.