

## An Insight into the World of Insurance Mergers and Acquisitions

## Recent Noteworthy Transactions

\$s in millions

## PROPERTY / CASUALTY DEALS

Target	Buyer	Value	Price to GAAP:	
			Equity*	Op. Earn
Praetorian Financial Grp.	Delek Capital, Ltd.	\$800	2.1x	N/A
Direct General Corp.	Elara Holdings, Inc.	\$453	2.0x	14.9x
NLASCO, Inc.	Affordable Res. Comm.	\$118	1.7x	7.8x
Merchants Group, Inc.	American European Grp.	\$71	0.9x	12.4x

\* Tangible

## AGENT / BROKER DEALS

Target	Buyer	Value	Price to:	
			Revenue	
Alexander Forbes Int'l. Risk Services	Lockton Inc.	\$170	0.8x	
Jardine Lloyd Thompson	U.S. Retail Alliant Ins. Services	\$100	1.7x	
Fortun Insurance	HUB International	\$26	2.6x	
Leader Associates	USI Holdings	\$20	2.3x	

## LIFE DEALS

Target	Buyer	Value	Price to SAP:	
			Surplus	Net Inc.
Mayflower National Life	Assurant	\$65	1.2x	16.1x

## Deal Activity is Fast and Furious

Insurance M&A is in full swing. In addition to some very sizable agent/broker deals, P&C carriers of all shapes and sizes are being acquired. It's a challenge to summarize all the action.

Following Lockton Companies' \$170 million purchase of Alexander Forbes' International Risk Services that will boost Lockton's annual revenue by roughly \$200 million (nearly 50%), CA-based Alliant, which is backed by the private equity firm Lindsay Goldberg & Bessemer, announced it is buying the US retail operations of Jardine Lloyd Thompson for \$100 million. This transaction adds about \$60 million, or roughly 25%, to Alliant's top-line. However, the biggest broker deal by far is the buy-out of USI for nearly \$1 billion (approximately 1.8x LTM revenue and 9.4x LTM EBITDA) by Goldman Sachs & Co.'s private equity group, GS Capital Partners. In October, USI announced that it had received an offer from a private equity group. This is the largest broker deal since KKR's \$1.7 billion management buyout of Willis Group nearly ten years ago.

Speaking of big deals, on the P&C carrier side Australia-based QBE takes top honors. In the last month it has agreed to buy both Winterthur US (General Casualty / Unigard) from AXA (who had owned it for about 11 days) for \$1.2 billion and Praetorian Financial Group, a specialty program underwriter, from Hannover Re for \$800 million. Earlier in '06, QBE bought two other operations: White Mountains' National Farmers Union (\$132 million) and OneBeacon's Agri-business (\$32 million). The result: QBE is now a large, diversified insurance / reinsurance player in the US.

QBE is not the only foreign buyer of note. Following on the heels of Delek Capital's acquisition of TX-based Republic, another Israel-based firm struck a deal for a US insurer in November. Clal Insurance (US\$1.6 million in revenue), a multi-line insurer that insures one of every three businesses in Israel, announced its \$120 million deal with GUARD Financial, a PA-based workers' comp company. Further product and geographic expansion is expected.

Meanwhile, non-standard auto witnessed action reminiscent of the late 90's as direct writers USAgencies and Direct General both accepted buy-out offers within seven weeks of one another for \$200 million and \$453 million respectively. The private equity controlled acquirers; Affirmative Insurance (USAgencies) and Elara (Direct

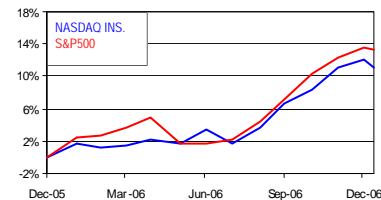
## Insurance Carrier Stocks

## PROPERTY / CASUALTY CO.'s

Median Price to Earnings (ttm): 11.1x  
Median Price to Book (mrq): 1.4x

## LIFE &amp; HEALTH COMPANIES

Median Price to Earnings (ttm): 15.4x  
Median Price to Book (mrq): 1.3x



## MULTI-LINE COMPANIES

Median Price to Earnings (ttm): 14.7x  
Median Price to Book (mrq): 1.4x

## INDEX PERFORMANCE

NASDAQ Ins. YE '06: 12.1%  
S&P 500 Total Return YE '06: 15.8%

## Insurance Broker Stocks

Price (1/8/07) to TTM (9/30/06)

	Revenue	Earnings	EBITDA	EBITDA/Revenue %
Maximum	4.6x	37.5x	14.4x	39.1%
Minimum	1.2x	15.3x	8.1x	13.3%
Median	1.9x	21.3x	10.4x	19.5%

## Deal Activity is Fast and Furious cont'd.

General) savor the non-standard auto's lower capital requirements and high fee income generation.

Deal activity among mutuals is heating up. ME-based Patriot Mutual has entered into a merger agreement with A+ rated, MI-based Frankenmuth Mutual. The deal will afford B++ rated Patriot substantial financial, technological, and product development support to grow its franchise. Meanwhile, in December, B++ rated Sheboygan Falls Mutual and Donegal Mutual struck an affiliation agreement whereby Donegal will make a contribution note investment of \$3.5 million into the 207 year old, WI-based mutual that wants to grow. CAT cover costs and technology requirements continue to pressure the smaller mutuals. The soft market will continue to exacerbate these challenges.

Softening rates, strong public valuations and piles of capital should continue to drive plenty of M&A activity. At this point, there are precious few insurance segments that are not of interest to buyers. In particular, look for carriers buying distribution (MGAs, MGUs) and private equity firms chasing everything. 2007 should be an interesting year.

## Deal Notes


## AJ Gallagher Buys The Rains Group, Inc.

According to its third quarter '06 10-Q, AJG paid \$13.5 million (approx. 75% in AJG stock) for the MI-based employee benefits broker. According to its website, the company was founded in 1996, has 29 employees and targets clients ranging from auto suppliers to school districts.

## Affordable Residential Communities Inc. Buying NLASCO Inc.

ARC is paying \$117.5 million (90% in cash) for the Waco, TX-based insurer of low-value dwellings and mobile homes. NLASCO's direct written premiums totaled \$147 million in '05 with a GAAP combined ratio of 77.5%. This deal should provide ARC an opportunity to leverage its \$361 million of NOL's in addition to cross-selling to its existing customers.

# SOME OF OUR TRANSACTIONS.....



State Auto Mutual Insurance Co.

*has agreed to acquire*

Beacon Insurance Group

PhiloSmith acted as exclusive financial advisor to State Auto Mutual Insurance Co.



The assets of  
Lorghon General Agency, Inc.  
&  
Lorghon Insurance Services, Inc.

*have been acquired by*

NALICO General Agency, Inc.  
a subsidiary of NLASCO

PhiloSmith acted as exclusive financial advisor to Longhorn General Agency



Texas General Agency, Inc.  
*and their affiliates*

Gulf States Insurance Co.,  
TGA Special Risk, Inc.,  
& Pan American Acceptance Corporation

*have agreed to be acquired by*

Hallmark Financial Services, Inc.

PhiloSmith acted as exclusive financial advisor to Texas General Agency, Inc.




GMAC Insurance Holdings, Inc.  
*and its subsidiary*

Motors Insurance Corporation

*have agreed to acquire*

MEEMIC Insurance Company  
*a subsidiary of*  
ProAssurance Corporation

PhiloSmith acted as exclusive financial advisor to GMAC Insurance Holdings, Inc.



HI Holdings, Inc.  
*and its subsidiary*

Zephyr Insurance Company

*agree to be acquired by*

Kingsway Financial Services, Inc.

Philo Smith & Co. acted as exclusive financial advisor to HI Holdings, Inc.

**D.E. LOVE ASSOCIATES**

D. E. Love Associates  
*a subsidiary of*

Direct Response Corporation

*has been acquired by*

National Penn Bank

Philo Smith & Co. acted as exclusive financial advisor to Direct Response Corporation



Future Planning Associates, Inc.

*has been acquired by*

U.S.I. Holdings Corporation

July 2004

Philo Smith & Co. acted as exclusive financial advisor to Future Planning Associates, Inc.



Beecher & Carlson  
Risk Management, Inc.  
*a subsidiary of*

American Re Corporation

*has been acquired by*

Risk Strategy Partners, Inc.

Philo Smith & Co. acted as exclusive financial advisor to Munich-American Global Services, Inc.




Andrews & Murray  
Associates, Inc.

*has been acquired by*

Neighborhood Insurance  
Connecticut, LLC

Philo Smith & Co. acted as exclusive financial advisor to Andrews & Murray Associates, Inc.



Allianz of America, Inc.  
and  
Fireman's Fund Insurance Co.

*have agreed to sell*

Fireman's Fund Direct  
to  
Response Insurance Group

Philo Smith & Co. acted as financial advisor to Allianz of America and Fireman's Fund Insurance Co.



GuideOne Insurance Group

*has agreed to sell*

GuideOne Life Insurance  
Company  
to  
Kansas City Life  
Insurance Company

Philo Smith & Co. initiated this transaction and acted as exclusive financial advisor to GuideOne Insurance Group



Response Insurance Group

*has acquired*

Worldwide Insurance Company  
and  
Worldwide Direct Auto  
Insurance Company  
*subsidiaries of*  
Great American Insurance Company

Philo Smith & Co acted as exclusive financial advisor to Response Insurance Group




Financial Industries Corporation

*has merged with*

InterContinental Life Corporation

Philo Smith & Co. acted as exclusive advisor to Financial Industries Corporation



State Automobile Mutual Insurance  
Company

*has merged with*

Meridian Mutual Insurance

*and acquired*

Meridian Insurance Group, Inc.

Philo Smith & Co. acted as exclusive advisor to State Automobile Mutual Insurance Company



Harleysville Mutual  
Insurance Company

*has agreed to merge with*

Penn Mutual Insurance Company

Philo Smith & Co. acted as exclusive financial advisor to Harleysville Mutual Insurance Company



GMAC Insurance  
Holdings Inc.

*has agreed to acquire*

National Alliance  
Insurance Company

Philo Smith & Co. acted as exclusive financial advisor to GMAC Insurance Holdings Inc.



Swiss Re Life and Health America

*has acquired*

Royal Maccabees Life Insurance  
Company  
from  
Royal & SunAlliance Group

Philo Smith & Co. initiated this transaction and acted as exclusive advisor to Swiss Re Life and Health America



United Fire & Casualty Company

*has acquired*

American Indemnity Financial  
Corporation

Philo Smith & Co. initiated this transaction and acted as exclusive financial advisor to American Indemnity Financial Corporation



Guardian Royal Exchange plc

*has exchanged its  
Canadian operations for*

The Netherlands  
Insurance Company  
*a subsidiary of ING Group*

Philo Smith & Co. initiated this transaction and acted as financial advisor to Guardian Royal Exchange



Virginia Mutual Insurance Company

*has agreed to affiliate with*

Alfa Mutual Insurance Company

Philo Smith & Co. acted as exclusive advisor to Virginia Mutual Insurance Company