

# To Our Business Partners:

We have completed another eventful and successful year. While 1992 has proven to be one of turmoil for the insurance industry, your company has avoided many of the industry's problems and is able to report excellent results. Our underwriting units achieved a 97% combined ratio and net income for 1992 amounted to \$26 million or \$4.64 per primary share. This represents a 27% return on average shareholders' equity. Since going public in 1986, return on equity has averaged 29% and book value per share has increased from \$3.42 to \$20.24.

Our primary objective in 1992 was to continue focusing on specialty underwriting and to continue unifying the various companies we had acquired in previous years. Since our "strategic evolution" in December 1990, we have substantially completed this important transition. In early 1992 we completed the sale of our Governmental Programs Division. This was a successful busi-

ness for Markel and we made a very significant profit on its sale. However, the operation was primarily a brokerage business and not consistent with our strategic focus on specialty underwriting.

In April we announced our plan to move Markel Rhulen Underwriters from Monticello, New York to Richmond, Virginia. This move was completed in October and involved a tremendous effort from our entire staff. With this relocation, we will sharpen the focus on underwriting profits as well as the development of appropriate insurance company support functions. We believe this can best be accomplished in Richmond.

To better manage our growing and changing organization, the roles of the executive management team were expanded in 1992. Tony Markel, who was previously Executive Vice President for the Corporation and President of Essex Insurance Company, was made President and Chief Operating Officer of Markel



Markel Rhulen Underwriters provides student accident and health plans for over 200 colleges and universities nationwide. This program is used to ensure that every student has insurance coverage, even if they are no longer eligible for their parents' coverage.



corporation. It is now responsible for all our underwriting operations and will be sure every unit remains concentrated on underwriting profits. By centralizing the management of our insurance companies, we expect to realize many efficiencies in operating and administrative activities. Product line management will remain decentralized and will not stray from our continued focus on quality customer service.

Steve Markel was promoted to Vice Chairman and will continue to have responsibility for strategic planning and investment activities. Additionally, Steve is responsible for capital allocation and loss reserve adequacy.

Darrell Martin was promoted to Executive Vice President and Chief Financial Officer. Darrell is responsible for corporate accounting, treasury and financial operations as well as most other corporate staff functions.

Alan Kirshner remains as Chairman of the Board and Chief Executive Officer. In addition to supervising corporate marketing and human resources, Alan has responsibility for internal communications. This function is particularly important as we are integrating the talent, knowledge and expertise of people from diverse cultures into the Markel "Style".

## Investments

Our investment portfolio at December 31, 1992 was \$442 million. This included \$290 million in fixed income investments which are purchased to assure our ability to meet our liabilities to policyholders. In 1992 we increased our investment in tax exempt securities to \$116 million as yields on these securities became more attractive and our tax position made this alternative worthwhile. The investment portfolio includes \$74 million in equity securities which we believe will provide us the greatest total return over the long term.

We have a larger portion of our portfolio allocated to common equities than many property/casualty insurance companies. Because of our confidence in our underwriting results, we feel comfortable with this strategy. While we believe this strategy will provide the best total return, our short term results may be less consistent because they will include capital gains and losses. Although we recognize the short term impact, we are confident our strategy will enhance shareholder value in the long term.

As we are all aware, we are now in an interest rate environment much different than any we have experienced for many years. With interest rates at such a relatively low level, it is more important than ever for us to maintain a sound underwriting discipline in order to earn our desired return on equity.

## Loss Reserves

As we have reported for many years, assuring adequate loss reserves is an on-going goal for your company.

Our loss reserves represent our best estimates of the amounts necessary to meet our obligations to our policyholders. In establishing these estimates, we attempt to take into consideration all of the relevant information and actuarial methods

available to us. While it is always difficult to accurately determine such future liabilities, we have established a standard for ourselves seeking to set our reserves at a level which we believe is more likely to prove to be redundant than deficient.

At December 31, 1992 total loss reserves were \$353 million compared to \$346 million last year. During 1992 we realized \$10 million in redundancies from prior periods. More importantly, we are pleased that in each of the past five years this has been the case.

As we reported last year, we were in dispute with regard to the contingent notes related to the acquisition of Shand/Evanston in 1987. With respect to the largest of these notes, in January of 1993 a final determination was made by an independent actuary and accountant. The good news is that, as to 1986 and prior reserves at Shand, this independent expert found our reserves to be more than adequate. The bad news is that we were required to make an additional payment on the note; however, this had no material impact on our financial results.

## Long Term Debt

Since December 1990, when long-term debt was \$127 million, it has been our objective to reduce this leverage. With good cash flow and the sale of our Governmental Programs Division, we reduced long-term debt to \$67 million at September 30, 1992. At that point in time debt was 40% of total capitalization...very near our goal of 33%.

In the fourth quarter of 1992 we increased borrowing by \$34 million leaving debt of \$101 million at year end. So what happened? We'll explain.

The Company's primary credit source has been a \$70 million revolving credit facility with provisions to convert to a seven year term loan at December 31, 1992. The rate and terms of this facility are most attractive. At September 30, 1992 we had borrowed \$34 million with the unused \$36 million representing our available credit. In order to assure ourselves of the availability of capital on these favorable rates and terms, we borrowed the full amount available through this facility prior to converting it to a term loan.

## The Future

We opened this letter by making reference to the turmoil in the insurance industry and think it appropriate to expand on this subject. We have been in a soft, competitive insurance cycle for the past five years. In each of these years the industry has seen declining returns on equity. In 1991, the industry return declined to approximately 7% and in 1992 the numbers will certainly be worse.

In 1992 there have been an unusual number of headline stories describing problems in the insurance business. These headlines describe major losses and company reorganizations, as well as the recognition that loss reserves have often been inadequate to meet claims costs. Even some very old line, established companies experienced difficulties as a result of Hurricane Andrew's estimated \$16.5 billion in losses and Hurricane Iniki hitting Hawaii.



Several companies that diversified into the insurance industry in the 60's and 70's are now exiting this business altogether. Many experienced losses for the first time in decades as a result of inadequate loss reserves, reinsurance bad debts, catastrophic losses and bad investments in real estate and mortgages.

The P&C insurance industry is truly battered and bruised!! 1992 brought big losses and sooner or later those companies most affected must return to good business judgment.

Having focused on specialty, niche marketing and having the discipline to make money as an underwriter, we've successfully avoided most of the industry's problems. But pricing has been soft and the marketplace very competitive for the past five years. Even today, with all of the industry problems, we still face a very competitive market.

### Within the negative industry headlines, there is good news for Markel

First: The significant restructuring currently taking place in the industry is likely to create new opportunities for Markel, whether it's an opportunity to underwrite a new product or to acquire a new business.

Second: Sooner or later the cycle will turn, even though it may not be as dramatic as we've experienced in the past. Shareholders will demand reasonable returns on equity. The result will be increasing prices and sound industry underwriting practices. We'll do well in this environment, too.

While these forecasts are both optimistic, our past success and our future success lies in being able to maintain focus on our mission:

- To provide quality products and excellent customer service in a variety of niche markets;
- To be a market leader; and
- To earn underwriting profits and superior investment returns.

At Markel, there is a feeling that the future we've been planning for is here.

Thank you.

Alan I. Kirshner  
Chairman and C.E.O.

Anthony F. Markel  
President and C.O.O.

Steven A. Markel  
Vice Chairman



A sharp-eyed shareholder noticed that this picture of Alan Kirshner flanked by Steve (*left*) and Tony Markel (*right*) appeared in both our 1990 and 1991 annual reports. He complimented the company for being "tough on costs". The photo is reprinted now to display our never-ending cost control efforts and our never-aging key executives.