



2008 Enterprise Risk Management Symposium

Pursuing Risk or Return?

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VP & CRO



Before we start talking about Risk and Return, it might be helpful to know who we are...





- The Allstate Corporation Is The Largest Publicly Held Personal Lines Insurer In The United States
- Engaged Primarily In The Personal Property & Casualty And Life Insurance & Retirement Businesses
- Market Rank
 - # 2 Property / Casualty – Personal Lines
 - # 12 Individual Life In Force
- 2007 Statistics
 - Revenues \$ 37 B
 - Assets \$ 156 B
 - Net Income \$ 4.6 B
 - GAAP ROE 21.2%



Allstate's Culture Change to Risk & Return Optimization...



- **ERM** 
(Enterprise Risk Management)
- **ERRM**
(Enterprise Risk & Return Management)
- **ERC** 
(Enterprise Risk Council)
- **ERRC**
(Enterprise Risk & Return Council)

ERRM is 1 of our 4 Corporate Operating Priorities!

Allstate's Strong Commitment to ERRM...



As indicated in our Shared Vision, Enterprise Risk & Return Management (ERRM) will be critical to our future success...

RECENT SUCCESS *due to:*

1. Operational Excellence

2. Capital Management

FUTURE SUCCESS *depends upon:*

1. Operational Excellence

2. Capital Management

3. Consumer Focus

4. Enterprise Risk &
Return Management

This Afternoon's Session: Risk vs. Return



In the Pursuit of **Return**, Have We Lost Sight of **Risk**?

OR

In the Pursuit of **Risk**, Have We Lost Sight of **Return**?

Gaining Insight...



What are the causes of the largest corporate bankruptcies?

Severe Recession?

Catastrophe?

Excessive Debt?

Technology?

Reasons for the 10 Largest U.S. Corporate Bankruptcies (1980 – Present)



Company	Pre-Bankruptcy Assets (\$ Bil)	Reason
WorldCom	103	Accounting shenanigans
Enron Corp.	63	Accounting shenanigans
Conseco	61	Poor acquisition due diligence & senior executive abuses
Texaco	36	Inebriated oil tanker captain
Pacific Gas & Electric	36	Regulated retail rates and unregulated wholesale rates
Financial Corp. of America	34	Loan Fraud
Refco	33	Accounting fraud
Global Crossing	30	Excessive debt building fiber optic cable network
Calpine	27	Rising gas prices with locked in electricity rates
New Century Financial	26	Sub-prime lending

Source: BankruptcyData.com

Reasons for 11-20th Largest U.S. Corporate Bankruptcies (1980 – Present)



Company	Pre-Bankruptcy Assets (\$ Bil)	Reason
United Airlines	25	Competitive business model
Delta Air Lines	22	Competitive business model
Adelphia Communications	21	Accounting shenanigans
Mcorp	20	Loan defaults in Texas
Mirant	19	Rising gas prices with locked in electricity rates
American Home Mortgage	19	Alt-A and adjustable rate lending
NTL	17	Debt from Cable TV acquisition spree
Delphi	17	GM auto slump / union wages
First Executive	15	Credit risk / product design flaws
Gibraltar Financial	15	S&L debt

Source: BankruptcyData.com

Competence...

Nearly all of the 20 largest corporate bankruptcies are primarily due to lack of basic management integrity / competency and operational risk failures.

Risks That Were Not Fully Understood Going Into This Decade...



- Hurricanes
- Earthquakes
- Terrorism
- Credit
- Sub-prime
- Certain Structured Securities
- Counterparties
- Liquidity
- Annuity Guarantees
- Customer Behavior (LTC)
- Avian Flu
- Misc. Operational

“Victims” of Direct & CDO Exposure to Sub-Prime

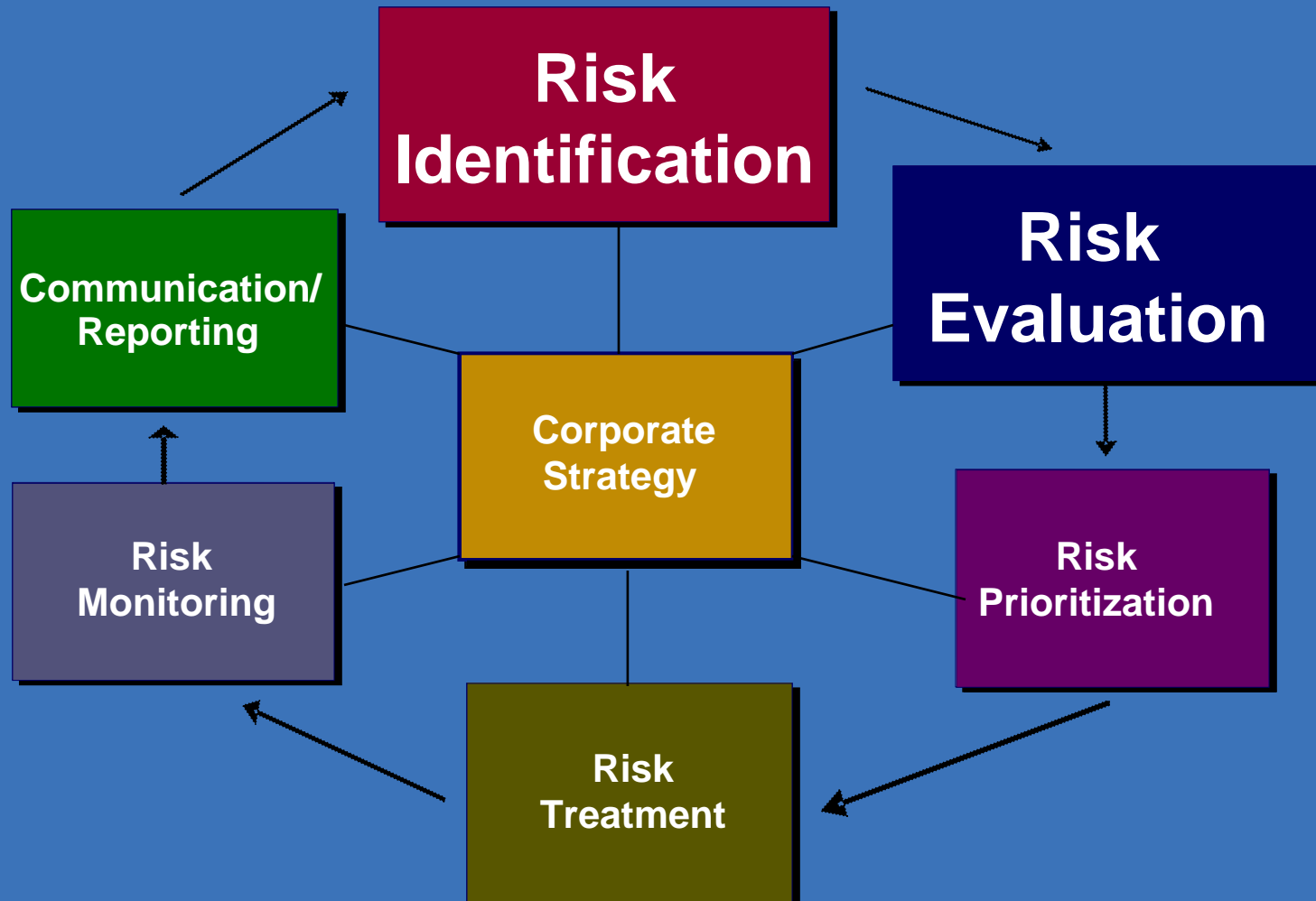


	MARKET CAPITALIZATION		
	52 Week High	Current	Change
Municipal Bond Insurers	(\$ bil)	(\$ bil)	(%)
Ambac	26	1	-93
MBIA	17	3	-83
Radian	5	<1	-90
Investment Banks / Mortgage Originators			
Bear Stearns	21	<1	-97
Citigroup	286	106	-63
Countrywide Financial	18	3	-88
Fannie Mae	76	30	-60
Freddie Mac	48	18	-62
Merrill Lynch	83	37	-55
UBS	167	47	-60
Washington Mutual	37	8	-78
TOTAL	784	254	-68

Source: Yahoo Finance 3/19/08

△ = 530

The Traditional Way to Manage Risk...



We Need to Go Back to Basic Risk Fundamentals



- I**ntegrity → Enron, Worldcom
- C**ompetency → Municipal Bond Insurers
- D**iversification/
- C**oncentration } → Mutual Benefit (Real Estate)
First Executive

The Role of ERM and the Corporate Risk Officer

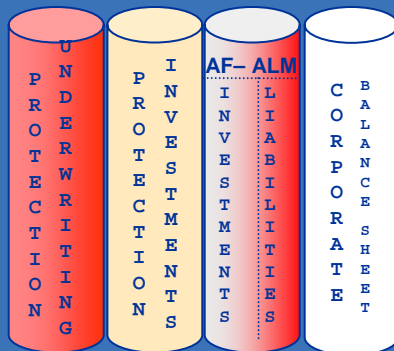
Create sufficient transparency and provide insight to the key risks facing the enterprise so that senior management and the B.O.D. can make the most well informed decisions possible.



ERRM Evolution to Risk & Return Optimization...

Risk Management in Isolation

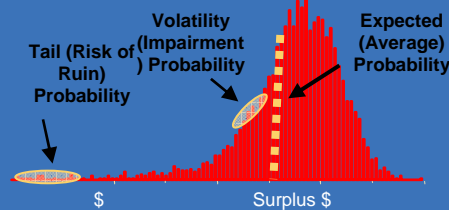
- Business Unit Silo Approach



Enterprise Risk Management

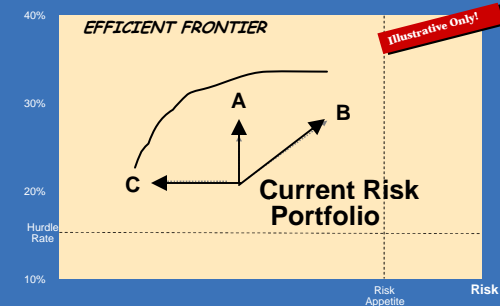
- Holistic Enterprise Perspective

of Trials Stochastic Modeling – Surplus Distribution



Enterprise Risk & Return Management

- Proactively dialing up & dialing down various enterprise risks to optimize shareholder value on the efficient frontier



- A. Projects that add return at similar levels of risk
- B. Projects that add return at added levels of risk
- C. Projects that reduce risk at the same level of return

ERRM... Delivering Insight

Enterprise Risk & Return Management (ERRM)



Proactive Risk Exploitation / Optimization



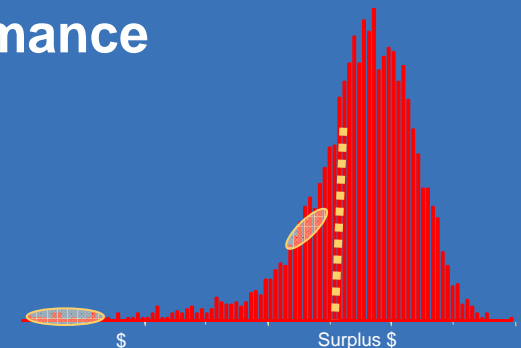
Drives Improved Decision Making



Leads to Improved Financial Performance



Drives Increase in Shareholder Value





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In the Pursuit of Return, Have We Lost Sight of Risk?
Perspectives for discussion.

James C. Allison
Regional Risk Manager, Gas and Power North America
ConocoPhillips





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Was risk ignored?

- Risk fiascos over the last few years might suggest so.
 - Trades gone bad on unprecedented scale
 - “Rogue trader” on unprecedented scale
 - Current financial crisis
- However...
 - Problems of unprecedented scale were absorbed (although the ultimate outcome of the financial crisis is still unknown)





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Then what went/is going wrong?

- Firms adapted to better risk transfer by taking bigger positions (safer cars and highways => people drive faster) – creating untested liquidity risk.
- Value of the instruments that effected the risk transfers was very opaque – creating untested transparency and model risk
- Broad acceptance of the risk transfer mechanisms led to a system that was tightly coupled in certain downside scenarios – systematic risk didn't disappear.



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Public and private challenges

- Private challenge to manage the adaptation to improved risk transfers.
- Private challenge to value liquidity risk appropriately.
- Public and private challenge to create appropriate incentives to assure liquidity.
- Public and private challenge to create transparency while balancing the value of transparency with the value of proprietary information. (Marginal benefit = marginal cost.)
- Public (and private?) challenge to evolve regulatory systems to deal with increasingly tight coupling.