

CITIZENS PROPERTY INSURANCE CORPORATION

**MINUTES OF THE
FINANCE AND INVESTMENT COMMITTEE MEETING
Tuesday, April 10, 2018**

The Finance and Investment Committee (FIC) of Citizens Property Insurance Corporation (Citizens) convened at the Sheraton Orlando North in Maitland, FL on Tuesday, April 10, 2018 at 3:00 pm (EDT).

The following members of the FIC were present:

Chris Gardner, Chairman
Gary Aubuchon
Bette Brown

The following members of the Board were present:

Blake Capps
James Holton
John Wortman

The following Citizens staff members were present:

Barry Gilway
Jennifer Montero
Barbara Walker
Andrew Woodward
Dan Sumner
Kelly Booten
Steve Bitar
Joe Martins
Jay Adams
Christine Ashburn
Mark Kagy
Michael Peltier
Stephen Guth
Carl Rockman

The following people were present:

Kapil Bhatia	Raymond James
Dave Newell	FAIA
Ken Vincent	Guy Carpenter

Call Meeting to Order

Barbara Walker took roll.

1. Approval of Prior Meeting's Minutes

Chairman Gardner made the motion to approve the April 19, 2018 Finance and Investment Committee (FIC) Minutes. Gary Aubuchon seconded the motion. All were in favor. Motion approved.

Chairman Gardner: We are to item two, market update. I would like to recognize Kapil Bhatia from Raymond James.

2. Market Update

Kapil Bhatia: Good afternoon, Mr. Chairman and Governors. There are currently 6.6 million people unemployed in the United States, while the unemployment rate is 4.1%. There are a total of 162 million civilians employed from a total civilian's population of 257 million and the labor participation rate is 62.9%. This is 4.4% less than the peak rate of 67.3% which translates to over 10 million people representing significant demographic changes and structural mismatch in our labor force over the last 15 to 20 years. The U6 unemployment rate is currently at 8% which includes part-timers looking for full time jobs and people under employed or marginally employed, again reflecting significant skill set mismatch in the labor force. If we add up all of these numbers there are potentially 15 to 16 million people available to join the labor force, and this is keeping the wages low. No pressure on the wage growth and inflation is low. After increasing rates once in 2015 and once in 2016, the Fed has increased rates three times more in 2017, March, June and December of 2017, and so far once in 2018. All of the six rate increases leaves the Fed fund rates currently at 1.5 to 1.75% compared to 25 basis points in December of 2015. And we project the Fed will increase rates at least once or twice more in 2018. However, with all of these increases the long term rates have not moved significantly, because Fed really has no control over the long term rates. Fed can control the short term rates, but significantly has no control over the long term rates. This increase in the short term rate has also narrowed the spread between two and 10-year Treasury. It was 1.26% right before the first Fed rate increase rate in December of 2015, to a current spread of 48 basis points as of today.

Again, the long term rates reflect global rates. So to put it in perspective, the two-year rate in U.S. is 2.31% compared to Germany at negative 60 basis points and Switzerland at negative 88 basis points. Looking at 10-year rates we are at 2.79% as of today compared to Germany at 52 basis points and Switzerland at one basis point, and that means there is potentially not much room for the long term rates to go up, regardless of what the Fed does in the short run. In addition, \$8.6 trillion of global debt is currently trading at negative yields and that means there is a lot of money sitting outside waiting to be invested in the U.S. fixed rate market, and partially it reflects the demographic changes as people are getting older, especially in Europe and Asia and the pension funds are investing more money in the fixed income market.

How does this affects us, it helps us on the reinsurance on the side and I will come back to that in a minute. Recent volatility in the stock market is basically noise. As markets are trying to price risk which is hard to quantify and therefore hard to price, and we hear about risk every day what is happening coming out of Washington, D. C. as well as the trade risk or whether it is some other noise, it is all noise and the market is going to have a hard time pricing that risk. We expect volatility to continue unless that risk goes away or at least the perception of that risk goes away. From a positive perspective, corporate earnings are expected to grow because of the recent tax changes and once the market figures out the noise we expect volatility to come down and markets to go towards upward trajectory.

Corporate bond markets have been strong, but we expect issuance to come down in 2018, because of reappropriation of cash from overseas, as municipal issuance is also expected to come down in 2018. Again, due to tax law changes which eliminated advance refunding. Looking at the risk transfer markets, the 2017 hurricanes caused approximately 10% of global reinsurance capital to go away. But most of that was absorbed by net income and it was not a capital event, the impact of this year's risk transfer pricing is going to be minimal, if any, at least for us. Most of the pricing impact we will see at the lower level where there were some losses incurred by some of the primary insurers. The overall reinsurance of pricing in 2018 is going to be almost similar to where the 2017 pricing was. We expect the cat bond market to be strong. We expect over \$10 billion of issuance this year, with \$6 billion maturing, we expect that the overall Cat Bond market at the end of this year to be \$35 billion and that is putting further pressure on the traditional reinsurance market and keeping the rates low. A couple of cat bonds were imported in 2017, however the total losses came out be only \$333 million. So the capital markets are strong and behaving rationally. Again, we don't expect much to change in our risk transfer rates. And lastly, the short term increase in interest rate is good for our investment portfolio as most of our portfolio is 10 years and under, and our income should go up at \$20 to \$25 million more in 2018, with some of the changes in investment policy as well as an increase in the short term rates. With that I will stop to see if there are any questions for me.

Chairman Gardner: Members, any questions? Thank you. Thank you, Kapil.

Kapil Bhatia: Thank you.

Chairman Gardner: Okay, we are to the third item, the reinsurance and layer chart update.

Jennifer Montero: Would you like the layer chart update first or the reinsurance update first?

Chairman Gardner: What is your pleasure, Jennifer?

Jennifer Montero: Let's do the layer chart first.

3. Reinsurance and Layer Charts Updates

Jennifer Montero: Citizens reinsurance plan considers and incorporates the transfer of hurricane risk in the coastal account to the global reinsurance market. In 2017 Citizens transferred more than \$1.3 billion of coastal account hurricane risk to the global market, which included \$350

million of coverage in the traditional wrap layer which sits alongside and above the Florida Hurricane Catastrophe Fund. \$580 million of traditional aggregate coverage of which \$180 million is multi-year, two limits over three years and \$400 million of single year coverage. Additionally, \$100 million of single year traditional coverage was purchased for the commercial non-residential book. Citizens also transferred \$300 million of risk transfer to the global capital market in the form of a three-year aggregate catastrophe bond. The proposed 2018 risk transfer program incorporates strategic elements from the continuation of existing risk transfer programs which includes the carryover of the 2017 multi-year traditional aggregate coverage of \$180 million and the \$380 million CAT bond. In addition, we are proposing \$183 million of traditional coverage alongside the mandatory layer of the CAT fund, and aggregate multi-year layer of \$400 million to be split between the traditional market and the capital market, and the \$250 million traditional aggregate single year layer to sit above the multi-year aggregate layers.

Citizens is also evaluating the transfer of \$100 million in losses in excess of \$235 million or right below the attachment of the CAT fund's mandatory layer. Citizens has never purchased reinsurance below the CAT fund attachment point. The cost of this covered layer may be relatively higher than the other risk transfer placements due to the lower placement within the capital structure. The attachment probability is 13.43%. The amount of reinsurance demand in this layer has also affected, has also been affected by the losses from 2017, and therefore, the pricing will be at a higher level on a risk adjusted basis. In addition, we are exploring two different tranches for the commercial and non-residential book. Both tranches are single year traditional coverage. The lower tranche attaches at \$78 million and provides approximately \$56.7 million of coverage. The second tranche attaches at \$267 million dollars and provides \$36 million of coverage. Citizens will evaluate the pricing quotes for these layers along with the other proposed layers and will determine the most cost effective risk transfer program that meets the objectives of transferring risk in order to cover up to the 1-in-100 year storm while minimizing the surplus exposed. We will have a separate Board teleconference in early May to present the proposed 2018 reinsurance program for the Board's consideration and approval. That completes my update on the layer chart. Any questions?

Chairman Gardner: Members, any questions for Jennifer? Okay.

Jennifer Montero: There is also, just to show, PLA/CLA layer charts are also included in your materials. The update for the reinsurance, we have been working with our co-brokers on the traditional side, Willis Re & Guy Carpenter. We completed the road show last month. We went to New York and Bermuda and then a trip to London. We expect the submission to go out later this week, and the reinsurers will have a time period to give us quotes back on those layers before we meet back together to come up with firm order terms. On the CAT bond side we have been working with our sole structuring agent which is Citibank and our joint book runner which is BAML and have had at least one offshore meeting and structuring meeting and we will be leaving next week for New York and Bermuda to start the road show for the CAT bond, and then the following week we will be in London and Zurich, and hopefully all of this will close early May.

Chairman Gardner: Great, any questions for Jennifer?

4. Citizens' Account History

Chairman Gardner: Okay. We are actually going to defer item four to the Board meeting tomorrow which is the Citizens' account history. For the benefit of the Board members we are going to revisit again why we have our current structure, what some of the complications are with that structure and some of the complications potentially combining that structure. So with that let's go to item five, which is the investments portfolio update, please.

5. Investment Portfolio Update

Jennifer Montero: Behind tab five you will find the summary update and then in the appendix you will find the full report. On slide one, the total portfolio is \$10.02 billion with \$8.8 billion being externally managed, and \$1.2 billion being internally managed. The taxable portfolio is \$8.07 billion or approximately 81%. The tax exempt portfolio is approximately \$1.95 billion or 19%. The total portfolio average duration is just over four years with 3% maturing in less than 90 days and 27% maturing between 90 days and three years. The total portfolio income return for one year is 2.31%. On slide two the rates for one, three and five year treasuries have been increasing over the last year, and currently as of yesterday are at 2.06%, 2.42% and 2.6% respectively. The tax exempt rates have also increased over the last year. On slide three, it is 88% or \$8.8 billion of the portfolio is externally managed by 15 taxable and/or tax exempt portfolio managers. Twelve percent or \$1.2 billion of the portfolio is internally managed, consisting of operating funds, debt service bonds and debt service reserve funds. The taxable and tax exempt portfolios both have very strong credit quality, 86% of the tax exempt portfolio are rated AA or higher and approximately 71% of the taxable portfolio is rated A or higher. Over 27% of the taxable portfolio is in Treasury and agency securities. And slide four, the total portfolio return summary has 2.31% of income return over the last 12 months and 1.94% over the last two years. And that completes my report unless there are any questions.

Chairman Gardner: I have got a quick question. What are you kind of estimating the investment income we are going to realize this year and how is that compared to the prior two years?

Kapil Bhatia: As Jennifer said, over the last two years our average return has been 1.94% and for the last 12 months was 2.31%. So last year was 60 basis points above the year prior, and this year we expect at least that to be income to be 25 to 30 basis points higher than where we were last year. Looking at our total portfolio so around \$10 billion. It should translate into about \$20 to \$25 million of additional income.

Chairman Gardner: Great.

Kapil Bhatia: The total return is volatile as the rates go up or down, but we are more income driven in our portfolio management. So we expect maybe at least \$20 to \$25 million more this year.

Chairman Gardner: Great, thank you, Kapil.

Kapil Bhatia: Thank you.

Chairman Gardner: Any other questions? Okay, let's go to item six, depopulation and Clearinghouse update.

Jennifer Montero: That is for informational, unless you want a report on it.

Chairman Gardner: I'll will defer to my colleagues.

Jennifer Montero: I think we made it informational and added it to FIC when we got rid of the depopulation committee.

Chairman Gardner: Okay.

Jennifer Montero: But if you would like us to go over it we are happy to do so.

Chairman Gardner: No, I think you confirmed that the market is pretty calm right now. There is not a whole lot of depop activity that is occurring.

Jennifer Montero: That is correct.

Chairman Gardner: Any other questions on that? Okay, I will take a motion to adjourn unless there is other new business.

Governor Aubuchon: So moved.

Governor Brown: Second.

Chairman Gardner: Thank you. Motion to adjourn.

(Whereupon, the proceeding were concluded.)