CITIZENS PROPERTY INSURANCE CORPORATION

MINUTES OF THE FINANCE AND INVESTMENT COMMITTEE MEETING

Tuesday, September 25, 2018

The Finance and Investment Committee (FIC) of Citizens Property Insurance Corporation (Citizens) convened at the Sheraton Orlando North in Maitland, FL on Tuesday, September 25, 2018 at 3:00 pm (EDT).

The following members of the FIC were present:

Gary Aubuchon, Chairman
Bette Brown (Telephonically)
Marc Dunbar (Telephonically)

The following members of the Board were present:

Blake Capps

The following Citizens staff members were present:

Barry Gilway
Jennifer Montero
Andrew Woodward
Dan Sumner
Kelly Booten
Steve Bitar
Joe Martins
Jay Adams
Christine Ashburn
Mark Kagy
Violet Bloom
Elaine Thomas
Michael Peltier
Barbara Walker

The following people were present:

Kapil Bhatia	Raymond James
Dave Newell	FAIA
Nathaniel Johnson	J.P. Morgan
Margaret Lezcano	UBS Financial Services
Coleman Cordell	Bank of America
Henry Reyes	J.P. Morgan
Doug Draper	Bank of America
Albert delCastillo	Greenberg Traurig

Call Meeting to Order

Barbara Walker took roll.

1. **Approval of Prior Meeting's Minutes**

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

Chairman Aubuchon: And we are on to item number two which is a market update and I will recognize Kapil Bhatia.

2. **Market Update**

Kapil Bhatia: Good afternoon, Mr. Chairman and Governors. Can you hear me okay on the phone, Governor Brown, Governor Dunbar?

Governor Brown: I can hear you, Kapil. Nice to hear you.

Governor Dunbar: Yes, I can hear you fine.

Kapil Bhatia: Thank you. So good afternoon again. For the record, Kapil Bhatia from Raymond James & associates. We are your financial adviser. I will quickly go through the market update. Please stop me at any point in time if you would like me to expand on any point. There are currently 6.2 million people unemployed, or the unemployment rate is 3.9%, which is only .1% above the lowest rate over the last 40 years. However, the labor force participation rate is still only at 62.7% compared to 67.2% in July of 1997. Effectively our labor participation rate is four and a half percent lower than where we were 20 years ago. Partially because of demographic changes in the population and partially because of the skill set mismatch in the labor force. However, this difference translates into approximately six to 10 million people available to join the labor force. The U6 unemployment rate which includes persons marginally attached to the labor force and those employed part time but looking for a full-time job is at 7.4%. If we add up all of the available people the difference between U6 and U3 labor force participation rate that translates into around 10 to 15 million persons available to join the labor force assuming either the skill set starts matching or people start coming back to the workforce as the wages start to increase. And that means we really don't have any wage pressure so far and you can see the wage numbers still growing only at two to two and a half percent and that means that inflation is still low, one of the reasons why inflation is so low. The feds have increased rates seven times since December of 2015, from zero to 2.25%, while the rates right now is between 2% to 2.25% and is again expected to increase one more time tomorrow. We expect an additional rate increase either in December or in March. Eventually the fed fund rate is getting closer to two and a quarter to two and a half or very close to the current inflation rate by the middle of next year. The current

10-year treasury is at 3.10%. We expect 10-year to get to three and a quarter and we also expect inflation to remain range bound where it is now, between two and a quarter to two and a half percent. So not much is expected in terms of the rates growing, increasing significantly larger or inflation increasing significantly larger. As the global growth is still low with eight trillion worth of sovereign global debt still trading at negative yields, and this is going to keep the U.S. rates low regardless of what you hear or see in the media. Simply because of the low inflation, available persons to join the labor force, as well as the global interest rates. Japanese and Euro's own growth rate is also very close to approximately zero. Japan at less than half a percent and Euro's growth at one percent while our growth is significantly higher partially because of the recent tax law changes as well as reappropriation of the foreign earnings coming back and being used for the productive resources. We expect 2018 growth rate to be around 3.2 to 3.4% which is one percent above the average of last five years which was 2.2%. Trade friction or trade war, whatever you want to call it, is an issue and we will have a marginal impact on our growth. However, that is estimated to be only .1%. Comparing it to the European and Chinese economy that means that the global growth rate will be much lower than it is right now than ours because of this trade war.

And lastly, the bond market issuance. In 2017, the corporate issuance was $1.67 trillion. Year-to-date issuance is $950 billion. We expect this number to be closer to $1.35 trillion reflecting lower issuance. Again, primarily due to reappropriation of foreign earnings. Municipal issuance is also low this year. Year-to-date is $224 billion compared to 2017 number of $400 billion or $408 billion to be exact. We expect this year's number to be $320 billion. Again, it is partially because of the tax law changes eliminative the advanced refunding's from the marketplace. Increase in short term rate which we are seeing, is going to help our investment portfolio. Our investment income to be at least $10 to $20 million higher this year with increase in short term rates. And then lastly, the reinsurance market is still strong even after projected losses from Irma from last year of $10 billion as well as Florence in the region of around $3 billion excluding the national flood program. We don't expect the reinsurance market to change significantly over the next couple of months unless there is a larger event or something like that, but if the market conditions remain where we are and no natural event, we expect reinsurance markets to remain where we are. With that I will stop unless you have any questions for me.

Chairman Aubuchon: Thank you, Kapil. Members, any questions of Kapil?

Governor Brown: I have none, but thank you, Kapil. Very interesting always.

Kapil Bhatia: Thank you, I appreciate it.

Chairman Aubuchon: Okay, hearing no questions we will move on to Jennifer Montero's next four items. We will start with risk transfer. Jennifer, you are recognized.

3. Risk Transfer Programs Updates

Jennifer Montero: Thank you. Behind tab three is a Power Point of our 2017 and 2018 layer charts. I am going to go through them and try to explain some of the recoveries. I would like to briefly walk you through the 2017 layer chart first. Given that we project some recoveries from the 2017 risk transfer program, this is a good opportunity to highlight some of the coverages and how they work. Citizens' layer chart is a visual representation showing the resources available to pay claims for a large wind event. The vertical access increases with storm size and this chart goes up to the 1-in-100 year storm. Citizens' purchases private reinsurance in the coastal account and like all other property insurers, Citizens must purchase coverage from the Florida Hurricane Catastrophe Fund. The left side of the chart shows coverage in the residential portion, both personal residential and commercial residential, and the right side of the chart shows the commercial non-residential coverage. The green blocks in the chart indicate losses which would be funded from surplus. We structured our 2017 risk transfer program so that all losses below a 1-in-11 year storm would be paid from surplus. You can think of it as a deductible. For the residential portion we have Cat Fund coverage, a traditional reinsurance coverage which wraps around the Cat Fund, hence why we call it a wrap, and then an $880 million layer of reinsurance which sits above the $350 million wrap. $300 million of the $880 million was placed in the capital market via a Cat bond. The remaining $580 million was placed in the traditional market as aggregate coverage. You also can see the CNR coverage in the amount of $200 million off to the right in the tan colored block.

Moving to slide three, this is the Irma estimated recoveries. This slide walks through the estimated coastal account residential risk transfer recoveries for Hurricane Irma. The blue diamonds show the trigger point for each of the risk transfer coverages. The green boxes represent our projection of Citizens' recoveries for Irma losses and loss adjustment expenses. We expect recoveries from the Cat Fund and the wrap, but do not anticipate payouts for Irma losses from the $880 million layer. The Cat Fund triggers based on loss only and then it pays 5% of loss as an allowance for loss adjustment expense. Our traditional coverage is triggered based on losses and actual LAE incurred, but then have inuring coverages which you see subtracted out in the blue diamond. The Cat Fund recoveries inure to the benefit of the wrap contract, meaning that the Cat Fund recoveries reduce the losses which will be covered by the wrap. The layer chart on slide two is a good visual of how recoveries work, but it is a simplification. Not only are LAE recoveries simplified, but the chart really only tells the story when there is a single large storm.

So moving on to slide four, this is what happens when we have multiple small storms. In 2017, in addition to Hurricane Irma, there were Tropical Storm Emily, Hurricane Nate and Tropical Storm Felip. And although the 2017 hurricane season officially began on June 1st of 2017 and ended November 30th of 2017, our risk transfer contracts run through the full year and end's on May 31st, 2018. So Tropical Storm Alberto which occurred at the end of May 2018, also falls within the last year's risk transfer program. These four storms are each projected to produce a relatively low level of losses, an aggregate total of $442,000 of loss in LAE. The traditional aggregate covers have lower attachment points, but also inuring covers, meaning that in order to meet the low attachment recoveries from other lower layer contracts such as the Cat Fund inure or are for the benefit of the traditional aggregate contract and potentially reduce payouts from the traditional aggregate contracts. On the other hand the Everglades Re Cat bond has a higher retention and no inuring coverage and attaches at $2.151 billion. All the covers in the $880 million layer have aggregate retentions and the losses from all the storms together need to meet the retention, not each individual storm. And because Irma met the retention the other four storms in aggregate do as well.

Moving on to the next slide. This is the 2018 layer chart. These next two slides are layer charts for the coastal account. The first one is personal residential, commercial residential, and then the second slide is the commercial non-residential. The risk transfer placements for 2018 include $183 million of traditional reinsurance alongside the Cat Fund at a gross rate online of 10.75%. $250 million of capital markets risk transfer through Everglades Re II at a gross rate online of 4.75%. $150 million of traditional reinsurance for aggregate multi-year coverage at a gross rate online of 6.6%. $300 million of traditional reinsurance for aggregate single year risk at a gross rate online of 5.25%, and $60 million of coverage for the traditional reinsurance for commercial non-residential risk with gross rate online of 5%. In addition we had multi-year coverage that carried over from the 2017 placement that consisted of $180 million of traditional reinsurance for aggregate multi-year risk, and $300 million of capital market risk transfer through Everglades Re II. The strength of Citizens and the marketing efforts in the traditional capital markets culminated an efficient pricing terms that enabled Citizens to transfer $1.42 billion of risk at a cost of approximately $89 million which has a weighted average gross rate online of 6.1%, while only exposing approximately 34% of Citizens' surplus in a 1-and-100 year event. And I will pause there for any questions.

Chairman Aubuchon: Thank you, Jennifer. Members, any questions? Okay, hearing no questions let's move on to our investment management services and that action item.

4. Investment Management Services [AI]

Jennifer Montero: Thank you. Behind, tab four is an action item from Investment Management Services. On May 3rd, 2018, Citizens released Invitation to Negotiate number 18-0018 for Investment Management Services. Responses were received and evaluated by an evaluation committee. The evaluation committee recommended award to vendors on August 24th, 2018. A listing of the vendors recommended for award and the notice of intent to award is attached as Attachment A. They include 10 taxable managers and four tax exempt managers. The action item seeks Board approval for Citizens to enter into contracts with multiple qualified vendors to provide Investment Management Services. This engagement requires selected vendors to make investment decisions that ensure strict compliance with Citizens' investment policies for taxable and/or tax exempt funds. Citizens has over $8.66 billion of total managed assets pursuant to its taxable and tax exempt investment policies that are focused on safety, stability, liquidity and competitive returns. The current breakdown of the $8.66 billion in assets is approximately 83% taxable, 17% tax exempt. Citizens' investment policies are reviewed at least annually and may be amended from time to time if deemed appropriate and necessary with approval from Citizens' Board. The estimated fees of $25,050,000 for the life of the contract include renewal terms is based on Citizens' current $8.66 billion managed portfolio. Fees will fluctuate based on the total market value of Citizens' assets. Yearly estimated fees of $4.17 million. Fees are based entirely on the total average annual assets under management. Fees will be calculated on the aggregate amount of assets. All assets up to $750 million will have a fee of five basis points. All assets above $750 million will have a fee of four basis points. And I will pause there for any questions before I read the recommendation.

Chairman Aubuchon: Members, any questions?

Governor Dunbar: Yes, this is Marc Dunbar. A quick question, Jennifer. How many of these are existing investment providers of ours?

Jennifer Montero: We have 15 currently and we lost seven. So we have eight existing and two new.

Governor Dunbar: Okay, thank you.

Chairman Aubuchon: Any other questions? Okay, Jennifer, please go ahead and read the recommendation.

Jennifer Montero: **Staff recommends that Citizens' Board of Governors (A) approve the contract including renewal period for Investment Management Services, ITN number 18-0018 to the list of vendors in Attachment A as set forth in this action item. (B) authorize staff to take any appropriate or necessary actions consistent with this action item. And (C) approve this action item for the three-year period and three optional one year renewals for fees based on the total average annual assets under management. All assets up to $750 million at five basis points and all assets above $750 million at four basis points for an estimated yearly annual fee of $4,175,000.**

Chairman Aubuchon: **Thank you, Jennifer. And Governors having heard the recommendation, do I have a motion?**

Governor Dunbar: **So moved.**

Governor Brown: **Second.**

Chairman Aubuchon: **Thank you. Thank you Marc and Bette. We have a motion and a second. Any further discussion? Any objection? Hearing no objection, let's show that motion approved** and we will move on to a consent item under tab five.

5. Reinsurance Advisory and Brokerage Services [CI]

Jennifer Montero: Thank you. The consent item is for Reinsurance Advisory and Brokerage services. It is contract renewals. The vendors are Guy Carpenter & Company, LLC and Willis Re, Inc. The purpose of the consent item is to obtain authorization for the first one year renewal of contract number 15-15-002-01 and 15-15-002-02 for Reinsurance Advisory and Brokerage services. The contract are the result of Invitation to Negotiate 15-0002 issued on July 1, 2015, for services related to reinsurance advisory and brokerage services. The resulting contracts were issued on December 31, 2015, and have two one year renewals. This will be the first of two one year renewal for each contract. And I will pause for any questions before I read the recommendation.

Chairman Aubuchon: Governors, any questions?

Governor Dunbar: This is Marc Dunbar. I have one quick question if I can.

Chairman Aubuchon: You are recognized.

Governor Dunbar: And this is just for my education. Is there a better time to -- and I certainly support the recommendation, but is there a time that is better to seek, to bid brokerage services when the market is favorable or does it matter? I mean, with the reinsurance market being very stable and favorable right now, is it a better time to bid brokerage services during this kind of time period, or does it not matter?

Jennifer Montero: Well, this is for the brokers, not the actual –

Governor Dunbar: Right.

Jennifer Montero: The price of the reinsurance is not real relevant. Do you want to make a comment, Kapil?

Kapil Bhatia: Sure. Certainly continuing with brokers is helpful for us to achieve the long term advantage of the reinsurance market which is what we are seeing now. So the softness in the reinsurance market is actually helpful with the consistency of the brokers and these are two of the largest brokers out there. So certainly that helps us to achieve the lowest rate which we have been able to achieve over the last couple of years.

Governor Dunbar: Right, that is what I figured. I just was curious if the actual fees that brokers charge changes based on a market or it really doesn't matter because it is what it is.

Jennifer Montero: Yes, our contracts with both vendors is a flat rate no matter what our placement is, you're not getting any more or less for how much we place or don't place.

Governor Dunbar: Okay, okay, great, thank you.

Chairman Aubuchon: Any further questions? Jennifer, please proceed to the recommendation.

Jennifer Montero: **It is recommended that Citizens Board, (A) approve the first one year contract renewal to Guy Carpenter & Company, LLC, and the first one year contract renewal to Willis Re, Inc. for Reinsurance Advisory and Brokerage services for a total amount of $3 million for both one year contract renewals. And (B) authorize staff to take any appropriate or necessary action consistent with this consent item.**

Chairman Aubuchon: **Governors, having heard the recommendation, do we have a motion?**

Governor Dunbar: **So moved.**

Governor Brown: **Move to approve.**

Governor Dunbar: **Second.**

Chairman Aubuchon: **Okay, we have a motion and a second. Any further discussion? Any objection to the motion? Hearing no objection, let's show that motion is approved.** And we will move on to our investment portfolio update.

6. **Investment Portfolio Update**

Jennifer Montero: Thank you. Behind tab six is our summary of Citizens' investment summary. On slide one, the total portfolio is $9.56 billion with approximately $8.66 billion being externally managed and $899 million internally managed. The taxable portfolio is $7.89 billion or 83%. The tax exempt portfolio is approximately $1.66 billion or 17%. The total portfolio average duration is marginally over four years with 3% maturing in less than 90 days and 22% maturing between 90 days and three years. The total portfolio income return for one year is 2.44%. On slide two, the rates for the one, three and five-year treasuries have been increasing over the last year and currently as of last Friday are 2.58%, 2.89% and 2.95% respectively while the yield curve is getting flatter. Tax exempt rates have also increased similarly over the last year. Turning to slide three, 91% of the portfolio is externally managed by 15 taxable and/or tax exempt portfolio managers. Nine percent of the portfolio internally managed consisting of operating funds, debt service funds and debt service reserve funds. Taxable and tax exempt portfolio both have strong credit quality, 86% of tax exempt portfolios in the money market fund are rated AA or higher, and approximately 82% of the taxable portfolio is in money market funds are rated A or higher. Approximately 30% of taxable portfolio is in the treasury and agency securities. And the final slide, slide four, total portfolio return summary is 2.44% of income return over the last 12 months, and 2.02% over the last two years. And I will stop there. And as a remainder, there is an appendix that is the full report, but the tab behind that and I will pause for any questions.

Chairman Aubuchon: Governors, any questions? I have one. The distinction on page 1 on the one year return of our total portfolio versus our income return, what is the distinction between total return and income return?

Kapil Bhatia: Governor, total return includes the mark to market changes if the rates go up or down. The total return goes up or down because it reflects where the rates are. As the rates have been going up, our total return may be less than our income return. What we really look for is the income return, because that is really what we are getting in cash. Our portfolio is hold to maturity most of it unless we need to sell some portion to pay claims. We look at the income return more closely, but we do report total returns.

Chairman Aubuchon: Thank you. Any other questions? Hearing none, are we going to -- just for information purposes the depop and clearing house update. Are there any questions regarding that?

Governor Dunbar: This is Marc Dunbar, just one quick question, Chairman. What is -- do we have a goal? I mean, where do we think, how low do we think we can get on depopulation?

Chairman Aubuchon: Steve, would you like to jump in there?

Steve Bitar: This is Steve Bitar for the record. You know, as it stands right now we are in the process as we regularly do of forecasting our policy counts and where we could potentially go. If you look at the depopulation numbers as they stand, there simply hasn't been much of an appetite whatsoever on the personal lines and the commercial lines. We have been consistent for the last 18 months or so at roughly 442,000 to 443,000 policies from a policy count perspective and really don't see any changes coming with regard to major shifts in the depopulation appetite. As you know, we support the programs, we work directly with the Office of Insurance Regulation and we meet with many of the carriers that participate from a depopulation perspective of a regular basis. And as it stands right now, the appetite with all that is going on with litigation, AOB, what is happening in south Florida specifically is keeping us pretty steady and we're not anticipating any major shifts or swings with regards to depopulation appetite.

Governor Dunbar: Mr. Chairman, may I ask a follow up?

Chairman Aubuchon: Absolutely.

Governor Dunbar: Steve, so with that in mind, let's say that the AOB is straightened out. Do we have internal modeling on where we think the depopulation will go if that issue is taken care of or taken off the table?

Steve Bitar: You know, I would tell you that it is probably premature for us to measure that at this point. When we look at the risks that is we have at Citizens and what the makeup is of our book of business quite frankly, it does support what is at Citizens belongs at Citizens. You look at policies with multiple claims, you look at mobile homes, you look at older homes. We really feel that the mix of policies that we have unless there are some major shifts in the market, for the most part are the policies that belong with us. So we would not predict quite frankly any kind of major shifts in our policy count as it currently stands unless something major occurred in the marketplace that we are not currently anticipating.

Governor Dunbar: I will ask this leading question and just a follow up. Is it an accurate statement to say that the AOB issue is preventing us from further depopulation?

Jennifer Montero: This is Jennifer. I would say one of the big issues that AOB is causing is large litigation hikes which affects our rates and other companies are able to recoup that litigation rate through rate filings and rate increases and we can't. We are capped at the 10% glide path. So as time goes on we are going to get more and more and more actually unsound and then we become very competitive. I am sorry, we don't become competitive. We become competitive that people want to come in and we will grow if that happens, but depop companies won't want us because they won't have the right rate for the risk.

Governor Dunbar: Got it. Thank you.

Jennifer Montero: Thank you.

Chairman Aubuchon: All right, any further questions. If there is no new business to come before the committee, I would entertain a motion to adjourn.

Governor Dunbar: Motion to adjourn.

Chairman Aubuchon: I will second that motion. Thank you all very much. The meeting is adjourned.

(Whereupon, the meeting was adjourned.)