

**T**HE INSURANCE BUSINESS IS all about managing risk, says UNITRIN INC. (UTR) President and CEO Don Southwell. Four days after graduating from Western Michigan University with a math degree in 1973, Southwell started as an actuary at Prudential Insurance Company of America (now PRUDENTIAL FINANCIAL INC. [PRU]). Rating risk for life insurance policies and pricing variable-annuity products gave him an understanding of the underpinnings of insurance that Southwell says he will never forget.

Southwell, 55, reports that he later oversaw all core lines of Prudential's traditional individual insurance business — property, casualty and life — and joined Unitrin in 1996 as head of its Life and Health Insurance Group. He says he became CEO in 2006 after serving as the financial-services company's president and COO for four-plus years. Unitrin reports that its 6 million policyholders and consumer-finance customers provide more than \$2.7 billion of annual premium and consumer-finance revenues.

Unitrin's expansion strategy has always involved taking risks, Southwell says. As an example, he points to the 2002 acquisition of Kemper Auto and Home during a severe downturn in the property-casualty market. Following a sector rebound, Southwell explains, the businesses included in that acquisition now contribute some \$700 million annually in premiums.

Unitrin's approach to risk is also reflected in how it invests, spreading cash holdings between highly liquid, low-risk bonds and more aggressive equity investments to generate strong total returns, notes Southwell. "Striking the balance between conservatism and risk-taking is what separates successful businesspeople from those who are less successful," he adds.



# BALANCING RISKS

*Don Southwell sees risk management as the key to business success.*

BY NELSON WANG

## » How does Unitrin assess risk when deciding which new insurance markets to enter?

Insurance is state regulated, so we look for a regulator that wants to take care of the state's consumers through a market-based approach to the business. We view that more favorably than someone who wants to manage the market through price controls.

We're currently in some 40-plus states, and our goal is to be in enough regions to take a nationwide approach to the market. We'd like to ensure that we can match up with 85 percent or more of our potential buying public. When it comes to expanding your market, avoiding mistakes is often as important as hitting home runs. But you can't get obsessed with that. We took a risk when we bought Kemper, which worked out well. Catastrophe risk isn't something that we shy away from if we can price it appropriately and manage our concentrations. So it isn't that we don't take risks, but we make sure they are wise risks and that we can afford to take them.

## How did Unitrin fare with claims related to Hurricane Katrina?

One thing we work hard at is minimizing our risk concentration — we use computer models to simulate storms and other catastrophes such as earthquakes. We know where we've got concentrations of exposure, and we buy reinsurance to take some of the peaks off our losses in really bad storm years. So we actually came through

Katrina pretty well. Unitrin paid out over \$100 million in claims and wind-pool assessments, but a large chunk of that was reinsured.

## What has Unitrin learned about selling auto insurance directly to consumers via telephone and the Internet?

When we started out in 2000, we knew that the direct-sales business was a long-term proposition. A big chunk of auto-insurance policies are purchased directly by consumers each year, especially younger consumers. We learned to be flexible and change with the times. We've shifted our ad spending away from direct mail and put more into television and especially the Internet.

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More people buy through the Internet than we had anticipated, and the customers are better, in terms of both retention and loss experience.

## Before becoming CEO of Unitrin, you were president and COO. How did you plan for your new role?

A number of experiences over the years prepared me for the new post. I had direct hands-on exposure to each of our major

businesses and was placed on the board of directors a few years back, so I got a first-hand look at our governance structure. When the time came to become CEO, I was intimately familiar with every aspect of this company, and it was a story of continuity. I would hate to be a CEO who stepped into a situation where I didn't know the people and the businesses. You could wreak a lot of havoc before you figured it out, and people want you to move fast.

## What major changes will the insurance industry see over the next five years?

Technology has enabled lots of changes in the way we interface with insurance agents and consumers. We're investing heavily in technology, including our Unitrin Direct Website as well as a tool that allows our independent agents to instantly access price quotes and process transactions. That's because we believe the ease of doing business made possible by technology is very important and is going to become even more so. Technology will also drive the market shift toward direct purchasing by consumers, primarily in the more commodity-like businesses such as auto insurance.

Also, as we understand our customers better and delve into customer data more, we can match our pricing with the risk characteristics of each individual. For example, if people want to live on the coast, they ought to bear the risk of hurricanes and related events. Why should someone in Manhattan pay for insurance on somebody's condominium in Palm Springs? So the better we match our pricing with the risk, the more we influence behaviors that affect the cost of insurance, and that's a good thing. □