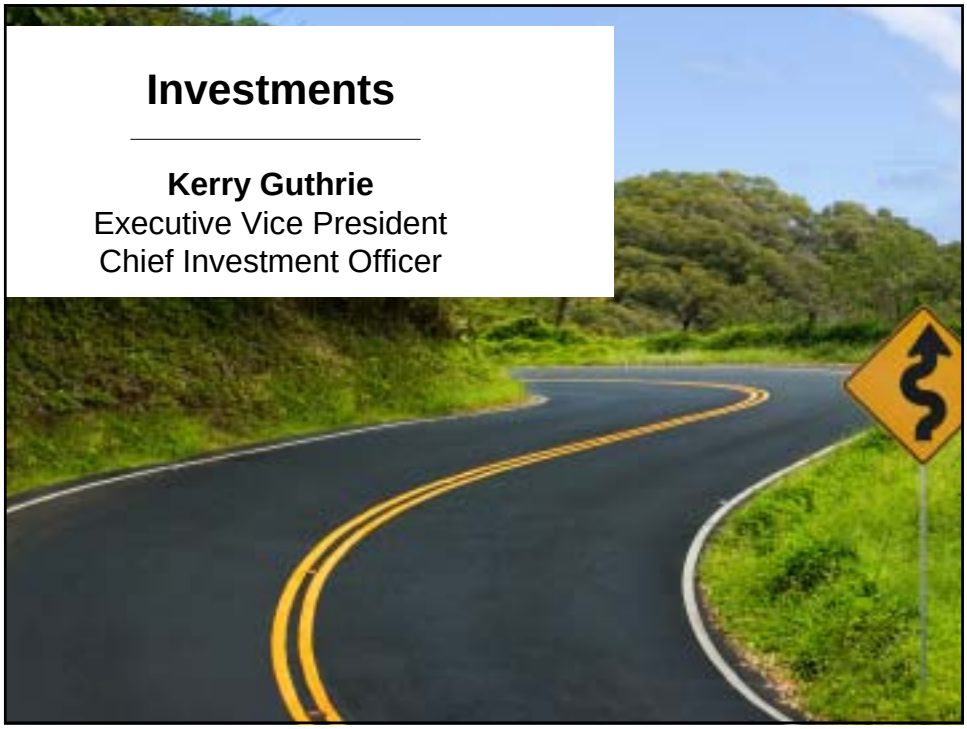


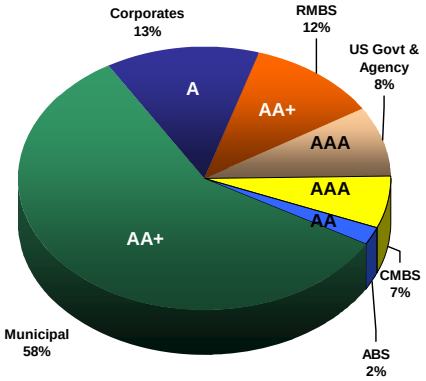
Investments

Kerry Guthrie
Executive Vice President
Chief Investment Officer

High Credit Quality Bond Investment Portfolio

As of February 28, 2009

$3.1 billion market value, 84% of overall portfolio



"AA+" average portfolio rating

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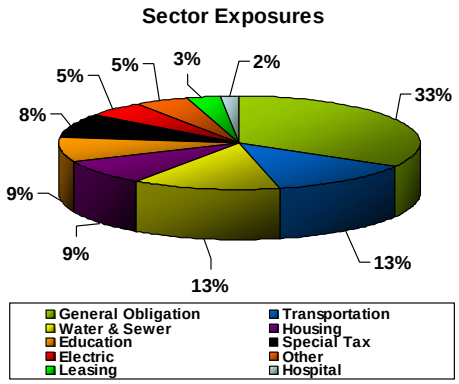
Municipal Securities – February 28, 2009

- $1.8 billion market value, 49% of overall portfolio
- "AA+" rated ("AA" without insurance enhancement)



Challenges

- Significant revenue shortfalls
- State & local budget pressures
- Weakening credit profiles
- Ratings turbulence

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Municipal Observations

- Comfortable with underlying credit quality, which remains very high
- First quarter actions:
  - $1.3 billion reclassified to held to maturity (HTM)
  - $500 million AFS highest quality bonds, most liquid names
  - Sold $39 million of state general obligation bonds
- Underweight potential troubled spots (CA, MI, OH)
- Significant portfolio diversification by geography/sectors

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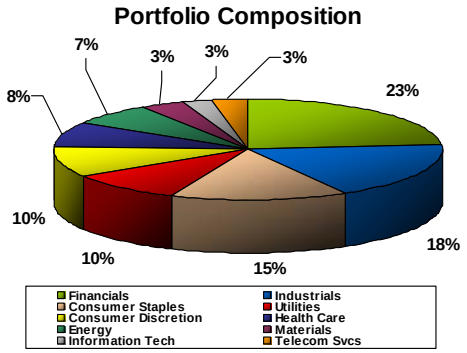
Corporate Bonds – February 28, 2009

- $407 million market value, 11% of overall portfolio
- Average rating "A"



Challenges

- Capital market access
- Declining corporate earnings
- Ratings turbulence

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Corporate Bonds Observations

- New purchases
  - Limited financing needs
  - Recession resistant companies
  - Strong balance sheets
  - Avoiding troubled sectors
  - Focused on short duration paper
- No "Big 3" auto exposure
- Underweight financials and cyclicals
- Portfolio is high quality and has performed well

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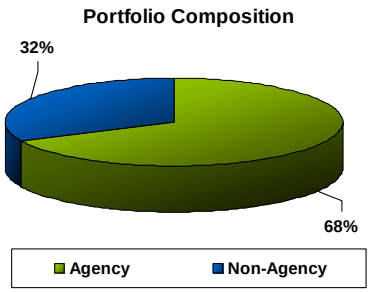
RMBS and RABS Securities – February 28, 2009

- $352 million market value, 10% of overall portfolio
- High quality ratings profile, "AA+" average rating



Challenges

- Unemployment continues to rise
- Home values continue to fall
- Illiquid non-agency RMBS market
- Ratings turbulence
- Regulatory/Political risk

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RMBS and RABS Observations

- Total Prime RMBS portfolio – "amortizing effect"
  - Received $56 million in principal paydowns in 2008 – 15% of portfolio
  - Averaging $14 million in principal paydowns per quarter
- Prime Non-agency RMBS under pressure
  - Received $23 million in principal paydowns in 2008 – 17% of portfolio
  - $113 million, 13% of stockholders equity
  - Average FICO score 726
  - Average loan-to-value (LTV) ratio 67%
  - Average market evaluation $62

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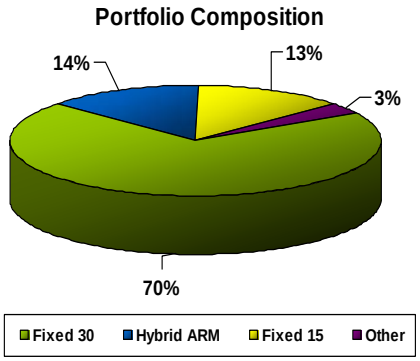
Alt-A RMBS Securities – February 28, 2009

- $41 million market value, 1% of total portfolio
- "AA" average rating
- Predominantly fixed-rate loans



Challenges

- Refinancing risk
- All Alt-A's viewed negatively
- Illiquid market
- 2006 vintage issues
- Rating downgrades

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Alt-A Observations

- Total Prime Alt-A portfolio
  - No Alt-A purchases after 3rd quarter 2006
  - Unrealized loss $38 million
- Alt-A 2006 vintage:
  - $25 million, 60% of total Alt-A, 3% of stockholders equity
  - Average FICO score 710
  - Average loan-to-value (LTV) ratio 73%
  - Average market evaluation $42
  - Unrealized loss $34 million

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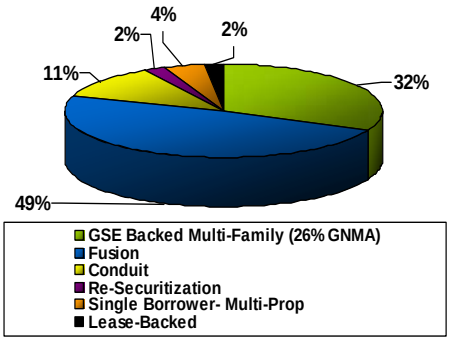
CMBS Securities – February 28, 2009

- $209 million market value, 6% of overall portfolio
- High quality ratings profile, Average rating "AAA"
- Diversified portfolio

Portfolio Composition



Challenges

- Corporate bankruptcies rising
- Weak operating conditions
- Declining property values
- Refinancing risk
- Subordinated classes

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CMBS Observations

- Actions taken in first quarter:
  - Sold $65 million
  - Purchased $23 million GNMA-backed project loans
  - Reduced exposure by 20%
  - $100 million reclassified to HTM
- $11 million principal paydowns received in Q1 2009
- Received $18 million in principal paydowns in 2008
- $12 million in unrealized losses

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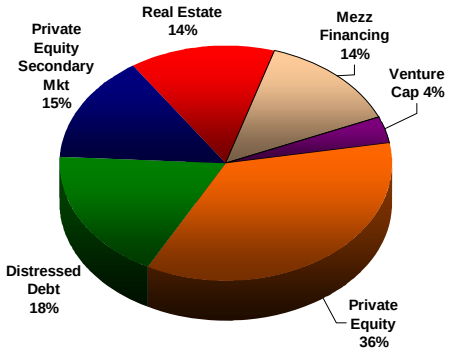
Alternative Investments – December 31, 2008

- $165 million market value, less than 5% of portfolio
- Alternative investments outperformed S&P 500 by:
  - 2,700 bps in 2008
  - 1,000 bps since 1997 on an annualized basis



Challenges

- Global financial asset decline
- Accounting = Earnings volatility
- FAS 157 adding more volatility
- Credit crisis = low M&A
- Quarter lag in reporting NAVs
- Illiquidity

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Alternative Investment Observations

- No new commitments planned
- Private equity structure, no hedge fund exposure
- $119 million unfunded commitment at 12/31/08
- Expect some reduction in unfunded commitment from a few general partners
- Distribution and contributions have slowed significantly
- Awaiting 12/31/08 net asset values

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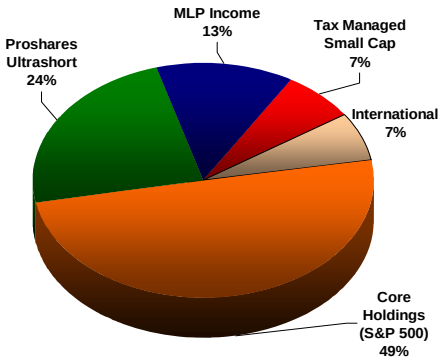
Equity Securities – February 28, 2009

- $114 million market value, 3% of total portfolio
- Equities outperformed S&P 500 for last nine years



Challenges

- Current bear market
- Extreme volatility
- Decline corporate profits
- Limited earnings visibility
- Regulatory/political risk

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Equity Observations

- Actions taken in the first quarter:
  - Further sales reduced gross equity exposure to approximately $90 million
  - Including the hedge, net equity exposure of approximately $50 million or only 1.4% of invested assets, 6% of stockholders equity

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Investment Strategy for the Current Environment

- Recognition of current high risk investment environment
  - Preservation of capital is paramount
  - Increased allocation to government and agencies
  - Investment grade corporate bonds
  - Actively reducing portfolio risk where appropriate

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Selective's Investment Philosophy

- Conservative buy & hold strategy
- Fundamental analysis driven decision-making
- Value-oriented investment style
- Investing for the long-term
- Confidence in the strength of our investment portfolio

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