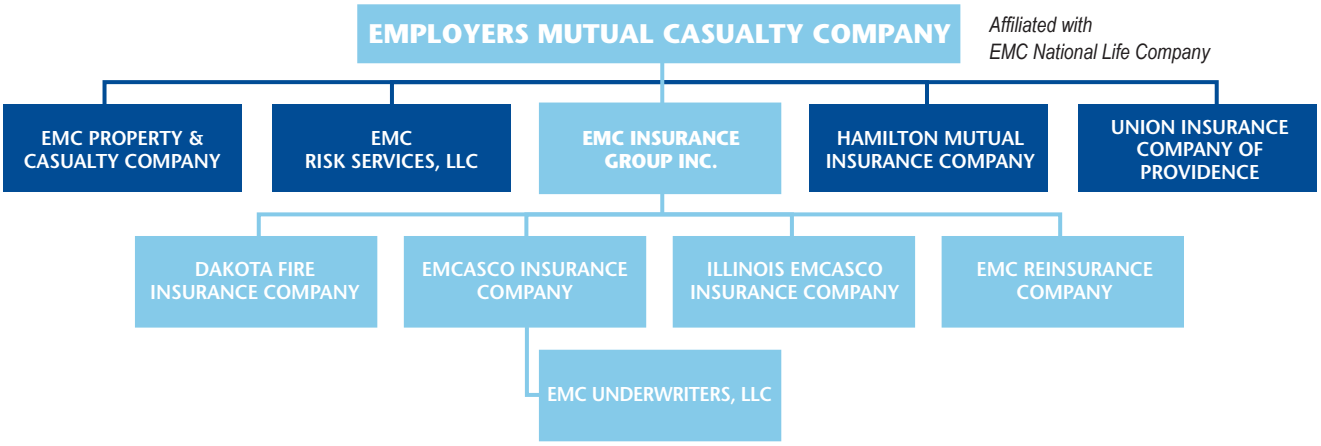
2011 Annual Report

EMC Insurance Companies



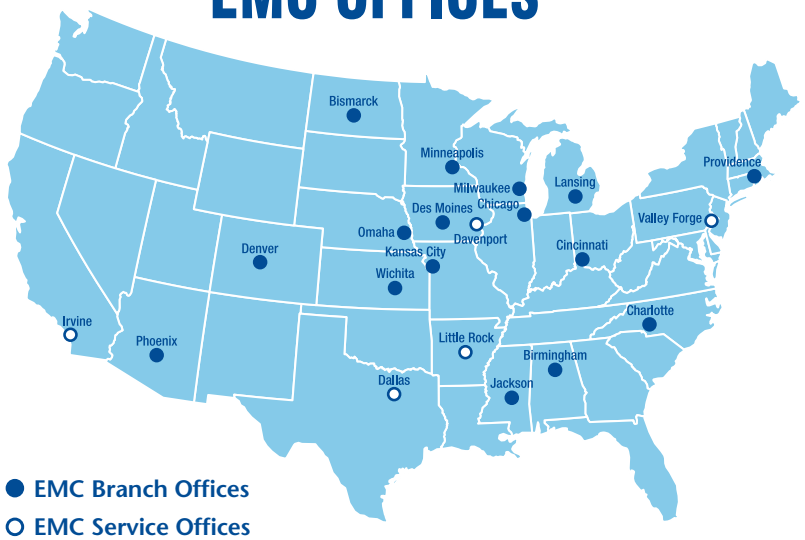
CORPORATE PROFILE

EMC Insurance Group Inc. (EMCI) is a publicly held insurance holding company with operations in property and casualty insurance and reinsurance. EMCI was formed in 1974 and became publicly held in 1982. The Company's common stock trades on the NASDAQ OMX Global Select Market tier of the NASDAQ OMX Stock Market under the symbol EMCI. EMCI is a controlled company in that its parent owns greater than 50 percent of its outstanding stock. As of December 31, 2011, EMCI's parent company, Employers Mutual Casualty Company, owned 61 percent of EMCI's outstanding stock and public stockholders owned the remaining 39 percent. EMCI has no employees of its own.

Employers Mutual Casualty Company (EMCC) is a mutual insurance company founded in 1911 and is headquartered in Des Moines, Iowa. EMCC employs more than 2,100 people countrywide and markets its products exclusively through a network of independent insurance agents. EMCI and EMCC, together with each entity's subsidiary and affiliated companies, operate collectively under the trade name EMC Insurance Companies.

EMC Insurance Companies (EMC) writes property and casualty insurance in both commercial and personal lines, with a focus on medium-sized commercial accounts. Reinsurance business is also written, with an emphasis on property business. Products and services are offered through independent insurance agents who are supported by a network of 16 local branch offices. EMC is licensed in all 50 states and the District of Columbia and actively markets insurance products in 42 states; however, the majority of its business is generated in the Midwest.

EMC OFFICES



Dear Stockholders:

If ever there was a year to step back and contemplate the myriad of reasons for doing what we do, it was 2011. Our parent organization, Employers Mutual Casualty Company, celebrated its centennial anniversary – 100 years of continuous service to its policyholders and independent insurance agency partners. We, as the publicly traded arm of that organization, prepared to celebrate our 30th anniversary as a NASDAQ OMX – listed company and what that degree of longevity means to our stockholders and the value reaped from their investment in our company. Celebrations of both milestones have been long in the making for what promised to be a year-long celebration of accomplishment.

But 2011 was much more than just a time to celebrate accomplishments – it was one of those defining moments in time when we were challenged to PROVE who we are and how we add value to all our stakeholders, including our policyholders, our independent agency partners and our stockholders.

In 2011, there were 171 catastrophe events in the United States of America resulting in just under $36 billion in insured losses. These events overwhelmingly included thunderstorms and tornadoes such as the devastating events in Tuscaloosa, Alabama; Joplin, Missouri; and Springfield, Massachusetts. They also included Hurricane Irene, which resulted in $5.5 billion in damages over much of the eastern coast of the United States, unusually severe winter storms throughout the central and eastern United States and wildfires in the southeastern and western United States.

As devastating as the losses were in the U.S., there was no comparison as to the global damage due to catastrophe losses such as Japan's earthquake and subsequent tsunami, New Zealand's earthquakes and Thailand's flooding. Global insured losses in 2011 totaled $105 billion and the total global economic losses as a result of these catastrophes were $380 billion.

For our company, catastrophe losses in 2011 totaled $80 million or $4.04 per share. Catastrophe losses added an astonishing and unprecedented 19.3 percentage points to our combined ratio – the second new record in four years. Both our property and casualty segment and our reinsurance segment were affected by record-setting losses in 2011. As a result, the Company experienced a net loss of $2 million or $0.16 per share and reported a GAAP combined ratio of 115.1 percent.

Though we never enjoy reporting net losses, we are very proud of the fact we were there to assist our policyholders in putting the pieces of their lives back together again. We were in Tuscaloosa; we were in Joplin; we were in Springfield; and we were in many of the eastern communities affected by Hurricane Irene. We also had claims from Japan as that nation dealt with its greatest disaster in a very long time.

Despite claim counts being up significantly in 2011, our claims staff increased less than one percent with no decline in claims efficiency or service. As a result of our local presence and de-centralized structure, our claims representatives were quickly on site following all major events and readily available - providing expeditious service to our claimants. To us, exceptional service remains a crucial part of our core values. It's what we do – it's who we are.

Catastrophes certainly dominated our discussion in 2011, but it clearly was not the only topic on our radar screen. The industry as a whole has been somewhat depressed due to weak economic conditions and declining premium rates for several years. In 2011, however, we achieved rate level increases across all lines of business, especially in our personal lines. Personal lines rates have been increasing for several quarters and have begun to move rates to more adequate levels. Commercial lines rate increases have not been as prominent, but are currently moving in a positive direction. For the first time in six years, our overall rate levels increased for all major commercial lines of business.

Net written premiums increased 8.6 percent in 2011. In the property and casualty insurance segment, commercial lines net written premiums increased 7.5 percent for the year, and in personal lines, net written premiums increased 6.0 percent for the year. The greatest increase in net written premiums was in the reinsurance segment. Those premiums increased 13.7 percent for the year as a result of increased participation in the MRB pool, an increase in both facility business and reinstatement income, and improved pricing.

Retention remained high in all lines of business. Commercial lines retention averaged 88 percent and personal lines retention averaged 89 percent.

Our investment income decreased 6.8 percent in 2011 due to a decline in the annualized yield of the Company's fixed maturity portfolio over the last few years and an increase in short-term investments. We are actively addressing this issue by investing in new types of securities, such as master limited partnerships, which yielded approximately six percent in 2011. We continue to monitor potential investments carefully. We have no direct European sovereign debt exposure. We do, however, have some European exposures within our investment portfolio, including investments in highly rated European banks in Great Britain, Switzerland and Germany, but we have no investments in France, Portugal, Italy, Ireland, Greece and Spain.

Our balance sheet remains strong with invested assets of $1.1 billion, total assets of $1.2 billion and stockholders' equity of $359 million.

In 2011, the Board of Directors increased our quarterly dividend to $0.20 per share and authorized a new $15 million stock repurchase plan to enhance stockholder value.

Looking ahead, we expect personal lines rates to continue increasing at a moderate pace, especially in the homeowners' line of business. Despite the high level of catastrophe losses experienced by the industry in 2011 and the continuing low interest rate environment, we do not expect a quick turn-around in commercial lines premium rate levels, but rather, we expect steady, meaningful improvement throughout the year. Reinsurance rates are expected to increase for the January 1 renewals and then remain steady for the remainder of the year. Our overall expectation is that net written premium growth will be in the mid- to upper-single digit range.

On the economic front, we expect the economy to continue to improve moderately in 2012. Investment income will likely decline again in 2012 due to the persistent rate environment, but we expect the decline to be less than what we experienced in 2011. And, we expect to return to profitability assuming we don't have a recurrence in catastrophe losses similar to 2011.

2011 was a time of personal celebration for past accomplishments, but more importantly, it was a time to shine at what we do best – provide the financial assistance to rebuild the businesses, homes, and lives of the people we serve when they are faced with devastating challenges.

Thank you for your continued interest in EMC Insurance Group Inc.

Sincerely,

Bruce G. Kelley
President &
Chief Executive Officer

Ronald W. Jean
Executive Vice President of
Corporate Development

Kevin J. Hovick
Executive Vice President &
Chief Operating Officer

Financial Highlights

($ in thousands)	2011	2010	2009	2008	2007
Revenues	$ 463,341	$ 439,395	$ 432,525	$ 438,348	$ 442,086
Realized Investment Gains (Losses)	$ 9,303	$ 3,869	$ 17,922	$ (24,456)	$ 3,724
Income (Loss) Before Income Taxes	$ (10,007)	$ 42,445	$ 62,525	$ (10,290)	$ 58,919
Net Income (Loss)	$ (2,098)	$ 31,346	$ 45,371	$ (1,705)	$ 42,478
(per share)					
Net Income (Loss)	$ (0.16)	$ 2.40	$ 3.44	$ (0.13)	$ 3.09
Catastrophe Losses	$ 4.04	$ 2.10	$ 1.55	$ 2.52	$ 1.37
Dividend Paid	$ 0.77	$ 0.73	$ 0.72	$ 0.72	$ 0.69
Book Value	$ 27.86	$ 28.52	$ 26.11	$ 21.32	$ 26.15
($ in thousands)					
Average Return on Equity (ROE)	-0.6%	8.8%	14.5%	-0.5%	12.7%
Total Assets	$ 1,230,459	$ 1,187,795	$ 1,165,788	$ 1,108,099	$ 1,202,713
Stockholders' Equity	$ 358,768	$ 368,641	$ 342,418	$ 282,916	$ 360,352

Common Stock History

	2011			2010		
	High	Low	Dividend	High	Low	Dividend
1st Quarter	$ 25.90	$ 21.48	$ 0.19	$ 23.08	$ 19.96	$ 0.18
2nd Quarter	25.40	18.59	0.19	24.89	20.84	0.18
3rd Quarter	20.38	16.45	0.19	22.75	20.11	0.18
4th Quarter	21.41	17.10	0.20	23.39	21.00	0.19
Close at Dec. 31	20.57			22.64		

Cautionary Statement

FORWARD-LOOKING STATEMENTS: The Private Securities Litigation Reform Act of 1995 provides issuers the opportunity to make cautionary statements regarding forward-looking statements. Accordingly, any forward-looking statement contained in this report is based on management's current beliefs, assumptions and expectations of the Company's future performance, taking into account all information currently available to management. These beliefs, assumptions and expectations can change as the result of many possible events or factors, not all of which are known to management. If a change occurs, the Company's business, financial condition, liquidity, results of operations, plans and objectives may vary materially from those expressed in the forward-looking statements. The risks and uncertainties that may affect the actual results of the Company include, but are not limited to, the following:

- catastrophic events and the occurrence of significant severe weather conditions;
- the adequacy of loss and settlement expense reserves;
- state and federal legislation and regulations;
- changes in the property and casualty insurance industry, interest rates or the performance of financial markets and the general economy;
- rating agency actions;
- "other-than-temporary" investment impairment losses; and
- other risks and uncertainties inherent to the Company's business, including those discussed under the heading "Risk Factors" in the Company's Annual Report on Form 10-K.

Management intends to identify forward-looking statements when using the words "believe," "expect," "anticipate," "estimate," "project," or similar expressions. Undue reliance should not be placed on these forward-looking statements.

Common Stock

EMC Insurance Group Inc.'s common stock trades on the NASDAQ OMX Global Select Market tier of the NASDAQ OMX Stock Market under the symbol EMCI. As of February 24, 2012, the number of registered stockholders was 867.

There are certain regulatory restrictions relating to the payment of dividends by the Company's insurance subsidiaries. (See note 6 of Notes to Consolidated Financial Statements in the Company's 2011 Form 10-K) It is the present intention of the Company's Board of Directors to declare quarterly cash dividends, but the amount and timing thereof, if any, are determined by the Board of Directors at its discretion.

Dividend Reinvestment and Common Stock Purchase Plan

A dividend reinvestment and common stock purchase plan provides stockholders with the option of receiving additional shares of common stock instead of cash dividends. Participants may also purchase additional shares of common stock without incurring broker commissions by making optional cash contributions to the plan and may sell shares of common stock through the plan. (See note 13 of Notes to Consolidated Financial Statements in the Company's 2011 Form 10-K) Effective March 14, 2012, the Company has temporarily suspended the issuance of shares of common stock under the dividend reinvestment and common stock purchase plan due to the late filing of an amendment to a Current Report on Form 8-K with the Securities and Exchange Commission. The Company intends to resume the issuance of shares of common stock under the plan at such time that all required reports have been filed in a timely manner with the Securities and Exchange Commission. More information about the plan can be obtained by calling American Stock Transfer & Trust Company, LLC, the Company's stock transfer agent and plan administrator.

Stockholder Services

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Transfer Agent
American Stock Transfer & Trust Company, L5.L5.r2(

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