First Monetary Mutual Limited

Twenty-Sixth Annual Shareholders Meeting
Friday, 10th June 2011
The Fairmont Southampton Princess Hotel
Southampton, Bermuda

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Chartered in 1986, First Monetary is a Bermuda based mutual insurance company owned and operated by commercial banks, savings banks and savings and loan associations in the states of New York and Pennsylvania. Two distinctively unique Bermuda symbols serve as marquees for First Monetary's Annual Shareholder's meeting. The Longtail Tern, a native bird, connotes beauty and freedom. The Bermuda moongate, a coral-stone arch shaped like a full moon, conveys unity, peace and happiness.

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President's Report
Play It Again

Last year this time, we assembled here to reflect fondly on the first 25 years of this company's history and our joint accomplishments. The 2011 annual meeting and presentation reorients the focus from retrospective to prospective. We'll compare and contrast First Monetary's past and present circumstances as we outline the plan we now envision to "Play it Again" and carry forward our string of successes.

Francis J. Shashaty
President & CEO

Let me elaborate on the "Play it Again" reference a moment, and comment on its applicability in current context. Today's financial industry finds itself mired in a financial crisis not completely unlike the one that existed at FM's inception in 1986. Since problems in the real estate market surfaced in 2008, over 300 banking institutions, some widely respected, global firms have completely collapsed. Sitting down to this meeting today, over 950 additional institutions have made the government's troubled bank list.

The same agencies that in go-go years of the decade pushed questionable lending and assured us of the system's integrity under their watchful oversight now express pained and feigned shock somewhat reminiscent of that scene in Casablanca when authorities articulated suspicions that gambling was being conducted in the casino. NOW - regulators, analysts and litigants offer up a "usual suspects" list of greedy, incompetent and overpaid management as the root cause of losses, and unsurprisingly profess that only greater oversight can fix it.

Not mentioned anywhere in the dialogue is one key factor that distinguishes collapsed companies from their surviving counterparts -- the scope of the latter group's commitment to sound risk management. FM's own resilience in the face of adversity testifies to the veracity of argument in favor of it.

For the past 25 Bermuda sessions, FM's annual reports have been filled with references to the "rear view mirror" underwriting philosophies employed by major commercial insurance companies. We've consistently held that underwriting insurance risk and pricing D&O insurance based solely on the most recent CAMEL rating is like driving a car while looking only in the rear view mirrors. Sooner or later, you'll crash into something right in front of you, something you would have readily seen had you been looking where you should have -- forward. First Monetary has always kept our eyes open for risks that lie ahead, where they remain. That, combined with our strict adherence to underwriting fundamentals, has kept FM in position to "Play it Again" – and again – and again.

Distilled down to basics, the following sections provide a snapshot overview of current market conditions, financial highlights and risk management actions.

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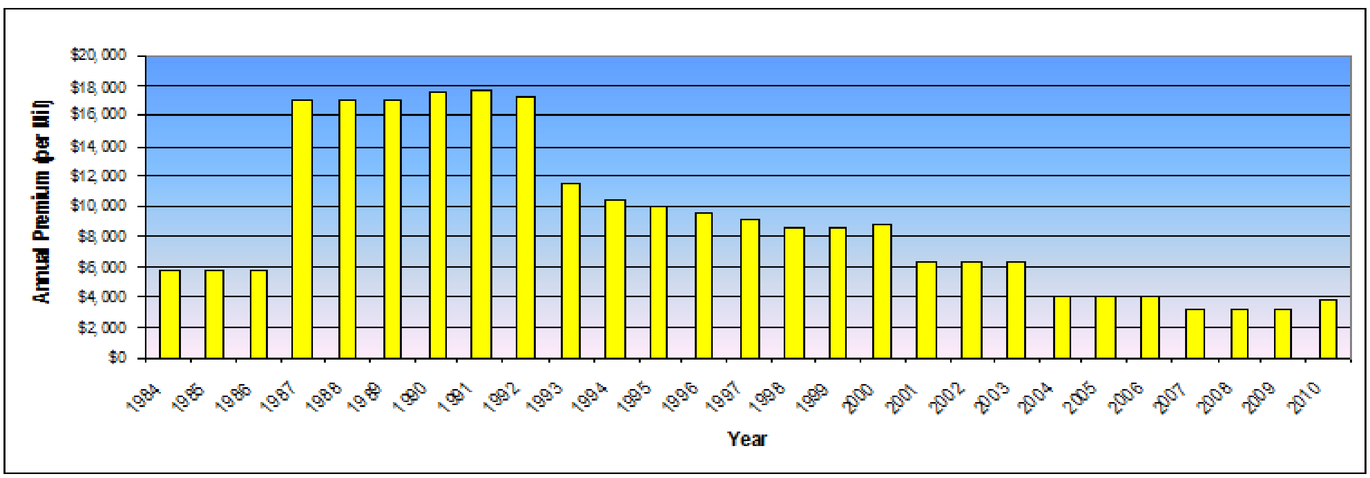
President's Report

Play It Again

The D&O Market Past and Present

At the time of FM's inception, the entire community bank market was lumped together and viewed through a single lens. Such treatment left EVERY institution impacted by the 80's D&O insurance lines crisis. The following chart illustrates the cost for $1M of primary commercial D&O insurance from 1984 (pre-crisis) through 2010 for an A-rated FM Member institution. The chart reflects pure cost, and does not account for changes in coverage provisions. As you can see, the cost per million increased over 200%, in 1987, BUT DID NOT provide coverage for claims initiated by regulators ("Regulatory Exclusion" was added by issuing carrier).

Commercial Market - Historic Rate Per Million for a CAMEL 1 - A Rated Member Institution



FM's 2009-10 underwriting cycle index calculated a 54% probability that the insurance market would begin turning hard in 2010. While commercial D&O markets tangentially flirted with moves in that direction this year (some insurers issued restricted term contracts and others refused to reduce or modestly increased expiring premiums), the overall market for NY and PA community banks remained stable to competitive during the first three quarters of 2010.

Examining things as they stand today, one thing has clearly changed. The one-dimensional market for community bank purchasers that existed in 1986 has now fragmented into multiple underwriting slices. Today's economic crisis and its resulting impacts on insurance availability are being felt more selectively by this market. C, D & E - rated institution are seeing rate increases, sometimes significant, while premiums paid by A & B - rated institutions remain at record lows.

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Play It Again

2010 Financial Highlights

Our "Play it Again" song echoes a familiar chorus this year. Results can be very briefly summarized as follows:

- FM will pay its fourth consecutive dividend and post its sixth consecutive profitable year.
- Interest income experienced a modest decrease as earnings continued to provide little return and rates continued their pattern of decline.
- PMI income tallied $205,271 in 2010 after returning $211,000 in 2009... Income appears to have stabilized at this level and is expected to be flat over the new forecast period.
- FM Membership remains essentially static and is presently open to only C or better rated institutions
- A premium stabilization fund remains in place four full years after what was anticipated to be its exhaustion date. The current balance exceeds $500,000 and remains still available for use as an offset to higher than expected losses or a ready reserve for windup expenses.
- Significant results and key initiatives pertaining to expenses are summarized below. Costs have been effectively capped by PROPHET plan actions that began to be introduced in 2004. While costs have seen some annual variation, overall figures have been reduced approximately $120,000.
- **Director's Reimbursement Expenses:** Expense reimbursements have been restricted in accordance with the approved business plan. Reimbursements for the special 25th anniversary meeting were increased to $800, but will be reset to the 2009 level of $400 in 2011.
- **2010 Underwriting/Service Fees:** Rex Wyon Services maintained it's voluntary fee reduction during 2010 and took a further one-time reduction of $17,500 as an offset for the atypical 25th annual meeting expense increase. Third-party audit, actuarial and legal expenses remained flat, and are expected to remain that way through 2011.
- **Meeting Expenses:** A two-meeting schedule continues to be observed, comprised of the Shareholders meeting in June, and the year-end board meeting and dinner in December. 2010 meeting expenses amounted to approximately $130,000 -- up $20,000 from 2009 -- again due to the atypical cost of the special anniversary meeting. June meeting itineraries will follow a 1.5 day activity schedule going forward.

Risk Management

First Monetary ("FM") is a non-assessable mutual insurance company charted in Bermuda in 1986. Its strategic plan is executed in accordance with Board approved policies, practices and procedures that are based upon a balance sheet risk management approach. Accordingly, FM places significant emphasis on management of the following risks:

Asset Quality & Liquidity

A major source of income to FM is the investment income earned on its available funds. The amount of funds available for investment is determined by FM's capital and surplus and the expected time within which incurred losses are paid.

With a high degree of importance is placed on the liquidity, security and marketability of assets, FM has implemented a very conservative investment policy that relies on returns from certificates of deposits deposited with FM members. All certificates values are less than the FDIC guaranteed limit.

Quality & Appropriateness of Our Reinsurance Program

FM has continuously underwritten Director and Officer Liability risks of the group on a direct basis for the past twenty-six years. The program is reinsured in respect of these risks by Lloyds of London, an A-rated reinsurer. The treaty provides:

1. Loss experience stabilization
2. Large limit capacity
3. Limited catastrophe protection (automatic reinstatements)

As respects the coming year, we are delighted to report that Lloyds of London renewed FM's D&O treaty for 2011/12 **without an increase in reinsurance rates or reduction in coverage limits or restriction on terms.**

Adequacy of Loss Reserves

The proportion of loss reserves to capital and surplus – reserve leverage ratio - provides an important insight into insurer solvency. The proportion of 3:1 or more is used by many property/casualty captives. FM's regulator, The Bermuda Monetary Authority ("BMA") permits a ratio as high as 10:1.

FM considers the Loss Reserve Ratio a key risk management component. Insufficient reserves are a leading cause of insurer insolvency. For long-tailed lines like D&O, estimating loss reserves accurately can be difficult and imprecise. Therefore, FM believes it wise to build in a small margin of safety in the event that its total claim reserve is less than required for a specific incident.

Here's why. A reserve leverage ratio of 2:1 implies that in a situation where reserves are underfunded by just 5%, surplus is overstated by 10%. Under this scenario, a surplus correction could impair a company's condition.

FM closely monitors its reserve leverage. A ratio under 1:0 could be considered conservative and a ratio above 2:1 would call for extra reserve attention.

- **FM's policy is to maintain a loss reserve ratio not exceeding 2:1**
- **FM's 2010 loss reserve ratio is currently less than 1:1.**

Capital @Risk (CAR) - Capital Formation and Adequacy

FM has paid particular attention to the management of its capital at risk (C@R) since the Company's founding in 1986. Oversight of the solvency and retention ratios are key risk management components.

Solvency ratio: This ratio represents the maximum level of premiums FM is permitted to write on a net basis compared to its capital and surplus position. In Bermuda, a 5:1 ratio is permitted. That would allow FM to write up to $6MM based on current assets.

While a 5:1 ratio is permitted by regulation, FM voluntarily observes a more conservative 2:1 maximum limit. FM's capital and surplus are provided by members that make a single reserve premium contribution equal to 50% of the Member's first year annual premium for a $600,000 policy limit - generally between $2,500 and $6,000. Accordingly, FM is able to maintain a minimum 2:1 solvency ratio as new members join the company.

- **FM's 2010 solvency ratio is less than 1:1.**

Retention ratio: This ratio represents the amount of per-occurrence risk retained net by FM compared to its capital and surplus position. It has been FM's policy to:

1. Maintain a 10% capital at risk maximum, net of reinsurance, on all primary D&O policies
2. Maintain a 25% capital at risk maximum, net of reinsurance, on all secondary "wrap-around" contracts.

- **Both ratios were maintained in 2010**

Managing the Underwriting Cycle

Pro-Cyclical Management Strategy: Traditional Commercial Insurance

From a logical and objective business standpoint, the inherent problem with the conventional commercial market insurance pricing is that it moves *pro-cyclically.* When bank profits are high, reserves for loan loss fall to their lowest point. During these periods, D&O, FDIC insurance and other risk-based expenses tend to be low. The problem for banks occurs in downturns, when they confront a painful "double whammy". At the very time banks must add to reserves, they face a situation where:

- Insurance markets close at the time they are MOST needed
- Insurance costs rise at a time they are least affordable

Counter-Cyclical Management Strategy: First Monetary

FM has always pursued a contrarian approach to management of the underwriting cycle. Our approach works best in tough economic times, when the risk of loss is most tangible, and the value that comes with the peace-of-mind of knowing you'll have access to affordable insurance is most apparent.

FM's counter-cyclical approach perfectly complements our central mission and commitment to "Protect the Decision-makers (Directors, Trustees and Officers) at Community Banks". First Monetary's tack promotes stability and predictability in up and down markets alike. When times are toughest, membership in this organization offers comfort and benefits in the form of:

- Continued coverage availability
- Stable pricing and
- Potential profits that offset premium costs

On both a philosophical and structural basis, FM is configured to maintain its commitment to members WHEN – rather than IF – circumstances merit. We maintain a long-term perspective on risk management. That's the niche we chosen to occupy and our central reason for being in business.

On the corporate level, FM's counter-cyclical operation provides an important financial benefit as well. Our structure permits us to take advantage of the US tax code. While existing rules do not permit deductions for future claims reserves to be expensed, it does permit such treatment for insurance premiums. FM premiums are tax deductible, and FM profits inure to owners under the company's mutual structure, Members build share accounts with after-tax dollars. Our set-up affords each partner the flexibility to maintain insurance coverage through rough patches.

The Immediate Horizon

It has now become apparent that a forward-looking approach to bank supervision will be a central part of every future regulatory exam. Inspectors have clearly become zealous converts to the Nassim Taleb, Black Swan camp of institutional oversight.

First Monetary's focus on risk management will be similarly forward-oriented in the year and years ahead. In our case, however, it ALWAYS has been. While routinely affording a healthy respect to the possibility of haphazard, "black swan" events , the secret to FM's longevity and success over time has been an ongoing and conscious attention to their more detectable counterparts, something Taleb's contemporary Nouriel Roubini refers to as "white swans". These are potential crises we can see coming and DO have the power to predict, prepare for and prevent. The simple reality of the financial crisis that has come to envelop today's banking industry is that there's nothing new, random or particularly unique about it. It's very much the predictable outcome of financial policy decisions that eventually led to asset bubbles, over-leveraging and vulnerabilities; something we're all acquainted with and have seen in the past.

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President's Report

Play It Again

As respects our immediate future, I hope you're not put off by the prospect of more of the same, "boring" routine. The roadmap we've chosen to follow doesn't have interesting scenery, but its gets us where we need to go while avoiding hills, valleys and tolls. You can fully expect that our conservative approach to investing, expenditures and risk management will not change without a clear discussion and understanding of the black and white swans we could face.

Our straight path decision will safeguard resources, and permit us to concentrate on things we do particularly well. As respects member relationships, our shareholders can be assured that they will continue to receive valuable information, insights and tools that help them assess and manage their own risk effectively, through development of strategy, contingency plans, capital allocation and strong Compliance Management System (CMS). The Monetary System's E-Board library links and subscription feeds are just one proof-of-concept.

FM remains firmly committed to servicing existing members and has the wherewithal to continue doing so without dramatic changes in our operating profile through the next position assessment in 2015. We will continue to monitor a very fluid strategic risk situation during this period for developments that might provide opportunities, and will premise our longer-range plans on what transpires in the interim.

Thank you as always for your confidence and steadfast support. It's a major element in the two–part harmony that keeps our group making beautiful music and doing encores. It's also the source of our ability to get out there for another in a string of "Play it Again" repeat performances.

Frank Shashaty

Frank J. Shashaty, CPCU, President & CEO

First Monetary Mutual Limited