

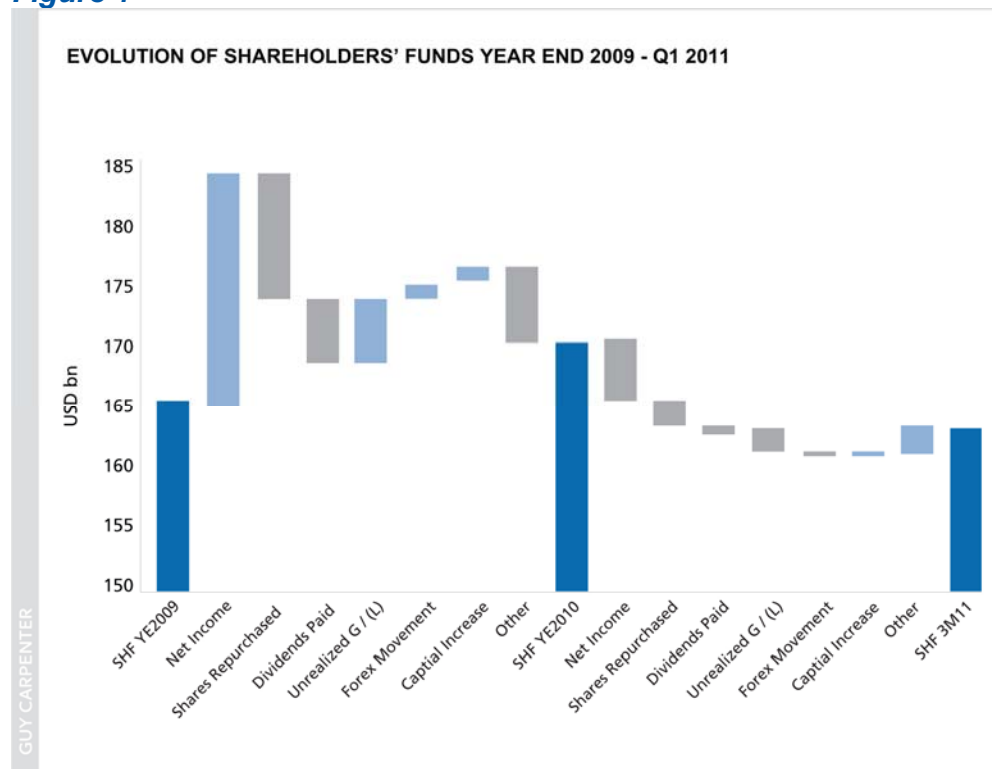
JULY 2011

Focus on Hurricane Season at July 1, 2011 Reinsurance Renewal

July 1 represents the last major renewal period of the year. As we wrap up the majority of placements for 2011, there are several occurrences that have played a key role in the positioning of the market. Chief among the critical 2011 events are the global catastrophe losses and the release of RMS v11, both of which had an impact on reinsurers' capital positions and views of risk. The longer term impact of both of these factors remains somewhat unclear as losses from recent events are not fully developed and there is not a consensus position on the integration of RMS v11.

During the first quarter of 2011, the Guy Carpenter Global Reinsurance Composite's dedicated capital position fell by 4.2 percent to USD163.7 billion (Figure 1). This was driven by net losses caused by significant reinsured catastrophes. In the second quarter, reinsured catastrophe losses were again above average, with the result that the reinsurance capital remained essentially flat over the quarter and moderately down year-to-date.

Figure 1



Source: Guy Carpenter, company information

The moderate decline in capital over the first six months has corresponded to a mitigation of share repurchases. It also contributed to firming in rates-on-line of property catastrophe business underwritten at the April 1, June 1, and July 1 renewals.

The development of the reinsurance sector's capital position over the remainder of the year is now heavily dependent on large loss experience, which will in turn be influenced by the hurricane season. A light hurricane season with no significant landfalls could enable reinsurance capital to resume growth, while a heavy season with at least one significant landfall could mitigate growth or even result in an impairment of capital for the remainder of 2011.

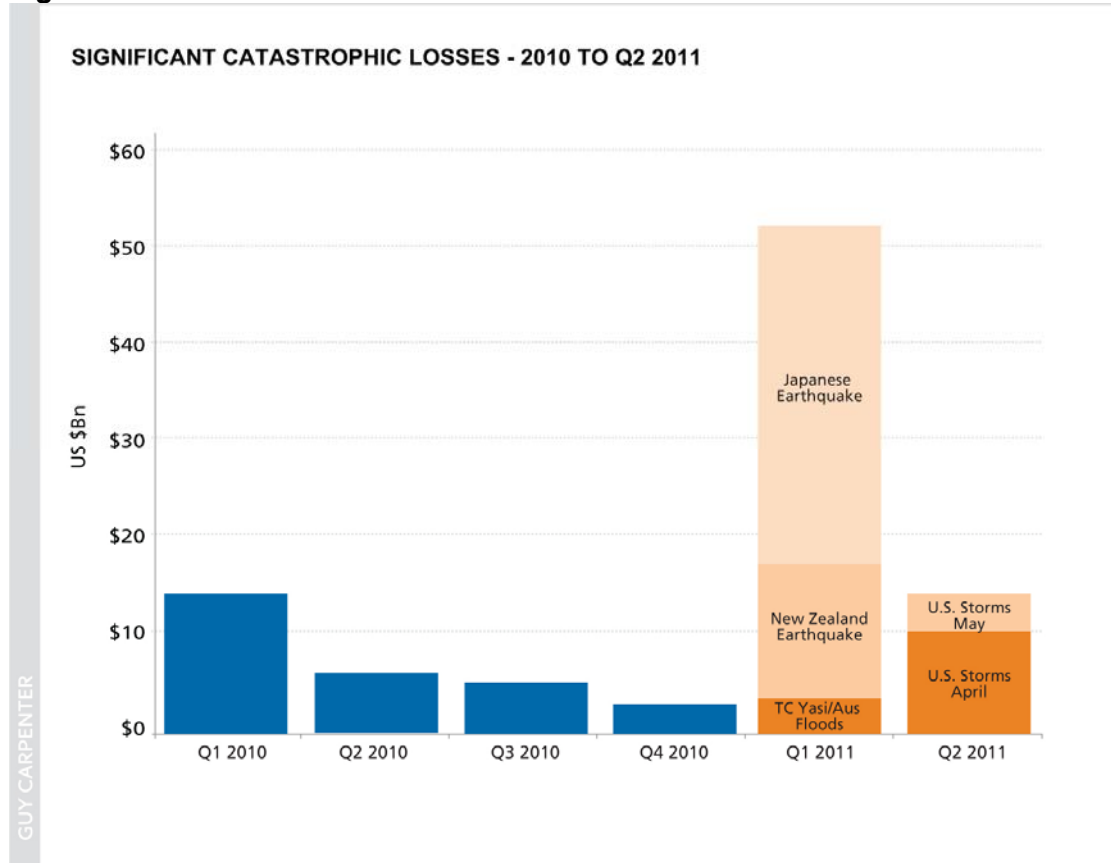
Catastrophic Events of 2011

The first six months of 2011 saw massive losses from global catastrophes. A series of powerful earthquakes in New Zealand and Japan, combined with multi-billion dollar payouts from tornadoes and floods in the United States and Australia, meant the (re)insurance industry experienced the most costly first half on record. Losses of around USD70 billion are estimated for the period. At least nine natural catastrophes incurred insured losses of more than USD1 billion during the first half of 2011. Five were related to tornadoes and severe weather in the United States (causing a combined insured loss of more than USD14 billion). Australia sustained two major losses when floods inundated parts of Brisbane City in January and Cyclone Yasi made landfall in northern Queensland the following month.

However, the heaviest losses of the year, so far, were triggered when two of the most damaging earthquakes in recent times struck New Zealand and Japan. Thousands of buildings were destroyed in Christchurch, New Zealand's second largest city, after a shallow 6.3Mw earthquake shook the region in February. In Japan, meanwhile, more than 23,000 people were killed or left missing after a 9.0Mw earthquake struck off the country's northeastern coast in March. The event caused severe shaking along much of Japan's eastern coastline and triggered a massive tsunami that devastated coastal communities. Tens of thousands of buildings were destroyed or damaged by the Tohoku earthquake, which was the largest to hit in Japan since modern instrumental recordings began 130 years ago.

Figure 2 shows the accumulation of significant losses over the last 18 months. The losses sustained so far in 2011 have already surpassed those recorded in 2010 and 2009 combined. It is against this backdrop that the (re)insurance industry faces the 2011 hurricane season.

Figure 2



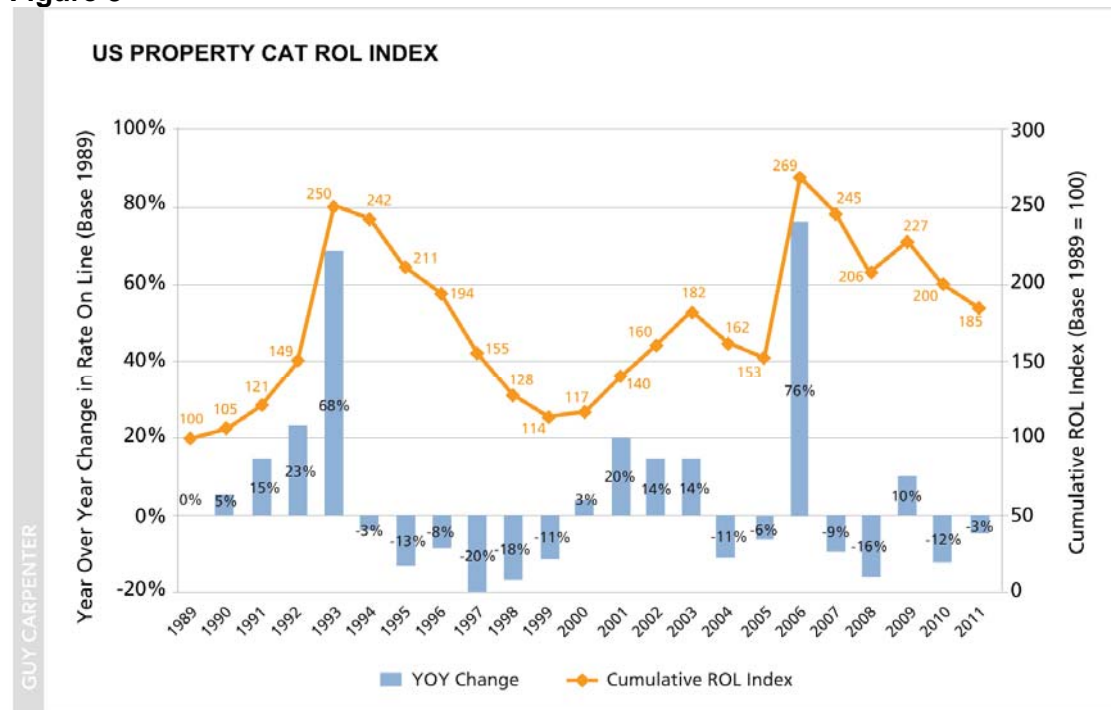
Source: Guy Carpenter & Company, LLC

Property

US Property Catastrophe

Analysis of the renewal data indicates pricing trends for June and July 1 non-Florida renewals are similar to the market behavior reported in the June 1 Florida renewal report. Pricing increased in the range of 5 percent to 10 percent on a risk adjusted basis as measured by RMS v9. This is in contrast to the January 1 renewals, which were down on average. The weighted change in pricing for the aggregation of renewals in 2011 ended down roughly 3 percent, due to the majority of renewals having anniversary dates at January 1. Historical pricing activity is shown below in Figure 3.

Figure 3

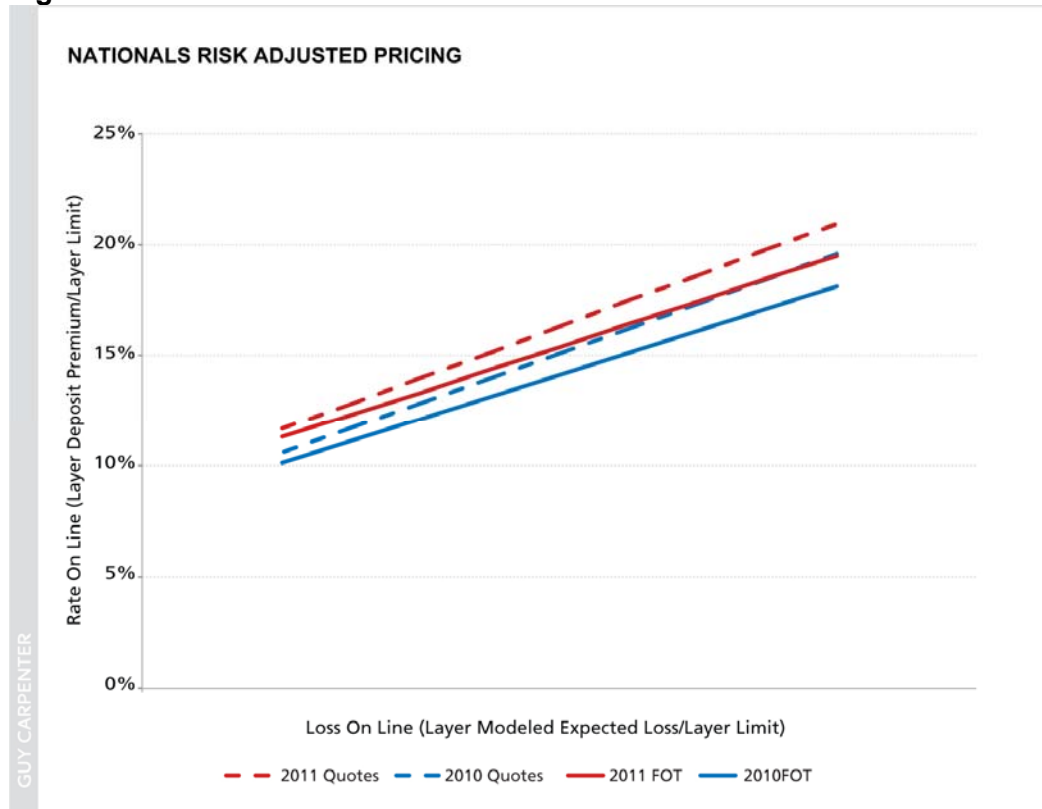


Source: Guy Carpenter & Company, LLC

Evaluating the pricing behavior for national and regional renewals excluding Florida at June 1 and July 1, we see that the general market response in both groups was fairly consistent. Pricing for lower layers increased less significantly than upper layers. In both cases, there was some additional pressure on upper layer pricing due to demand for those limits. In particular with regional writers, there was an up tick in minimum capacity charges that had been pushed to fairly low levels in recent years.

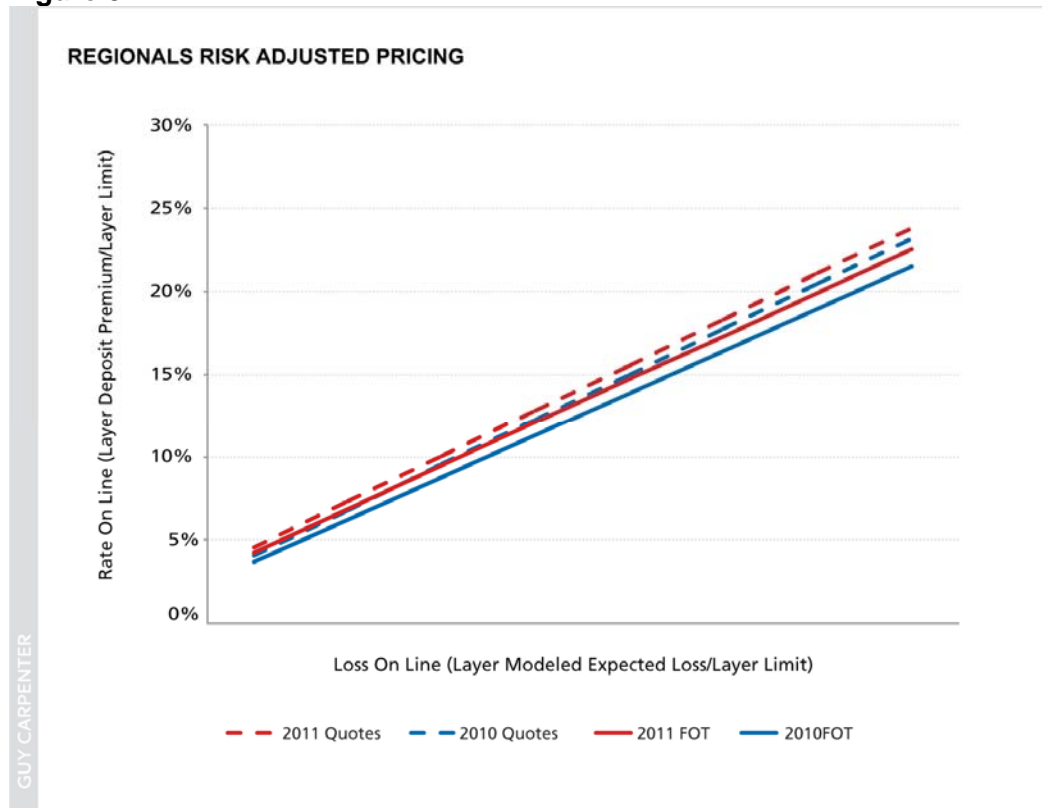
The charts below represent the relationship between the rate-on-line (the amount charged) and the loss-on-line (the amount of risk) for the programs renewing at June 1 and July 1, excluding Florida-only renewals, using RMS v9 to measure loss-on-line. Upper layers have lower loss-on-line (the left side of the charts). Note that, while visually, the movement in the upper layers appears to be less significant than the lower layers, the percentage movement is greater, as the overall pricing is significantly less than the lower layers.

Figure 4



Source: Guy Carpenter & Company, LLC

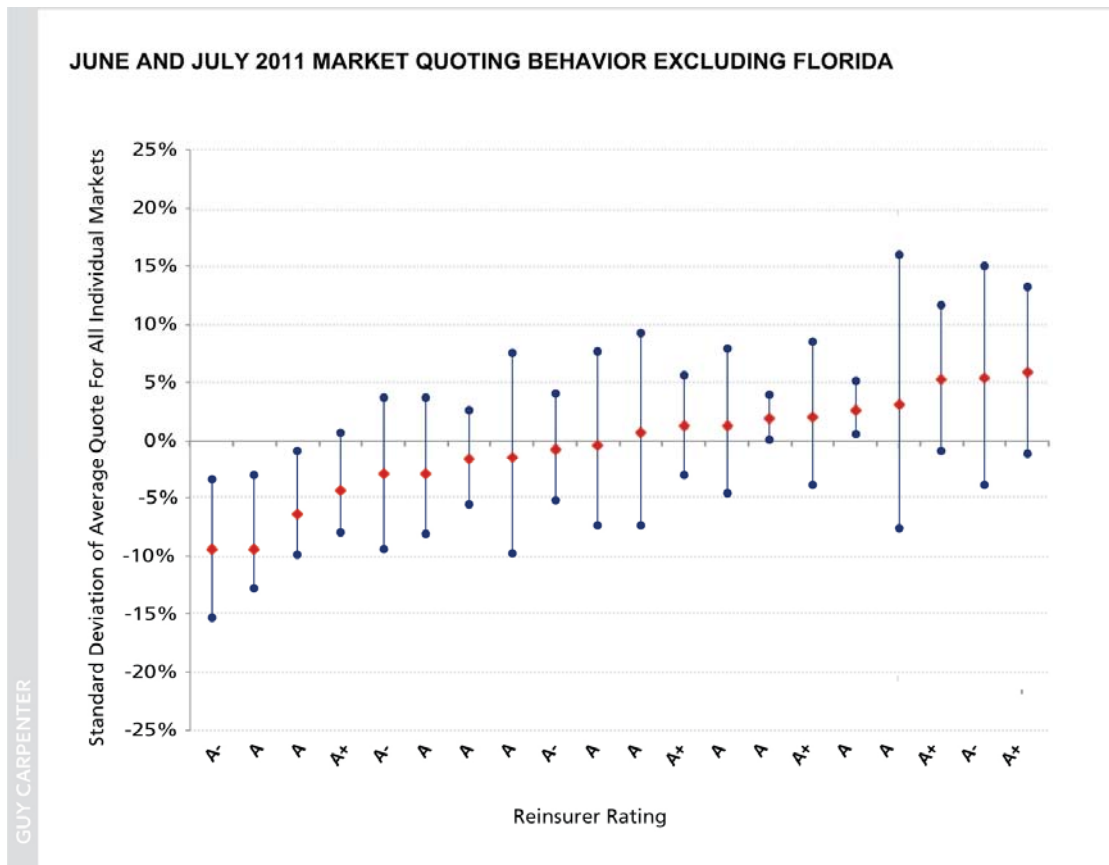
Figure 5



Source: Guy Carpenter & Company, LLC

As reported in the June 1 renewal report, the calculation of risk adjusted pricing is dependent on the method used to calculate the “risk.” RMS v9 provides a consistent measure of the level of risk from 2010 to 2011. However, to some extent, reinsurers also assessed the results of the new version of AIR and the new version of RMS in making their pricing decisions. Consistent with the Florida renewals, the change in risk adjusted pricing is flat when using AIR v12 and down 15 percent when using RMS v11 to measure the amount of risk the reinsurer is assuming for a given price. Unadjusted change in rate-on-line increased approximately 3 percent to 6 percent. Quoting behavior did not demonstrate the same level of deviation from renewal activity seen at June 1 with the Florida renewals. The range in the June and July non-Florida renewals from the average quote for a program was up approximately 5 percent to down 10 percent. This is very close to the overall average for the 2010 renewal season.

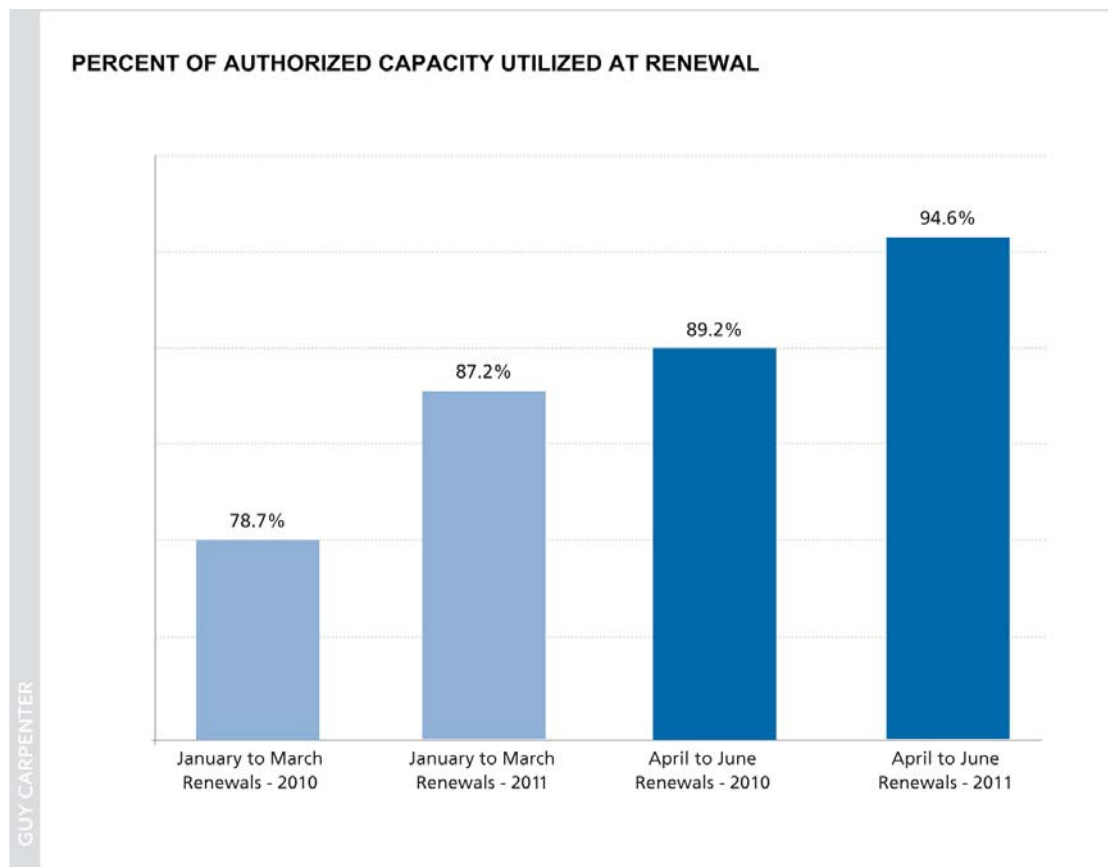
Figure 6



Source: Guy Carpenter & Company, LLC

Regarding capacity, a significantly larger percentage of authorized capacity was utilized to fill out the 2011 renewals as compared to 2010. April through June renewals in 2011 signed almost 95 percent of authorized capacity, as opposed to approximately 90 percent in 2010. That said, we are not experiencing any capacity shortage – rather, a more careful evaluation by reinsurers of where they will deploy their capacity in a transitional market.

Figure 7



Source: Guy Carpenter & Company, LLC

Looking ahead, prior to the January 2012 renewal season, a significant amount of evaluation will occur within both insurance and reinsurance companies. For insurers, analysis of key drivers of the model version changes and assessment and validation of new risk management parameters is essential. This will allow an approach to the January 1 renewal season with a clear message to corporate stakeholders, rating agencies and reinsurers. While the view of risk the new model versions put forth is one component of this assessment, companies have also utilized additional methods to measure risk and manage portfolios. Decisions regarding reinsurance purchasing and risk management in light of the new model versions will also be influenced by other risk assessment factors.

Analysis of renewal data and discussions with reinsurers indicate that there are still some disparate views on the integration of the new models into pricing, as well as assessment on the impact of reinsurers' own portfolios. Insurers' ability to provide detailed reasoning for their own assessment of their portfolios, as well as reinsurers' solidifying their position on metrics for deploying capacity, will be key factors leading into January 1. The catastrophe activity for the remainder of the year will also have a critical impact on reinsurer capital and the market position at January 1.

US Property Risk

Risk programs are generally impacted by their own history of loss experience, changes in the composition of the underlying portfolio in terms of risk class or limits and the amount of cat risk they are exposed to. Recent risk renewals reflect this and experience at renewal was varied. Capacity was plentiful, although some markets did cut back on authorizations for more heavily cat exposed programs. Overall, pricing was flat to down slightly.

Australia and New Zealand Property

The 2010-2011 year has proven to be a significant one for the Australian/New Zealand insurance industry as a result of the natural catastrophe activity that impacted the market over the past twelve months.

In Australia, the most significant event has been the flooding that predominantly affected Queensland. Separate events in December 2010 and January 2011 resulted in both insured and economic loss on a large scale. These events have once again led to considerable debate regarding flood as a peril, with coverage definitions varying greatly between insurers. In light of these disasters, the Australian Assistant Treasurer in early March of 2011 began a Natural Disaster Insurance Review, which issued its initial thoughts for further comment in early June. Its early findings suggested two alternative strategies for handling flood – automatic cover or an opt-out position.

In New Zealand, the city of Christchurch suffered a devastating 7.1 Mw earthquake in September 2010 that resulted in insured losses of approximately USD4 billion. An aftershock measuring 6.3 Mw struck in February 2011, with an epi-center that was much closer to the city. Damage sustained was much greater. With close to 200 fatalities, this second earthquake also caused significantly more building damage, and early estimates put the insured loss as high as USD12 billion. Further aftershocks and earthquakes have continued to impact the Christchurch area. Discussion is ongoing between the insurance industry, government and EQC in New Zealand regarding the role insurance (and reinsurance) will play in the reconstruction of Christchurch and its surrounding area.

As a major reinsurance renewal date for the Australian/New Zealand market, July 1 was the first real test of how these various natural catastrophe events of the past 18 months have impacted reinsurer pricing and capacity for catastrophe excess of loss programs. Final outcomes of these events remain unknown. Prior to the renewal, reinsurers signaled that rates would need to increase and this proved to be true. Pricing was adjusted upwards to account for exposure growth in addition to a further general increase in pricing, as reinsurers looked to achieve a higher return for the capacity being deployed. Where programs were impacted by the loss activity, additional increases were imposed. While capacity has remained adequate, reinsurers' approach to the renewal was largely uniform. Catastrophe program rates increased in a range from 20 percent to greater than 100 percent. While reinstatement provisions were expected to come under pressure, most reinsurers continued to offer and support these on a pre-paid basis.

The impact of these natural catastrophe events also had an impact on the proportional and per risk reinsurance markets. Reinsurers sought to further limit the amount of catastrophe cover given under these treaties, with commission terms being amended to reflect treaty experience over the past 18 months.

Latin America and Caribbean Property

Property catastrophe rates in the region were stable, with a tendency to increase between 5 percent and 10 percent in the wind-exposed regions. Reinsurers' views on the extent of the increase are quite divergent. The divergence is often related to each reinsurer's own first half 2011 catastrophe losses and what each believes the Latin America and Caribbean contribution should be to the recovery of the loss.

The market was slightly more varied than in previous renewals, with some markets looking to grow in the region while others tightened their underwriting criteria. Rates on Chilean catastrophe programs were flat, following the significant increases of last year. Property proportional treaties in the region experienced the same terms and conditions as last year. The ability of buyers to receive any kind of risk adjusted price decrease was virtually gone.

Capacity is readily available for property business from existing players and new entrants. However, we saw some pricing resistance on the upper layers of big catastrophe programs, where the key players looked for a better return on their capital in earthquake exposed territories.

Pressure on reinsurers' proportional capacity continues to grow. Several reinsurers reduced their proportional capacity, as the impact on their own numbers from unlimited sideways coverage of pro rata continued to cause issues. Reinsurers are increasing the scrutiny of their own aggregates and how the aggregates grow. Pro rata is an area that tends to stress reinsurers' accumulations.

Original property rates were still competitive, as some multinational insurers, many untouched by losses in the Pacific Rim, look to maximize their opportunities arising from the growth in Latin American economies. This is in direct contrast to the trends in reinsurance property rates.

The new regulatory environment in Argentina and Brazil, which proposes to enhance cessions to local reinsurers, has dominated reinsurers' strategic thinking recently. Ultimately, this is likely to accelerate the development of two hubs for the region: Brazil in the Southern Cone and Miami for the rest of the players in the region.

Property Retrocession

The run up to July 1 is not traditionally a big renewal period for catastrophe retrocession. It is more about new and opportunistic purchases, as clients look to mitigate the effects of the coming US wind season as best they can. However, it is precisely because of this renewal date's proximity to the wind season that deals purchased at this time tend to be an important indicator of pricing direction and activity. We have observed that activity within the sector has continued the trend towards rate rises (on both loss-affected programs, and, to a lesser extent, loss-free programs). This activity has been mainly driven by industry loss warranty (ILW) and county weighted industry loss (CWIL) purchases. It must be viewed against a background of significant tornado activity and flooding in parts of the United States and the latest earthquake in New Zealand in June.

Capacity is expanding as a result of the development of some sidecars that have been proposed to write catastrophe retrocession business. As a general rule, we have seen demand from buyers for new covers, specifically United States all perils first event and

second and subsequent loss covers. There has been strong demand for all types of traditional/industry loss warranty/CWIL covers. CWIL, in particular, has seen a sharp increase in interest, with Guy Carpenter having now placed over USD1.3 billion in limits to date for 2011.

Trading activity has also been healthy in the ILW market in recent weeks. Focus, as always at this time of year, is on United States wind, both first and second event protection. Despite increased demand, pricing remained stable following price increases earlier this year. Capacity remains readily available from both hedge fund and traditional carriers who set aside limits to take advantage of the price increases we saw at the end of the first quarter. The ILW market is thus comparable with the same time last year (where rates surged in the short term to similarly healthy levels) if not up slightly.

A demand for additional levels of protection has been driven by several factors. One of these is a desire to lock in profits for year-end by spending what is left in the catastrophe budget on additional coverage, thereby assisting the maintenance of a positive result. Other factors include the much-discussed new model RMS v11, which has seen average expected losses for portfolios increase significantly in many areas of the United States. Coupled with these factors is the overwhelming desire of clients to not become 'outliers,' which might negatively impact their standing with the equity markets. They would rather stay within the expected range of returns for their peers in the market.

Industry Loss Warranties

As we moved towards the wind season there was a steady increase in activity. Prices increased steadily rather than with the big jump that was seen at this time last year. Capacity is still freely available for most types of covers, but the proliferation of "non-United States" covers in the first few months of the year gave way to the annual pre-wind season activity. Last year, with much credence given to hurricane forecasts, hedge funds were prominent among the buyers of the product. This time around, however, it is most definitely the rated carriers who are the biggest buying group. Because the rated carriers have better access and more established positions in the territories where the losses have been sustained, they have suffered more than the hedge funds. Accordingly, the rated carriers have lower appetites for taking on more catastrophe losses in the United States. If activity continues at the same pace through the July 1 renewal season, pricing is likely to nudge record levels.

Catastrophe Bonds*

The second quarter of 2011 saw four catastrophe bonds come to market, totaling USD592 million of new bond issuance. The cat bond market continued to become heavily weighted to US hurricane exposure, causing some investors to pull back on their allocation to US hurricane exposure. Other perils did not grow at the same rate. The percentage of the cat bond market with exposure to US hurricane has grown from 38 percent in 2003 to 71 percent today.

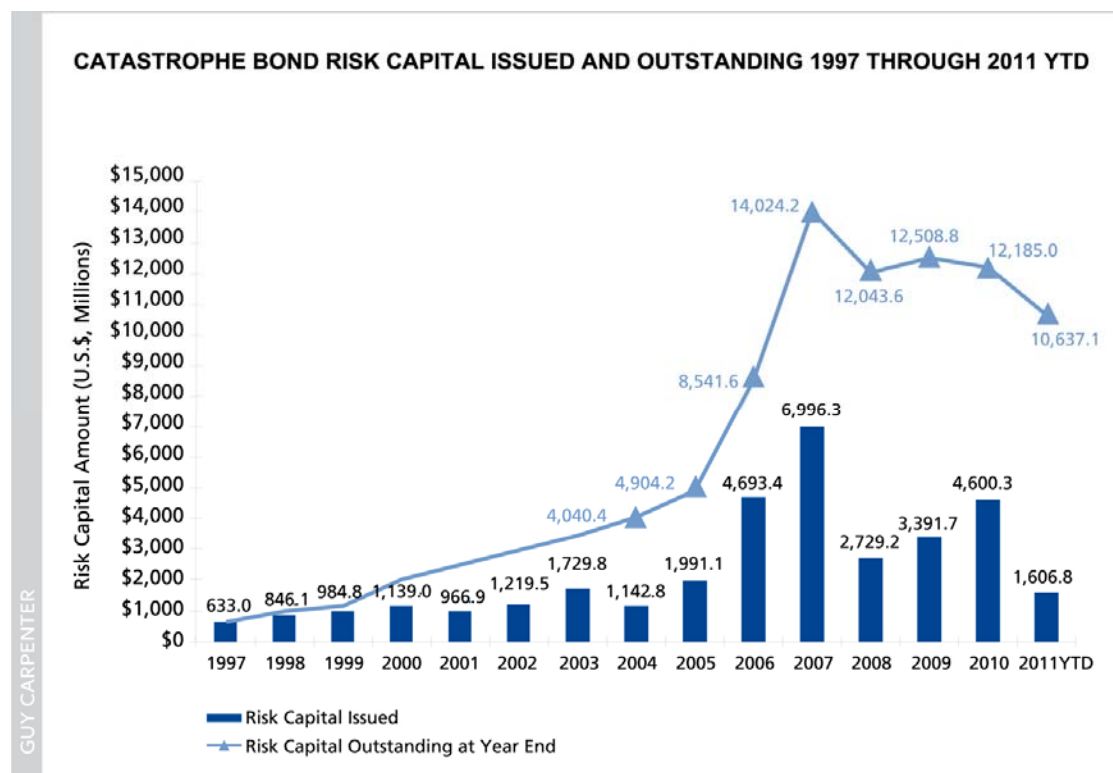
During the quarter, USD1,617 million of risk capital was returned to investors through maturing cat bonds. Investors also suffered a full loss on one of the bonds as a result of the Tohoku earthquake: the USD300 million Muteki issuance. While other bonds have

been affected by the impact of the Tohoku earthquake, caused, for example, by the shifting from second event to first event, none other besides Muteki have had to make a principal payment. The secondary market traded down during March, reflecting expected principal losses from the Tohoku earthquake, mark to market losses as second event bonds shifted to first event bonds and potential for reinsurance rate increases. However, it is important to note that in the aftermath of one of the largest earthquakes in recorded history, the catastrophe bond market continued to trade in an orderly and disciplined fashion, and the investors are assessing whether this is the market opportunity to increase their allocation to catastrophe risk.

The second quarter also saw a new issuer come to market, Argo Re. Argo's bond, Loma Re, provides Argo Re with 18 month protection against certain US hurricane, US earthquake, Europe windstorm and Japan earthquake on a per occurrence second event basis.

The first quarter of 2011 was the most active first quarter in the history of the catastrophe bond market in terms of new issuance. All told, four transactions came to market, securing USD1.02 billion of new and renewal risk transfer capacity. This is a significant increase over the USD300 million issued during the first quarter of 2010 and previous first quarter high-water mark of USD615 million posted during the first quarter of 2008. Issuance was diverse in terms of risk profile and structure, though US hurricane risk was a common theme in all four transactions. All transactions marketed during the first quarter of 2011 priced within or inside of their initial spread guidance.

Figure 8



Source: GC Securities

Table 1

CATASTROPHE BOND ISSUANCE 2011YTD

ISSUE DATE	TRANSACTION/ TRANCHE NAME	SPONSOR	TRIGGER	COVERED PERIL(S)	TRANSACTION/ TRANCHE TERM (YEARS)	TRANSACTION SIZE (\$MM) ⁽¹⁾	TRANCHE RATING (S&P / MOODY'S)	ROL AT AT ISSUANCE ⁽²⁾
18-Feb-11	Successor X 2011-1 IV-E3	Swiss Re	PCS / Parametric	U.S. HU / Cal Q	3.02	\$160.0	B	9.25%
18-Feb-11	Successor X 2011-1 IV-AL3	-	-	-	3.02	\$145.0	Unrated	13.00%
18-Feb-11	Foundation Re III 2011-1	The Hartford	PCS	U.S. HU	4.02	\$135.0	BB+	5.00%
7-Mar-11	East Lane IV 2011-A	Chubb	Indemnity	U.S. All Perils	3.01	\$225.0	BB+	5.75%
7-Mar-11	East Lane IV 2011-B	-	-	-	4.01	\$250.0	BB	6.65%
22-Mar-11	Queen Street II	Munich Re	PCS / PERILS	U.S. HU / EUWS	3.03	\$100.0	BB-	7.50%
15-Apr-11	Blue Fin Series 4	Allianz	Modeled	U.S. HU / EQ	2.12	\$40.0	Unrated	8.50%
17-May-11	Johnston Re 2011 Class A	NC JUA/IUA	Indemnity	U.S. HU (North Carolina only)	2.98	\$70.0	BB-	7.60%
17-May-11	Johnston Re 2011 Class A	-	-	-	2.98	\$131.8	BB-	6.90%
31-May-11	Residential Re 2011 - 1	USAA	Indemnity	U.S. All Perils	4.02	\$57.0	B+	9.00%
31-May-11	Residential Re 2011 - 2	-	-	-	4.02	\$33.0	B-	12.00%
31-May-11	Residential Re 2011 - 5	-	-	-	4.02	\$160.0	B+	8.75%
17-Jun-11	Loma Re 2011-1	Argo Re	Various	U.S. HU / EUWS / JPEQ	1.50	\$100.0	BB-	9.50%
SUMMARY STATISTICS						RISK CAPITAL	DEAL COUNT	
TOTAL ISSUANCE - 2011						\$1,806.8	8	
Notes								
(1) Where applicable, non-U.S. dollar denominated transactions are converted to U.S. dollars using the prevailing exchange rate on the issuance date								
(2) Expressed as a spread above the applicable benchmark rate								
-> GC Securities Transactions								

Source: GC Securities

Marine & Energy

London Market Excess Loss (LMX) & Global Retrocession

April 2011 and prior renewals with energy (particularly, energy liability) experienced exposure paid rate increases of approximately 20 percent. This represented the first opportunity to re-rate since Deep Water Horizon (DWH). Pricing for non-energy classes remained flat but with little downward pressure. Following the Gryphon loss in April, the energy market hardened further. While there are relatively few excess of loss placements renewing at this time, the perception in the market was that rates are likely to harden further where energy related coverage is sought. There has been very little demand for any additional Gulf of Mexico wind limits prior to the wind season, as original rates remained static and insurers maintained or reduced their aggregate. Retro renewals outside the January 1 renewals are rare, but those that did happen paid increases similar to those at January 1 – between 20 percent and 25 percent. Marine industry loss warranty covers tend to attach mid-year and renewed generally at expiring rates. They experienced rate increases following DWH and generally were in excess of any potential loss from Gryphon 'A'.

EMEA Marine & Energy

There are very few mid-year treaty renewals of any note emanating from Europe. Capacity is plentiful, especially for single territory marine business, where rates have remained 'flat' at best.

There has been no real impact from the catastrophes in Japan, Australia and New Zealand on the European market, although this has yet to be properly tested, as the larger clients' programs generally all renew in January 2012.

It would appear the main issue many Europeans are facing in the short term is preparation surrounding compliance with future Solvency II requirements.

Asia Pacific Marine & Energy

Japan:

Clearly, the Tohoku earthquake and tsunami colored the market's approach to Japanese business, where, although no client was able to provide an accurate estimate of its loss, it was assumed that they would be significant.

Cargo excess of loss attracted rate rises of 20 percent to 40 percent, depending on level and circumstances. On the whole, the London market seemed a bit tougher than European (with one major exception) and Asian markets. Rates declined cumulatively since 2002 and some reinsurers took the opportunity to include some rating adjustment. Since April, more accurate estimates have come in suggesting that losses will not be as bad as originally feared. Japanese inland transit policies (which also cover shipments to Free on Board) exclude earthquake and tsunami.

Hull treaties, already underperforming, sustained significant losses during the tsunami. Although most of the pleasure craft and fishing boats (featured frequently on television bulletins) are not insured in the commercial market, there were substantial losses from commercial coastal vessels and some oceangoing hulls. The market gross hull loss is estimated at JPY20 billion, which compares with the Diamond Princess building risk loss of JPY26 billion in 2002.

South Korea:

Most of the business in the open market is excess of loss and, although orders did not come out until after the Tohoku event, rates were not really affected by the Japanese disaster. Korean companies generally reinsure at a much lower level than the Japanese. Most companies experienced losses, leading to rate adjustments.

United States Marine & Energy

A majority of programs covering general marine portfolios renewed with small premium and occasional rate reductions owing to good loss records and significant capacity. On more specialized programs with good records, reductions of 10 percent to 15 percent were achieved. However, those programs impacted by last year's Deepwater Horizon catastrophe did pay rises commensurate with the magnitude of their losses. These increases generally ranged from between 15 percent to 25 percent.

At April 1, the Tohoku earthquake caused some initial confusion in the market as to its impact on pricing. There was some movement by certain reinsurers towards halting further reductions, but this position in most cases was short lived. Even those programs quoted at reductions were generally over-subscribed, as reinsurers seemed to scramble to try to maintain income when terms were set.

Insurance market conditions were competitive for virtually all classes of marine. Rates were flat to down 5 percent to 10 percent. While under pressure to maintain if not grow their top line revenue, most clients were unable to meet their premium estimates. In light of this, there was greater pressure on reinsurers from clients to offer reduced percentage minimum premiums on excess of loss renewals.

Some clients saw increased shipping activity owing to the recovering economy, which may have had a positive impact on the cargo market. Meanwhile, energy underwriters are adjusting income estimates to reflect the fact that anticipated hardening did not materialize following DWH.

Reinsurance capacity remains abundant and relatively stable in the United States, although there has been some shifting of capacity, with senior staff movement to other carriers

There is a good deal of ongoing dialogue in the market about the impact of RMS v11 model results relative to v9. Many clients are rejecting the results until they better understand why the projected losses are so much higher. Not surprisingly, reinsurers are trying to push the use of v11, although, ironically, the modeled losses for most yacht portfolios have actually declined.

Global Marine & Energy Outlook

The potential marine loss from the Japanese earthquake remains below initial expectations, and at this point in time, that event is unlikely to have a significant impact on ongoing rates outside of Japan.

Many reinsurance writers who purchased retro protection found themselves with two retention losses in the first half, as both the Japanese earthquake and Gryphon 'A' likely fell around the attachment point of their covers. This will apply further pressure to their results, placing their 2010 and 2011 financial years in a parlous state. Inevitably, this will encourage the reinsurers to seek further increases at the next January 1 renewal, when there will likely be increased focus on the underlying energy portfolios. Furthermore, there will undoubtedly be added pressure on the marine sector from managements struggling under the weight of the recent spate of property catastrophe losses. They may also be wary of the current negativity surrounding the rating of energy and energy liability business. Barring a catastrophic event and with capacity remaining plentiful, resistance to upward pricing pressure will continue for the foreseeable future.

Aviation

At July 1, the major risk (airline and manufacturing) sector of the aviation reinsurance market showed stable pricing on a 'like for like' exposure basis. Most renewals either quoted or ordered as-before pricing, with similar levels expected for those who had yet to enter the market. This occurred against a back drop of a direct market where soft conditions continued to prevail, with a trend towards rate reductions. Premium levels had been stable through post recession fleet and passenger growth. Although the aviation excess of loss market had not sustained any significant loss since the middle of 2010, reinsurers did not appear to be willing to give any reductions in view of the positive rating environment in other reinsurance lines and the recent occurrence of natural catastrophes.

In the general aviation reinsurance sector the outcome at July 1 was more reflective of individual performance, with ratings movements matching exposure and loss activity. In the US market the expected upward movement did not materialize, with rates now on a more stable basis.

Credit Reinsurance

Capacity in the credit reinsurance sector remains meaningfully over-subscribed, impacting pricing and terms. Over-subscription arises as a result of various signal contributing factors. The (re)insurance industry in general is oversubscribed, with returns in other lines of business relatively lower. We see no realistic expectation for significant change in the short term. Credit loss ratios worldwide returned to profitable positions far faster than had been anticipated.

Credit is currently delivering relatively more favorable capital returns than most other lines of business. Therefore, new capacity has been attracted into the line in the last 18 months. The new capacity is driven mainly by existing underwriters establishing new operations with reinsurers previously not active in the line of business. Considerable confidence exists for macro-economic conditions to continue to favorably influence and perpetuate below average loss ratios.

Discipline around insurance underwriting and focused risk management activities have allowed quick responses to adverse developments. These may include the Greece financial crisis, the revolts in Arab nations and sectoral collapse, such as the British retail sector. This reduces perceived volatility, maintains confidence and increases the level of capital allocated to the class.

Credit reinsurance rates remained under pressure for a variety of reasons. The premium from non-proportional contracts represents less than 5 percent of the global credit reinsurance premium. The vast majority of credit reinsurance premium is derived from proportional, largely, quota share, contracts.

Even though the global recession was credit's one in eighty years event, most excess of loss structures were untouched. The global financial crisis really proved that credit is a frequency loss class, with a complete absence of severity.

The direct writers still remain cautious and ever watchful of economic indicators for evidence of systemic deterioration. Paradoxically, with understandably increased demand from insureds, direct prices have fallen month on month for more than 20 months. Such a slackening in original disciplines will undoubtedly impinge on the next cycle.

Casualty

US Casualty

July 1 renewals in the US casualty lines overall continued to operate in a soft pricing environment, with little change from renewals earlier in the year. Commercial primary casualty pricing continued to decline during the first half of 2011, albeit at a slower pace than 2010. Of all the casualty lines, rate hardening on a relative basis has been more evident in workers compensation. General liability rates remain flat. Subject premium base reductions for many of the casualty lines have begun to slow and stabilize and, in some cases, increase, as a result of the recovering economy.

Excess/Umbrella

Primary rates for excess umbrella coverages were relatively flat, on average, with some individual accounts still experiencing some rate reductions of up to 5 percent. However, in certain classes and account-specific situations, the market saw some rate increases. Exposure bases have stabilized since last year, when we saw larger reductions in premium due to exposure reduction that resulted from the economic recession. Reinsurance capacity for the business has contracted year over year. Along with original rate movement, the main driver is energy exposure. Since the Japanese earthquake event and other catastrophe events, the reinsurance market has stabilized somewhat, with reinsurers renewing existing transactions at roughly expiring terms. Overall, the reinsurance market still had a more pessimistic view of the profitability of the original business.

Umbrella and excess loss ratios trended upward, on average, for large-account lead umbrella business. This occurred during the past few years as older accident years developed further. This drove some increased pricing on this business, recently. Small and middle market standard accounts experienced stable loss ratios through the cycle, in many cases, due to minimum premium redundancy. The Bermuda excess liability market experienced loss activity during the last year. As a result, insurance carriers reduced gross limits exposed by account and also raised rates on certain classes of business – in particular, energy risks. Insurance carriers closed operations, reducing available limit to the market.

Since the recent property loss events, reinsurance proportional capacity has stabilized. Reinsurers are encouraged by the recent reduction in insurance capacity and stabilization in primary rates. Reinsurers will continue to be judicious with capacity until there are more concrete signs of market improvement.

Workers Compensation

Those reinsurers that provide a majority of the workers compensation reinsurance capacity also suffered losses from the catastrophic events of the first and second quarters of 2011. The top 20 reinsurance groups assuming workers compensation reinsurance premium declared losses of nearly USD13 billion. On average, the losses represent nearly 9 percent of the 2010 year-end stated group equity for the top 20 workers compensation reinsurance markets.

Unlike the 2006 renewal season (post Hurricanes Katrina, Rita and Wilma), when reinsurers sought rate increases but were bound at rate decreases, July 1, 2011 renewals wrestled with new, enhanced pressure to increase rates.

One of the annual bellwethers for the primary workers compensation industry is the May National Council on Compensation Insurance Annual Issues Symposium. The primary workers compensation market results presented this year continued to erode due to a variety of economic and market cycle factors. The calendar year combined ratio increased from 110 percent to 115 percent and the long-term trend of reducing frequency of loss has reversed, with an adjusted up tick in loss frequency noted in 2010. Rate-making bureaus indicated primary rate increases for more US states this year, compared to recent history. Depending on carrier discount, we may start to see premium increases in the primary market.

Working layer reinsurance, structured to provide coverage to occurrences that involve one or more injured workers, is dependant on primary loss ratios. The increased loss ratios combined with low investment/interest rates and fears of increased inflation rates resulted in very few working layer reinsurance price decreases. Any decreases were tied to either shifts in the portfolio to less hazardous classes of business or superior individual company experience.

Catastrophe layer reinsurance, structured to cover larger, multi-claimant events, is more dependent on exposure concentrations, modeled output, cost of capital trends and reinsurer aggregate budgets/appetites. Ceding company data sets have steadily improved over the years and the best catastrophe reinsurance pricing is rewarded to companies with the most complete data sets.

Second quarter renewals followed the trends observed at January 1, 2011 with, on average, flat to slight rate increases for working layers and mid to high single digit rate on line decreases for multi-claimant catastrophe layers.

For July 1, reinsurers quoted increased rates on renewal structures. Buyers reacted by seeking an increased number of structure options to find a fit within typically shrinking reinsurance budgets. (Ceding companies are still hampered by decreased premium volume due to depressed payrolls and primary premium decreases).

The original quoted rate increases and increased number of additional options sought have resulted in delayed final placed firm order terms compared to previous July 1 renewals. Programs are being bound later than usual and the final July 1 workers compensation reinsurance rate level index will not be available until all the final renewal data has been analyzed.

We also observed the following shifting on July 1 program terms and conditions trends:

- Non-earthquake exposed catastrophe programs were renewed flat.
- Pressure to increase rates on earthquake exposed programs resulted in several restructures, in order to hold costs to expiring dollars.
- Working layers are continuing to feel upward rate pressures.
- Regional, rural and smaller employer terrorism reinsurance program capacity is available for companies in order to buy down their Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA) retentions.
- There is increased pressure from reinsurers to pick and choose participations on programs with both working layer and multi-claimant catastrophe layers.

International Casualty - Europe

Motor

UK:

Original rates continued to increase, particularly in the private car sector, where rates are moving upward at an average rate of 1 percent to 2 percent per month. Movements in commercial rates are less pronounced, but year on year rate movements are increasing in the range of 5 percent to 10 percent.

Movements in the original rates, combined with substantial excess capacity in the reinsurance market, mean that reinsurance rates were generally flat. Accounts with good loss experience saw reductions of up to 5 percent.

Periodical payment order (PPO) awards remain a real issue for reinsurers. There are signs that the frequency of such awards is continuing to increase, but the impact on reinsurance pricing is still limited. Similarly, the discount rate issue, very much in evidence at the January 1 renewals, appears to have dissipated in light of the recent announcement by the Lord Chancellor. He intends to review not only the level of the discount rate, but the method of calculation.

The number of reinsurers offering quota share capacity is increasing, and the continued upward movement in original rates may produce further opportunities, as some of the smaller market players become increasingly capital constrained.

Continental Europe:

Across Continental Europe, there are very few reinsurance treaties renewing at dates other than January 1, but the conditions for those renewals have been stable despite recent loss turmoil in other market segments.

Motor liability reinsurance rates remained at a commoditized low price at the catastrophe level. Unlimited cover continues to be available with a surfeit of reinsurance capacity, despite the withdrawal of almost all unlimited retrocession capacity following Partner Re's takeover of Paris Re. Reinsurance rate changes on working layers varied widely in accordance with experience. Social inflation, in particular, medical care costs, had an impact. For example, in Italy and Germany, rates have increased by 5 percent to 15

percent. There is special concern about the impact of under-estimated annuity reserves in certain Eastern European countries.

Quota share treaties continue to play an important role in Germany. A rise in the number and size of quota share cessions in the run-up to Solvency II may be expected. This should coincide with a general improvement in loss ratios as the motor market begins to firm up in response to a period of increasingly difficult results amidst strong market competition in the period 2007 to 2010. Underlying rates in a number of countries have bottomed out, and now that reserve redundancies have been drawn down and the cushioning effect is exhausted, pressure will be felt on rates.

General Liability & Professional Lines

UK & Continental Europe:

Economic difficulties persist in many European Union countries, resulting in depressed turnover and, consequently, lower underlying premiums in general liability business.

There is a concern about the high level of capital needed in the future. It will be needed for allocation to long-tail reserves and catastrophe volatility exposures, as companies prepare for Solvency II. This puts new emphasis on the value of reinsurance for catastrophe and reserve run-off exposures, with revived interest in loss portfolio transfers and adverse development covers. Monoline mutuals are particularly vulnerable due to the high portions of reserves held against relatively small capital bases.

Reinsurance excess of loss renewal rates were generally stable. Although, when they are applied to premium incomes that have declined due to the recession, there is some reinsurance premium shrinkage. Losses, with the exception of the classes specified below, have, however, been benign. Exposure rating discipline is evident in what has become a very technically-oriented market, but good experience can generate significant discounts. There is an abundance of capacity, especially for smaller regional accounts.

In the pharmaceutical, energy, directors and officers and medical malpractice segments, there was an increase in losses, which led to individual loss-affected accounts undergoing both restructuring of coverage and premium increases. Nevertheless, for UK and European insureds, there remains an abundance of capacity, which has partially mitigated premium increases and contributed to a stable market.

International Casualty – Australia & New Zealand

There are a handful of casualty placements in Australia/New Zealand at the July 1 renewal. General casualty rates were flat. Most reinsurers seemed either reluctant or were instructed by their boards to not give up any rate levels. Renewals proceeded on a case by case basis. Where good claims experience and change in exposure mix justified it, reinsurers accepted rate reductions of up to 5 percent.

However, for the most part, reinsurers looked to hold the line. Some casualty reinsurers are bracing themselves for suits filed against various Queensland

municipal councils regarding allowing construction in recognized floodplains, but nothing has materialized, yet.

Professional lines accounts, such as medical malpractice, fidelity and directors and officers, saw rates flat to declining 8 percent across layers and programs.

Life and Accident & Health

Medical

Medical insurance reform remains the strongest driver in this space, with insurers still grappling with concerns around unlimited lifetime maximums and minimum loss ratios. Reinsurers have responded by offering unlimited lifetime excess of loss coverages that have proved popular with some insurers. Pricing for these very high layers, such as unlimited excess of USD10 million per person, is capacity and market-based, as the layers are so far out-of-the money that there is no credible experience. Further, in the short term, many insurers will maintain annual maximums where possible, which will limit observable experience at the highest amounts. Claims and rate-making for the very high reinsurance coverages will be interesting to watch over the next couple of years as the different elements in the healthcare delivery value chain adapt to the new incentives in health care reform.

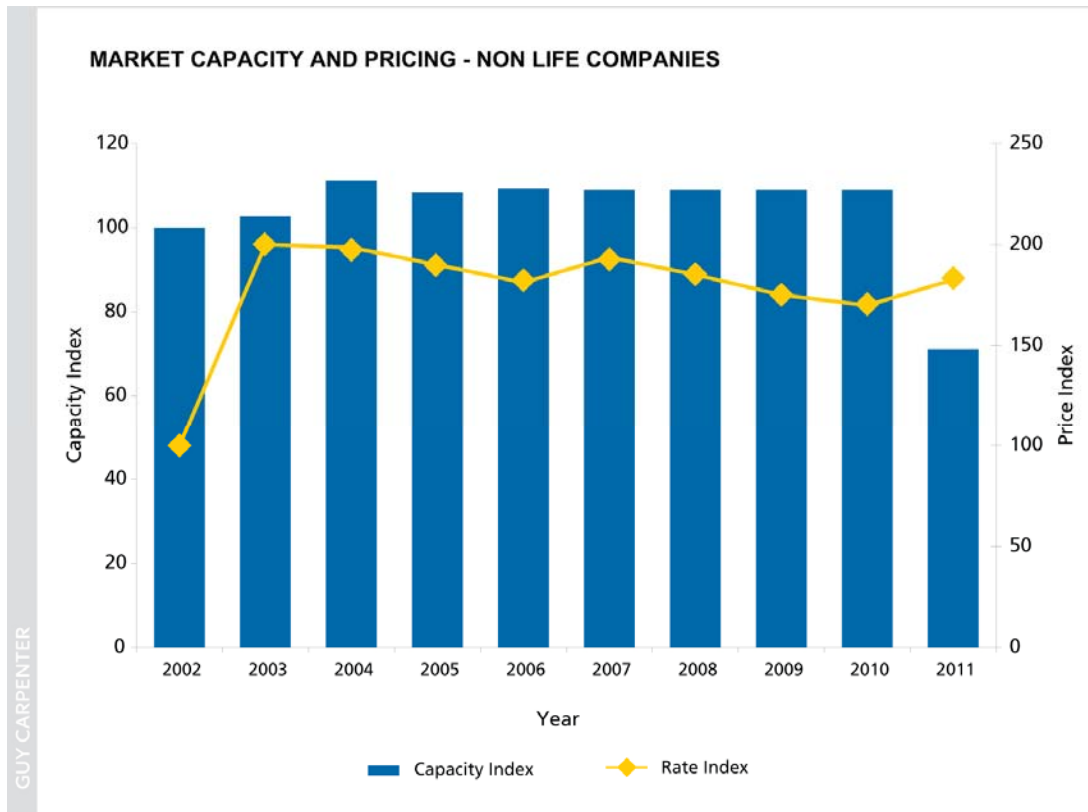
On the demand side, several companies have bought for the first time in the last six months or are exploring a new purchase for the end of the year.

At least as interesting, is the activity on the supply side – reinsurers are hungry for business and have been aggressive, relative to recent experience. Overall, pricing for quota share and working layers held steady, indexing upward a bit below leveraged trend. Pricing for super-high claims seemed to have converged at attachments excess of USD10 million.

Personal Accident Catastrophe

The big story in the personal accident (PA) catastrophe market is the power of available capacity. Many PA cat writers also underwrite property business, and, due to the number of natural catastrophes in the past year, have been working to increase pricing. We would have expected this to carry over into the PA pricing as well, and at first it seemed like it might, but ample capacity from other markets was sufficient to forestall any significant market hardening.

Figure 9: Personal Accident



Source: Guy Carpenter & Company, LLC

The hardest hit may be the Japanese insurers, which are reinsured by a combination of the large European companies, Lloyds and London company markets. Due to the timing of Japanese PA catastrophe renewals, most programs had been quoted by the time of the earthquake and reinsurers stood by their pricing. Ultimately, new capacity came into the market, lower limits were purchased and rate increases were in the range of 7.5 percent to 12 percent, giving back just a bit more than 2010's decreases. The full impact will be better understood next year, as the major markets are expected to revise their earthquake and tsunami loss models.

For domestic US and international programs, the market hiccupped a bit, but settled back down very quickly. Incumbent markets generally pushed for rate increases between 5 percent and 10 percent, but new capacity offered decreases in the 5 percent range up to, an extreme example, 20 percent. Net results were flat to modest decreases, with notable outliers.

How Guy Carpenter Can Help

Guy Carpenter is uniquely positioned to help clients navigate a changing and increasingly volatile reinsurance market. Our services and solutions through GC AnalyticsSM include industry-leading proprietary catastrophe models, actuarial services and capital models. We encourage you to contact your Guy Carpenter representative to review and discuss your risk modeling capital needs in more detail.

For more information, please contact:

David Flandro

Global Head of Business Intelligence

+44 207 357 3267

David.flandro@guycarp.com

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