Reinsurance Market Outlook

April 1, 2011 Update

AON BENFIELD

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Executive Summary — Partnership Performed

The partnership between insurers and reinsurers has rarely had the opportunity to perform in such a highly publicized manner as it has in the first quarter of 2011. Reinsurance has responded to the needs of global and regional insurers as intended. Material volatility has been shifted to reinsurers from the balance sheets and income statements of global and regional insurers. Much greater stability in the regional insurance markets has been achieved because of reinsurance. Affected insurers have gained new or reaffirmed existing respect for the volatility that can accompany frequent chance events.

The string of meaningful regional insurance events has been enough to stir even the thought that a global insurance and reinsurance market turn may be near. While such a global hardening has not occurred, meaningful regional adjustments are afoot. With over $470 billion in capital involved in the reinsurance market, the kind of meaningful capital impacting event that is necessary to stop the decline in U.S. and European markets has yet to occur.

The April 1 renewal season saw U.S. property catastrophe programs including hurricane risks decrease at a rate of 5 to 10 percent. June and July renewals for U.S. hurricane driven programs will find price changes flat to down 5 percent – a decrease in the rate of decrease as reinsurers absorb the results of U.S. hurricane model changes. Few European programs renew in April.

Substantially all Japanese programs renew at April 1. Understandably, a number of the major programs have paused the renewal process through extensions so that the impact of the March 11 earthquake and tsunami can be more fully assessed. Where Japanese catastrophe programs were renewed at April 1, the costs of typhoon programs increased 5 to 10 percent and most earthquake programs increased within a range of 25 to 50 percent.

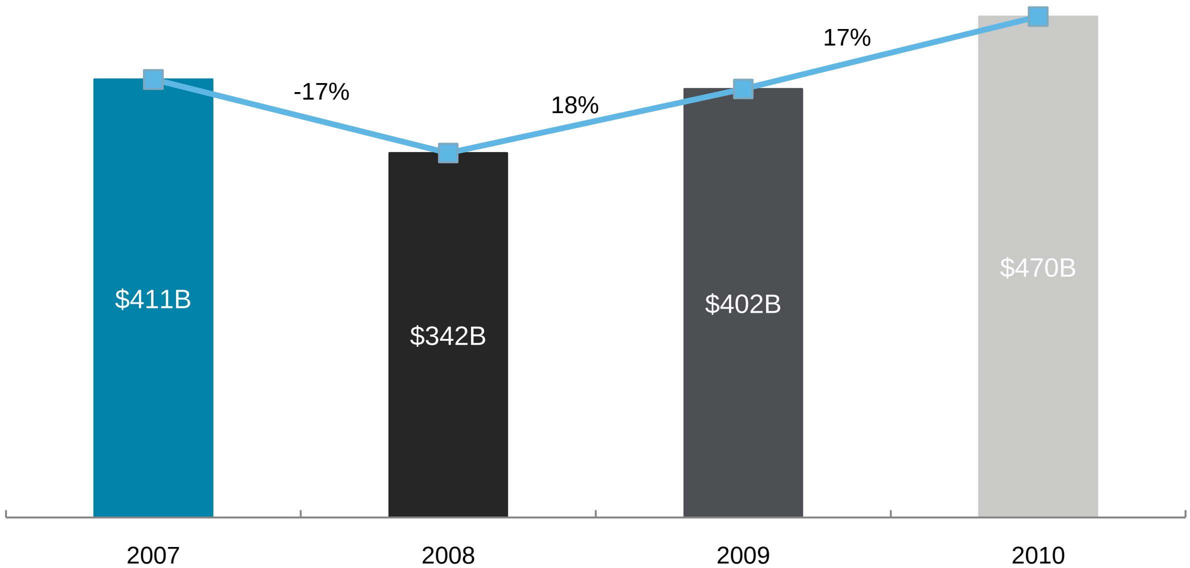
Few reinsurance programs covering New Zealand renew at April 1 where a second major earthquake struck Christchurch in February (following a significant event in September of 2010). Back-up covers, for an assortment of local, regional and global reinsurance programs were in process before the event and continue to be placed today. Many programs cover Australia and New Zealand and there had been weather activity in Australia impacting these programs prior to the most recent Christchurch earthquake. Reinsurance pricing for these back-up covers reflects conservatively on recent experience and is sensitive to the potential of increased insurer retentions.

Just as we witnessed following the regionally significant Chilean earthquake in early 2010, the reinsurance market continues to offer the capacity required by insurers at terms and conditions that remain lower than the cost of insurer's equity capital. The reinsurance market remains functional with its existing capital base. We do not anticipate the need for material new capital flows into the reinsurance market to satisfy insurer demand for catastrophe reinsurance based upon events to date.

Supply and Demand

Capacity ended 2010 at its peak of $470 billion with reinsurer capital change flat from Q3 to Q4 2010. Continued profit led to increased dividends and share buybacks in the quarter that reflect supply being adequate and demand for reinsurance unchanged throughout the period.

Figure 1: Change in Reinsurer Capital

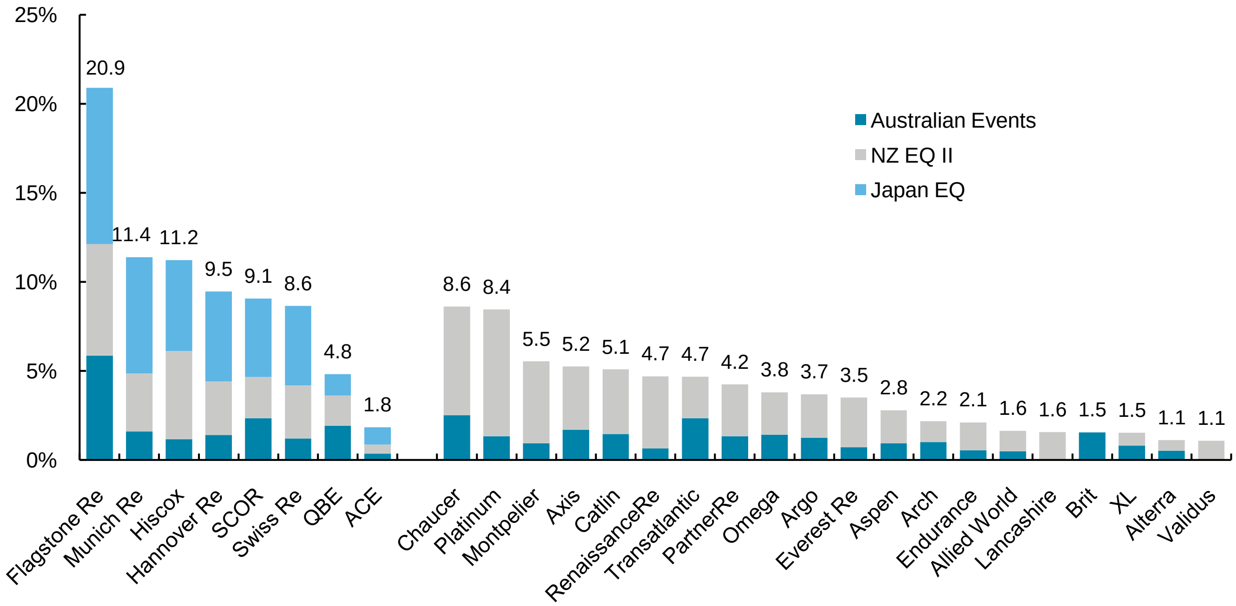


Source: Individual Company Reports, Aon Benfield Analytics

Q1 Catastrophe Loss Impact to Reinsurer Capital

While not all reinsurers have provided indications for estimated losses as a result of the catastrophe events in Q1, the following reflects the information provided to date with regard to losses as a portion of individual reinsurer capital at the beginning of the quarter.

Figure 2: Q1 2011 Catastrophe Losses as Percent of FY 2010 SHF



Note: Midpoints used where a range of loss was reported
Source: Individual Company Reports, Aon Benfield Analytics

Global Market Dynamics for April Renewals

April 1 renewals were impacted by the uncertainty associated with the accumulated events in New Zealand and Japan as well as a material change to the U.S. hurricane component of one of the more popular catastrophe models used by insurers and reinsurers. The following provides an update of renewals in various regions and lines.

Japan

Japan renewals, which are almost entirely placed at April 1, were overshadowed by the Tohoku earthquake on March 11 resulting in an interruption in the renewal process while both insurers and reinsurers contemplated the impact. Even though there is still much uncertainty over the loss, it remains difficult to access the worst areas due to the nuclear restrictions as well as the tsunami devastation.

For the mutual companies that will likely be able to estimate real losses in a shorter term (one to two months), the obvious solution was to extend prior coverage, and this has typically been done for a three month period. Response by the reinsurance industry for this segment has been outstandingly good and reinsurers have been willing to unconditionally extend cover at pro rata to 2010 renewal terms, allowing clients time to assess the earthquake impact and to address any pricing issues at July 1.

For the non-life companies, where the development of loss is less straightforward and where reinsured business covers a broader mix, the aim has been broadly to press on with the 2011 renewals. This has been achieved through some concessions on pro rata commissions and by some significant cost increases on the excess of loss earthquake covers. That said, extensions have been pursued in some cases. The effect of Tohoku on wind and flood excess of loss pricing has been to reverse the previously expected cost reductions.

In Specialty lines, early indications are that reinsurers will be minimally affected by the Tohoku Earthquake since the region devastated is a non-industrial area in Japan. Segments such as Aviation, Specie, Offshore Energy and P&I are not expected to produce significant claims to the reinsurance market. Even in Hull business most of the vessels seen in the media coverage were fishing vessels, whose coverage is largely retained domestically. Only a small number of Japanese ocean-going vessels were damaged, and none of these are confirmed as a total loss so far. As to cargo, there have been few reported large risk losses and at present the overall cost is expected to be relatively small for an event of such magnitude. Also, the Nuclear reinsurance which emanates from Japan is all subject to exclusions which are triggered by this event.

Despite these positive early indications, leading marine reinsurers responded to this additional catastrophe loss by increasing excess of loss prices sharply, as well as cutting ceding commissions on proportional hull treaties. All renewals were completed at April 1.

India

Primary ratings have shown signs of leveling off in 2011 along with improvements in policy deductibles. That said, a number of small to medium size losses have resulted in a difficult proportional treaty renewals in the region. Ceding companies with continued negative results have been particularly challenging at placement.

Quotes for excess of loss programs were affected by the Japanese earthquake and led to many late placements. Pricing on a risk adjusted basis is flat to +5 percent year over year despite the turmoil in the market.

Per risk programs have seen some loss activity on the first layers of programs and pricing has been adjusted accordingly. With this increase in spend a number of companies are considering increasing attachment points.

United States

Despite ceded losses in other regions and additional detail unfolding regarding recent model changes, April renewals saw similar reductions to those in January for property catastrophe business of approximately 5 to 10 percent. Reinsurers quoting programs prior to the late February release of the updated U.S. hurricane model from Risk Management Solutions, Inc. (RMS) honored their quotes after its release. For April 1 programs quoted after the RMS model release, some reinsurers are finding surprisingly larger impacts to their portfolios from the RMS model change and are reacting with reinsurance program quotes that exceed expiring terms. The RMS model change is anticipated to decrease the rate of decreasing rates for reinsurance renewals in June and July 2011.

Despite the potential impacts from Q1 2011 catastrophe losses, there was no shortage of supply for reinsurance capacity on programs renewing on April 1.

United Kingdom

Property catastrophe pricing for Euro wind risk finalized prior to March 11 was in line with reductions of 5 to 7 percent that were achieved during January 1, 2011. After March 11, programs accessing significant capacity from the reinsurance market experienced more difficulties than smaller programs with reinsurers looking for flat renewals year over year. Ultimately, large programs were completed with small single digit reductions on a risk adjusted basis with smaller capacity programs achieving greater reductions.

Primary motor rates continue to increase which is dampening down upward pressure on reinsurance rates. Reinsurance premiums per vehicle on all contracts are inflating with a broad spread, averaging at about 20 percent and greater with middle layers attracting highest increases. The issue of PPO's continues and all parties are awaiting the Lord Chancellors decision on discount rates.

Soft market conditions in liability continue in both the primary and reinsurance sector and renewals saw minimal, if any impact from the recent catastrophe events.

Retro

While the majority of the retro market renews at January 1, a significant portion of the balance comes up for renewal throughout the first quarter. Pricing at January 1 was down approximately 5 percent to 7.5 percent on a risk adjusted basis. Capacity was up marginally year over year with most buyers renewing as before while capacity lost in a few renewals was picked up by new buyers in the market.

The uncertainty surrounding the Japan EQ has created a pricing differential across the market as retrocession writers have reacted differently due to varying loss experience. As we progress through the year and information on the quantum of this loss is released we expect the market to react more uniformly. A number of buyers have sought additional limits or expanded purchase at April 1. Given the high level of international catastrophe events so far in 2011 and the US wind season looming, we expect buyers to be reviewing their portfolios very closely with the aim of protecting / managing their risks sensibly over the next two/three months. Retrocession price spreads for April renewals are flat to +20 percent subject to level territorial scope and the projected business plan for the forthcoming period. Capacity is stable and there are currently no forecast supply issues.

ILW Market

Trade volume at January 1 was flat to down for peak and non-peak triggers. During the first quarter and post the Australian flooding/cyclones and the New Zealand / Japan earthquake events, pricing has reacted firmly with a 20 percent to 30 percent increase on average. Trading for peak trigger contracts has been stable, with upward pressure on pricing of approximately 20 percent for US windstorm and US nationwide contracts following the recent model changes and a mismatch of supply and demand for US windstorm. Irrespective of recent earthquake events, there is still sufficient capacity at reasonable pricing for earthquake triggers.

Expectations for Upcoming June and July Renewals

Our outlook for June and July 2011 renewals remains in line with our forecast at January 1, 2011. Although many reinsurers have not provided guidance on losses for the Tohoku Earthquake, record high capital at the beginning of the quarter suggests that current expectations of ceded recoveries will remain at a level that will not cause a major shift in the remainder of the global reinsurance market. Our expectation is that renewals in peak zones in the United States and Europe throughout the remainder of the year will be minimally affected by the reinsurance losses incurred during the first quarter of 2011. With major market renewals in the United States throughout the remainder of the year, we provide our views on how the reinsurance market is likely to continue throughout 2011.

Figure 3: June/July 2011 Renewals

	ROL Changes	Capacity Changes	Retention Changes
Personal Lines National	-5% to Flat	+5%	+5% to +10%
Personal Lines Regional	-5% to Flat	+10%	Stable
Florida Homeowners Specialists	-5% to Flat	+5%	Stable
Standard Commercial Lines	-5% to Flat	+10%	Stable to +10%
Complex Commercial Lines	-5% to Flat	+10%	+5% to +10%

Assumptions: No changes in insured catastrophe exposures. Rate of change measured from the expiring June/July 2010 terms.
Source: Aon Benfield Analytics

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