

August 2010



Review of the Marine
Hull Insurance market

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JLT is an international group of risk specialists and employee benefits consultants and one of the largest companies of its type in the world. We offer a distinctive choice to our clients and partners through our combination of independence, scale and specialism.

As an independent business, we are able to operate with autonomy and flexibility. We have the scale to provide solutions to the complex demands of the world's leading companies and to deliver global servicing whilst recognising that the needs of each of our clients are unique.

By developing highly specialised services, we provide our clients with a depth of expertise and experience. The value we create is driven through the personal determination of our 6,200 highly motivated and skilled people.

Overview

A review of the past 12 months in the marine hull insurance market can only be made mindful of the developments in world trade, the global financial situation and the impact this has on the shipping industry.

In addition to these global influences we have the insurance industry issues of fluctuations in capacity, the potential impact on both rating and image for the “Deepwater Horizon”, the piracy crisis in the Gulf of Aden (including the US Executive Order) and Iranian sanctions.

Within this paper we provide a commentary on these issues and offer our own view of the current situation in the marine market and where we believe the hull insurance market will be in the next 12 months.





Shipping Industry

The current climate for owners remains testing with many shipping companies still facing very difficult situations. World industrial output is down on recent years and world demand for oil has not increased as much as projected in 2009. The container trade has been through possibly the biggest slump this sector has ever seen and vessel values have dropped correspondingly over the past 12 months. We have seen a promising upsurge in the past few weeks which hopefully will be sustainable in the long run.

Over the past 12 months shipyards were left with a “toxic orderbook” due to the gap between contract and market prices. There are still a considerable number of new buildings to be delivered and establishing a line of credit remains challenging. This has led to some operators being left in a very difficult position, in some cases requiring the renegotiation of new building contracts, both in terms of price as the gap between contract and market price widened, and delivery which clearly Shipowners wanted to defer until the market improves or credit becomes more readily available. In some cases where renegotiation has not been successful this has led to increasingly complex and unpleasant legal disputes.

The industry has faced an up-hill battle due to downturn in demand against oversupply. The management of this oversupply will be the biggest challenge the shipping industry faces over the next few years, and obviously much will depend on how future demand develops.

Perhaps not surprisingly given the annually renewable nature of our business the financial downturn in world

trade had a delayed impact on the marine insurance market. We have seen a huge reduction in insured hull values and an increase in the number of vessels being laid up. These trends continued until recently where in the last few weeks we have seen values being increased and vessels being reactivated. In some sectors we have also seen a number of new buildings being delivered. From a marine insurance perspective, lower values, lay ups and therefore reduced exposures meant reduced premium volumes coming into both the Hull and Loss of Hire markets which has generally been the trend for the past nine months.

Underwriters remain concerned that the apparent lack of liquidity Owners and Operators are experiencing will impact vessel maintenance but this concern has not translated into any increase in claims activity. Strict regulations and the high standards maintained by ship owners generally have ensured this concern has not manifested itself.

We have seen a greater focus from underwriters on Owners' financial commitments, with disclosure of mortgage arrangements becoming a common request. The potential for late premium payment is also of some concern and tight credit control monitoring is commonplace. This activity is now generally outsourced in the London market where the underwriters themselves have little influence on extending terms of trade.

The "Deepwater Horizon" case will undoubtedly have an impact on the image of the shipping sector and the



carriage of energy related products by sea which the industry has fought so hard to improve over the years. The offshore energy sector will obviously feel this far more keenly both in terms of image and increases in rates. In our opinion we do not believe that this claim will have a negative impact on marine insurance rating. Whilst a number of treaty reinsurances are placed on a combined energy and marine basis we could see some capital providers reallocating capacity into what they consider more stable classes of insurance.

Piracy remains a concern for Underwriters, Owners and Operators alike, with vessels trading through the Gulf of Aden and Indian Ocean having to cope with the peril, exposure and cost of Piracy. This crisis seems set to continue with in excess of USD 300m in ransoms and associated costs having now been paid out by the insurance industry over the past two years. Underwriters are becoming increasingly nervous about the spread of this activity to 1,000 miles off the Somali coast.

The White House Executive Order 13536 on 12 April 2010 has applied more pressure and an even tighter

framework within which the shipping and insurance industries are able to deal with this criminal activity. We have written a separate paper on this subject providing guidance to owners and operators on the impact on this order and under what circumstances OFAC need to be contacted. Please visit www.jltgroup.com/piracy-insurance.

The United Nations Security Council adopted Resolution 1929 imposing additional sanctions against Iran which strengthened the existing measures in place. The EU is expected to implement this Resolution with further substantive sanctions in the near future. The sanctions stipulate that no insurance or reinsurance contract can be provided relating to the movement of refined petroleum products to Iran.

This is a developing situation but the depth of international concern regarding Iran and the need to carefully and diligently monitor compliance with all existing and future sanctions against Iran is paramount. A Lloyd's Market Bulletin was issued on 8 July 2010 (reference Y4409) to direct the market accordingly.

Marine Hull market

There remains a plethora of capacity for marine hull insurance in the market which creates a very competitive trading environment. The renewal season in January illustrated this being relatively stable with few headline increases and owners renewing for the most part on an “as expiry” basis for those with good records.

Whilst straightforward reductions are rare we have seen various mechanisms being used over the past three months which realise the same net effect to owners contingent on continuity, loss ratios or premium payment. We suspect that over the next 12 months longer term policies will again become more prevalent subject to the provisions of LSW 196A (Notice of Cancellation Clause for long term policies).

These comments relate to the market in general as undoubtedly there are certain specialised shipping sectors which have their own unique variables for which a specialist market has developed within the insurance industry, for example the offshore industry, overside equipment sector, the Yacht market and the Gas industry.

We continue to see banks demand quality security and anticipate that their requirements will become ever more prevalent in the marine insurance sector as has been the trend over the past few years.

We have also seen a greater differentiation between good operations with good loss records and sub standard operators who have a history of attritional losses. The market is generally making it harder to obtain all risks coverage from quality security at a cost effective price where there is evidence of poor maintenance. The emphasis is very much on the quality of the operation rather than the age of the tonnage as well run older vessels can be considered an attractive proposition in some markets.



Changes in capacity over the past 12 months and regional visibility

In recent years we have seen additional capacity for international business evolving from a number of markets including London, Holland, France and Russia. Some of these are new operations but there are a number of underwriters who were previously not writing International marine business who now have a remit to provide capacity in that arena. In the Middle East and Singapore we now have access to a number of operations which previously had a solely domestic focus.

By the same token a number of European operations have continued to pursue and bolster regional office strategies in order to become better aligned with the local industries. For example there are now a number of household names established in the Middle East and Singapore including AxA, RSA, Watkins, Catlin, Groupama and Chaucer all with marine capability. This in itself does not mean that capacity has increased rather it has been redistributed and become more visible in those regions. It does however mean that there is more focused competition in those now mature markets.

The new capacity joining the Marine market or about to join the Marine market include the following:

Montpelier Re	– Lloyd's
WR Berkley	– Oslo
Barbican	– Lloyd's
Laveretus	– Power Barge specific
WR Berkley	– Soon to write marine from Lloyd's
DMI	– Dutch Marine Insurance

Consolidation in the Marine market includes the following:

- Amlin purchased Fortis Corporate Insurance for EUR 350m. 3 June 2009
- Codan (a subsidiary of RSA) purchased TrygVesta Forsikring A/S marine book of business in April 2010

The net effect of this movement is more Marine capacity has been entering the market and will continue to do so towards the end of this year.

One of the reasons that capital providers are attracted to the Marine market is the lack of volatility. The peaks and troughs in the market have become relatively soft over the past few years. This obviously depends on the classes on which companies have focused and sectors in which they specialise. The following Lloyd's "T" risk grouping code figures illustrate the average loss ratio for the marine market over the past few years.

Hull Results to the Lloyd's market "T" Account

Year	Loss ratio
1999	139%
2000	116%
2001	91%
2002	92%
2003	59%
2004	78%
2005	80%
2006	90%
2007	96%
2008	90%
2009	61%*

- * (Six quarters' figures on triangulation)
- Figures are gross loss ratios

Source: Xchanging Data & information services.

Outlook

With the number of new Marine insurers continuing to enter the market the combination of increasing supply of capacity against relatively static demand will put rating levels under

constant pressure over the next 12 months. This year has, so far, not produced the headline marine losses we have seen in the past. Investment returns for underwriters have also increased

considerably compared with last year. This trend will assist in containing rating and deductible levels which if maintained we expect to be borne out in the December reinsurance renewals.

Construction and Conversion

The Builders Risks' market remains relatively soft with a number of underwriters now participating in this arena which has proved for some to be a profitable move. Underwriters who may not have made the profits anticipated under their "T" code are often able to rely on the balance of their "TS" code business to provide some balance to their portfolio.

This is becoming an increasingly specialised market requiring technical expertise and detailed

understanding of the associated risks especially in the offshore and mega yacht sector. There have been a significant number of conversions especially in the FSO/FPSO sector and this is a trend that is expected to continue as some of the major project around the globe come to fruition. Whilst the final contract values involved in these projects are significant there is enough capacity in the market to provide the protection required. We forecast that rating will remain stable in this sector over the coming months.

Ancillary Interests

Capacity for Disbursements, Hull interest, Mortgagees interest, Cash on Board and other ancillary marine interests as with previous years remains plentiful. Competition for attractive business remains strong and a number of facilities are readily available in the market with a number of alternative leading underwriters.

War Market

This class of business is dominated by the London market and by domestic War pools in some of the world's leading maritime nations. There is plenty of capacity for war risks and this is a very competitive market. The dynamics of the war market has led JLT to develop a number of very innovative War risks structures to assist owners and charterers alike.

In the past 12 months the exposure to this market has changed dramatically with most owners moving the peril of Piracy (where applicable) from the Hull clauses to the War placing. This provides clarity of coverage for owners and avoids the

application of a deductible in the event of a hijacking and protects owners' Hull records against a ransom claim. Whilst this has led to the application of additional premiums on charterers/owners we have also seen a significant number of ransom payments made. As we mentioned earlier we estimate the market has paid in excess of USD 300m in ransoms and associated costs to release vessels from Somali hijackers in the past 24 months. We have also seen a number of vessels sustain damage during attacks and hijackings.

The industry continues to monitor the situation in the Gulf of Aden/Indian Ocean very carefully and maintains a regular

dialogue with a number of shipping organisations, for example BIMCO, ICS and Intertanko who have been instrumental in ensuring the insurance industry is regularly consulted at IMO working groups and alike on this crisis.

The areas of "perceived enhanced risk" in general are subject to closer scrutiny than ever before with Aegis providing the Joint War Risks Committee (JWC) with regular advice and global intelligence. These listed areas are amended on a far more regular basis than in previous years to more realistically reflect the increase or decrease in global tensions in specific areas around the globe.

Special Contingency Cover

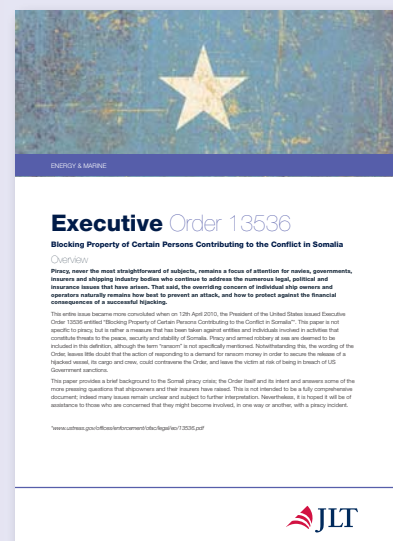
The Special Contingency or Kidnap for Ransom (K&R) market has not previously been the domain of mariners but with the advent of hijackings on the high seas of the scale recently experienced this class of business has developed considerably. There are now a number of underwriters in the market providing this type of coverage. A few have also incurred some of the losses referred to in the previous section and whilst there remains plenty of capacity for this exposure we have seen some increase in premiums on transit rates by some insurers recently who do not believe the market can be sustained at the current levels.

This is traditionally a Personal Lines coverage and therefore amendments to the wording have been essential to reflect the requirements of the marine industry. These include the waiver of subrogation against Hull or War underwriters to ensure that this is a first loss policy and also, where required, the placing is extended to include the property as well as the crew.

The existence of such a policy is highly confidential. The more specific advantages that can be derived are documented in our white paper "Piracy Coverage and Response" which can be found on our web page www.jltgroup.com/piracy-insurance

Jardine Lloyd Thompson Limited (JLT) have formed a Piracy Forum to harness the expertise of the marine team and the Financial Risks Security and Political Risks Division in order to monitor the international, political and legal arena, and assess the impact on the shipping industry and insurance market.

This forum ensures that JLT remain at the forefront of developments relating to this crisis which in turn enables us to design solutions and respond to clients concerns as they arise.



Business Interruption

Supply in the Loss of Hire market is far more keenly matched with the demand. This has been the case for a number of years and whilst we see the occasional rally with rates reducing this is the exception rather than the rule. London has a small and highly selective Loss of Hire capacity for placements on a stand alone basis and participation is normally dependant on a combination of Hull and Loss of Hire income. The Scandinavian market has traditionally had more success with this class of business and captures the majority of domestic and international owners.

The demand for Loss of Hire has not increased in the last 12 months which is perhaps not surprising given the dynamics in the shipping markets and financial institutions to which this coverage is often linked. We anticipate demand for Loss of Hire will increase as the market gathers pace that income stream protection will assist not only in the extension of credit but the basic protection of balance sheet exposures.

London-based Transmarine continue to grow their business as a stand alone specialist provider and leader in Marine Trade Disruption and Consequential Loss insurance. Writing 100% of risks this market

provides a real alternative to standard Loss of Hire cover with its product differentiation. The comprehensive policy wording provides a one stop solution to purchasing conventional stand-alone policies such as Strikes, Loss of Hire/Earnings and Cruise Indemnity.

The Strikes Club based in Monaco have also come to the fore in the past 12 months providing innovative coverage for delay exposures which are not readily available in other markets.

Underwriter transfer market

The following individuals have transferred or have announced a transfer around the hull underwriting community in the past 12 months.

- | | |
|--------------------------------------|--|
| From Aon to Swiss Re | - Peter Townsend/Lee Bright |
| From Swiss Re to Montpelier Re | - Mike Southgate/Mike Thompson/Chris Stafford-Hill |
| From Talbot to WR Berkley | - Louise Nevill |
| From Codan to Barbican | - Gary Sangedal/Suzanne Ward |
| From JLT to Watkins syndicate | - Emma Russell |
| From RSA to Catlin | - Keith Potter |
| From Fortis to DMI | - Ernst-Jan Sundermeijer |
| From Gerling Oslo to Bergvall Marine | - Mona Haakonsen |
| From NEMI to WR Berkley Oslo | - Bjorn Olav Norbye/Eva Bye |
| From Catlin to Amlin | - Iain Henstridge |
| From Swedish Club to Skuld | - Clas Ryden |
| From Swedish Club to Skuld | - Rune Bagenholm |
| From ACE to Liberty | - Rob Henbury |



JLT Marine Capabilities

At JLT we constantly look to align our business with the shipping industry and the various sectors we serve. We aim to continue to be flexible enough to do that so we can continue to assist owners and operators with their existing exposures and also their future aspirations.

Our marine division is one of the largest in the world looking after the interests of some 5,000 vessels from coastal tonnage to USD1bn FPSOs. We also look after a third of the world gas fleet and many of the world's largest port and terminal operators. We place in excess of USD 260m of marine premium into the market and handle over 1,500 claims each year.

We take pride in our service and the business that we have grown as part of a consistent team over a number of years. We have an average of 14 years service within our team. Our approach to business is different from other brokers which ensures that we deliver the best results to our clients.

We specialise in marine risks from traditional Hull and Machinery and P&I to Financial, Credit and Political risks exposures. We maximise the coverage with underwriters to ensure that our clients get value for money.

The size of our book also gives us the capability to leverage the best deals for our clients. For example, we are the largest producer of tanker business to the providers of COFR guarantees and hold a similar status with a number of the leading marine insurers in the world.

Most importantly we understand the shipping industry and the numerous pressures of operating in that arena. We ensure that the time and effort and considerable expense put into running operations are fully appreciated by insurers. We structure deals that are sensitive to an individual operator's position in the marketplace to enhance their trading position.

We invest heavily in spending time with our clients to understand their technical operation, aspirations and culture. When accidents happen we are there to swiftly get you back afloat. Our senior executives travel extensively to maintain this approach and we encourage the lead insurers to visit your operation for themselves to facilitate an understanding and co-operation which is in our view essential to getting the best value.



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