

Reinsurance Market Outlook

Value Creating Capital

September 2011



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Executive Summary— Value Creating Capital

Much of the industry dialogue following the most recent insured world catastrophe events has centered on reinsurance price, price movements and reinsurer returns. Indeed, we established and achieved goals for our firm’s performance for clients that included price change objectives where leadership was required in non-loss affected regions.

In this reinsurance market outlook report, we monitor the usual predictive price variables like reinsurer and insurer capital, rating agency standards and actual catastrophe losses. We also spend considerable time on the value delivered to insurers through their partnership with reinsurers. Reinsurance capital continues to provide financial stability for many insurers and their shareholders. Reinsurance capacity is widely available at earnings and capital cost accretive terms. Every insurance market that has been stressed by recent catastrophe losses has seen orderly renewals of reinsurance capacity at pricing, while higher, that implies a cost of capital that adds value to insurers, their insureds and their shareholders.

Insured loss estimates for recent events from Impact Forecasting, Aon Benfield’s wholly owned catastrophe model development firm, are revealed for the first time in this report and reflect our on-the-ground research and analysis. Important insight from this work informs our views of the needs of our clients in future events. Variations in modeling results from a variety of firms are important to consider and we add materially to that discussion through Impact Forecasting. Reinsurance, importantly, covers both the modeled and the non-modeled losses and provides certainty for the uncertain algorithms used in models—and that too adds value.

The insurance cycle remains challenging and the focus on reinsurance price, price movement and comparative insurance market “discipline” can defeat the opportunity for the market to do more with insurance partners following stressful events. Worse yet, price rather than value discussions can erode existing partnerships through raised retentions and short placements. Clear evidence of this pattern is exhibited in the latest seven years of the global casualty reinsurance market.

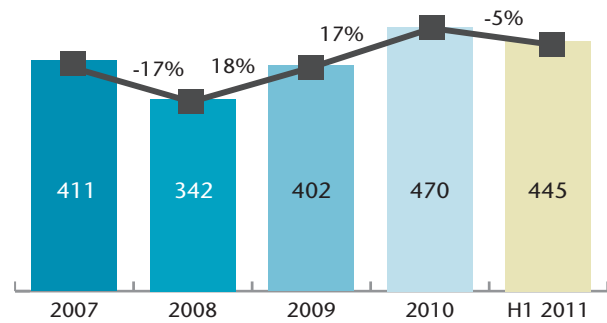
Reinsurance has a terrific record of pricing risk at terms that add value as an earnings and capital protection tool. Reinsurance underwriters are likely to end the year in a stronger capital position than the beginning of the year—as will insurers. The products provided by insurers and reinsurers are declining in their role in mature economies even though risk throughout those economies continues to grow. Insurance and reinsurance partners can collaborate, innovate and add more value to insureds.

Note: This reinsurance market outlook report should be read in conjunction with our firm’s views on rate on line, capacity and retention changes for each cedent’s market. Our professionals are prepared to discuss variations from our market sector outlook that apply to individual programs due to established trading relationships, capacity needs, loss experience, exposure management, data quality, model fitness, expiring margins and other factors that may cause variations from our reinsurance market outlook.

Capacity: Supply Remains Adequate Despite Catastrophes

Reinsurer capital is more than likely to end the year at a level higher than the USD470 billion at the start of the year. The second quarter showed a linked-quarter increase and without events in excess of expected second half losses, reinsurers will again have capacity in excess of demand from insurers in every region. Continued pressure on primary pricing has made any desired increases in demand difficult to budget for during recent years and capacity remains adequate to supply the current needs of insurers. While the impact of new model versions and recent loss activity may shift the balance of supply and demand going forward, our expectation is that supply will meet those needs causing no further impact to pricing in peak loss-free catastrophe regions.

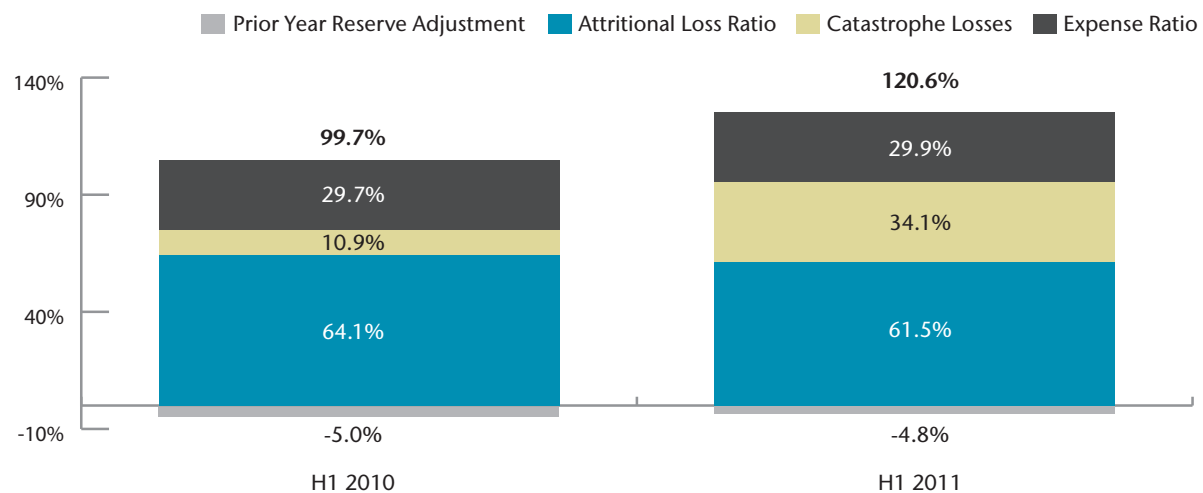
Exhibit 1: Reinsurer Capital Change (USD Billions)



Source: Individual Company Reports, Aon Benfield Analytics

Following major events in Japan, Australia and New Zealand in Q1 2011, Q2 tornado hail losses were substantially retained by insurers. For the 28 reinsurers that comprise the Aon Benfield Aggregate (ABA), H1 2011 ended with a combined ratio of 120.6 percent compared to 99.7 percent for the same period last year. Catastrophes throughout the first half contributed 34.1 percent to the combined ratio compared to 10.9 percent in the prior year while the attritional loss ratio, expense ratio and prior year reserve development were similar to 2010.

Exhibit 2: Aon Benfield Aggregate¹ Impact of Catastrophe Losses on Combined Ratio

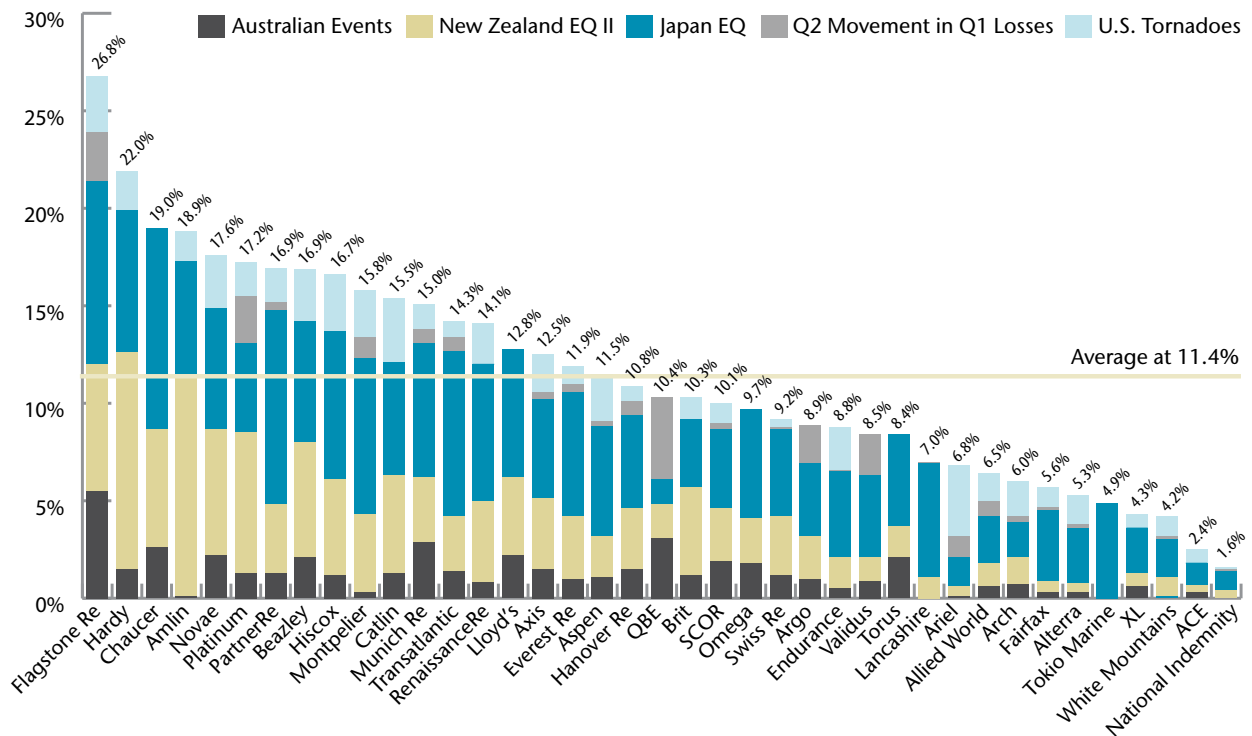


Source: Individual Company Reports, Aon Benfield Analytics

¹ The ABA is a group of 28 of the world's leading reinsurers; latest ABA study can be found at <http://thoughtleadership.aonbenfield.com/ThoughtLeadership>

Many reinsurers reported movement in Q1 losses with Renaissance Re and ACE being the only companies adjusting losses downward by 0.1 percent impact to shareholders' funds.

Exhibit 3: Major Reinsurers and Insurers Impact of Catastrophe Losses on Shareholders' Funds



Source: Individual Company Reports, Aon Benfield Analytics

Aon Benfield Securities Annual Review of the Catastrophe Bond Market

For the 12 months ended June 30, 2011, the Insurance-Linked Securities (ILS) market again demonstrated its consistent strength and provided sponsors with an attractive alternative to complement their traditional reinsurance purchases. Two stories emerged in the last 12 months:

- > A healthy and growing market in the first nine months capped by a very active issuance calendar in the fourth quarter of 2010 and the first quarter of 2011, and
- > A market interrupted by model changes and natural catastrophes in the second quarter of 2011.

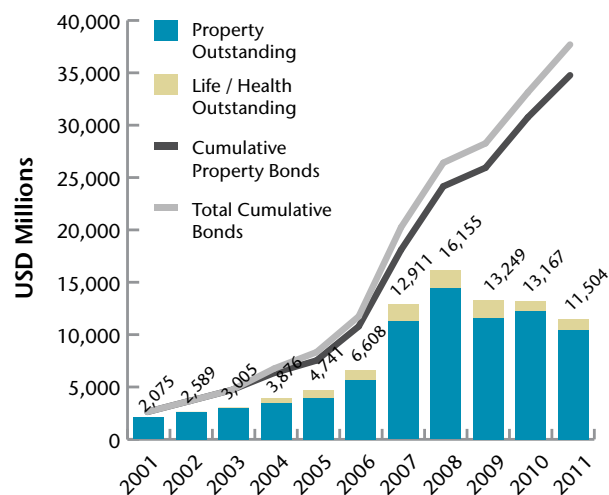
Overview

Despite the continued confidence of both sponsors and investors, along with steady issuance, outstanding bonds on risk declined over the 12 months ending June 30, 2011. The annual issuance volume was only marginally down at USD4.4 billion, from USD4.7 billion for the same period in 2010. The total bonds on risk as of June 30, 2011, however, finished at USD11.5 billion, down almost USD1.7 billion from the previous June 30. The overall decline was caused by the interruption of issuance in the second quarter of 2011, as well as large maturities of catastrophe bonds issued in 2007 and 2008. In all, the catastrophe bond market has seen USD37.6 billion of cumulative issuance since 1996, demonstrating its importance as a strategic and efficient risk management tool.

Issuance in the 12 months ending June 30, 2011 was overshadowed by two major factors, which slowed the growth of the ILS market. First, in 2011, Risk Management Solutions (RMS) completed major updates of its U.S. Hurricane Model and Europe Windstorm Model in February and July, respectively. Both updates are explained in more detail below (see “Market Drivers > RMS”). The RMS changes came after AIR Worldwide Corporation (AIR) had updated its models for the same risks in 2010. Even at time of publication, nearly six months after RMS issued version 11.0 of the U.S. Hurricane Model, sponsors and investors alike are still working to thoroughly understand the changes.

Second, on March 11, 2011, a mega-earthquake and tsunami, known as the Great East Japan Earthquake, struck the northeastern coast of Japan. This and other natural events (see “Natural Events” affecting the ILS market) led to a brief pause in the ILS market as both sponsors and investors assessed their impact. During this period, some investors also took time to rebalance their portfolios.

Exhibit 4: Outstanding Catastrophe Bond Volume, 2001–2011 (Years ending June 30)



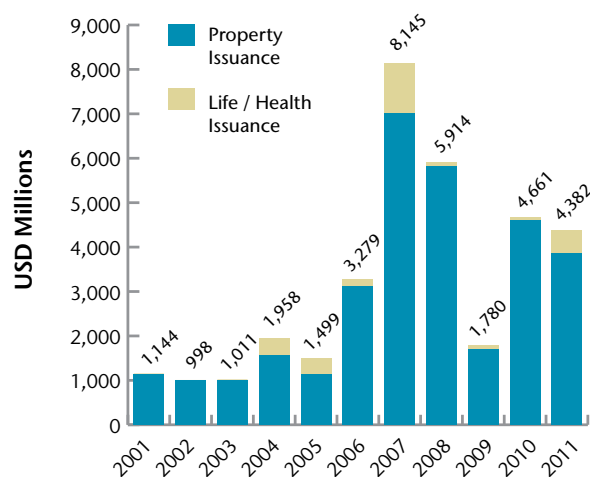
Source: Aon Benfield Securities

Transaction Review

Twenty-four transactions totaling USD4.4 billion of issuance (including four deals from the life and health sector) closed during the 12-month period ending June 30, 2011, compared to 21 transactions over the same period in the prior year. U.S. hurricane risk continued to dominate the market, with 53 percent of natural catastrophe issuance dedicated to this peril. The proportion of catastrophe bonds covering U.S. earthquake risk declined from 29 percent for the year ending June 30, 2010 to 17 percent for the same period in 2011.

By comparison, Europe windstorm transactions increased from 9 percent of issuance in the 12-month period ending June 30, 2010 to 21 percent for the same period in 2011. U.S. earthquake risk and Europe windstorm risk now price alike for a given level of risk. Life and health issuance activity rebounded with USD525 million of issuance, the second largest issuance year following USD1.1 billion for the year ending June 30, 2007.

Exhibit 5: Catastrophe Bond Issuance by Year
(Years ending June 30)



Source: Aon Benfield Securities

Market Drivers

> Supply and Demand

Despite the fact that June 2011 renewals that experienced losses in Australia and New Zealand were priced higher than those in 2010, Aon Benfield clients seeking to transfer U.S. risk through the traditional reinsurance market in the second quarter of 2011 found the market to be priced the same or even marginally lower than the previous year. These prices were consistent with prior forecasts published by Aon Benfield. With stable or lower traditional reinsurance costs and ample capacity, sponsors saw no significant price advantage nor capacity requirement in using ILS for a part of their reinsurance needs.

That said, sponsors continued to recognize the positive effects of diversifying their sources of reinsurance capital by periodically issuing ILS to the market. The number of repeat issuers during the past 12-month period demonstrated sponsors' desire to maintain relationships with investors and cultivate the ILS market as a source of reinsurance capacity.

From the buy-side perspective, investors found themselves with additional capital to invest following, in some cases, successful capital raising efforts in the prior 12 months. This led to some increased demand during the period, particularly for diversifying peril transactions, but in many cases, available capital was either held on the sidelines or invested in other markets.

> RMS

At the time this report is being prepared, sponsors and investors alike are still working to thoroughly understand the RMS updates in version 11.0 of the U.S. Hurricane Model. RMS implemented changes to both the Industry Exposure Database (IED) and to the model itself. Although the RMS model updates primarily drove the increase to the model loss curves, the total industry property exposure also increased by 12 percent across hurricane-exposed states. Commercial lines experienced a larger increase at 18 percent, compared to 8 percent for residential lines. It should be noted that the prior hurricane IED had a 2008 vintage.

Both the wind and storm surge hazard modules in version 11.0 of RMS' U.S. Hurricane Model have been pushed farther inland. The wind vulnerability module has been updated to include claims data from Hurricane Ike, where previous data was sparse. The module was also updated with reevaluated data from the 2004–2005 seasons. The commercial lines' average annual losses and select return periods are generally higher, both from the IED and Industry Loss Curves (ILC). Due to the increased inland hazard, the Texas and mid-Atlantic regions have the greatest increases for the ILC. The increased inland hazard is only partially offset by reduced coastal hazard. It will take sponsors some additional months to complete this process and implement rate changes.

While we have seen some relatively small price decreases in RMS-modeled hurricane bonds in the secondary market, the ratings downgrades of those bonds do not appear to have had any material impact on prices as of the date of this report.

The market has yet to digest the full implications of the Euro windstorm model released in mid-July. Aon Benfield has begun the process of model testing and evaluation of both Europe as whole and territory by territory perspectives. Our initial conclusions differ by country and, while the changes in some jurisdictions have improved, a number of areas have yet to be fully contemplated. For example, there are some countries that currently appear to exaggerate loss potential at the lower end of the curve. Equally, there are increases at the higher end of the curve for other countries which has not been verified with actual loss experience.

> Natural Events

A magnitude-6.1 earthquake struck New Zealand's South Island on February 22, 2011, causing widespread damage, fatalities and injuries. Extensive damage occurred throughout Christchurch. Given the intermingled damages from the Darfield earthquake of September 2010, which also impacted Christchurch, determining insured losses from the event proved to be extremely difficult and complex.

The Great East Japan Earthquake, which led to a full loss for the Muteki Ltd. Series 2008-1 Class A (Muteki) transaction and a partial loss to Vega Capital Ltd. Series 2010-1 Class D's Reserve Account, caused two other bonds—Montana Re Class E and Topiary Capital Limited (Topiary)—to be on-risk for the next event.

> Maturities

For the 12-month period ending June 30, 2011, approximately USD5.7 billion of natural catastrophe bonds matured. Since most of the matured transactions originated in 2007 and 2008, the period with the greatest historical ILS issuance thus far, it is not surprising that the amount of maturities exceeded the amount of new issuance, thus causing the market to decline in the overall value of bonds outstanding. We expect to see a reversal of the trend in 2012, as the 2009 issuance year is the lowest since 2005.

Outlook

Conditions remain positive for catastrophe bond issuance for the remainder of the 2011 calendar year. As noted, investors have strong demand for bonds, particularly those with non-U.S. hurricane exposure. Both repeat and new sponsors are expected to issue into the ILS market for diversification and to complement overall reinsurance purchases. Both sponsors and investors alike are working through the model change issues and will collectively work to form a commercially acceptable view of risk and return.

We expect that more non-U.S. risk will be ceded to the market in the near term. PERILS will have a positive impact on issuance for Europe perils and ILS will provide increasing support for the markets that have experienced loss from recent natural catastrophes.

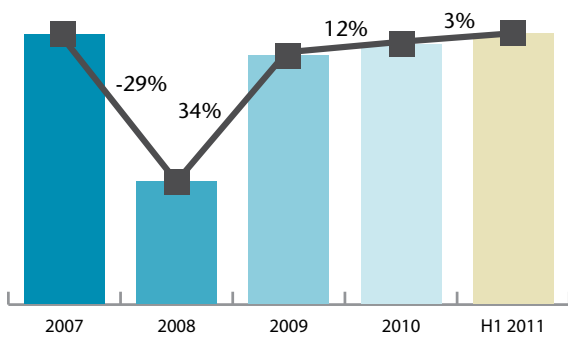
Finally, investors will continue to regard ILS as a viable option that has consistently provided competitive returns versus similarly rated corporate securities. Despite losses from the Great East Japan Earthquake, ILS returns for the 12-month period ended June 30, 2011 were 5.97 percent. Also as noted, investors have successfully raised additional capital that must be put to work.

For more details, please reference our latest annual ILS report ("Consistency and Confidence 2011") that was issued on August 31, 2011 and can be found at <http://thoughtleadership.aonbenfield.com/ThoughtLeadership>.

Insurer Capital Stable for 2011

Insurer capital increased 12 percent from year end 2009 to year end 2010 and despite significant natural catastrophes and insured loss throughout the first half of 2011, capital rose by 3 percent.

Exhibit 6: Insurer Capital Change

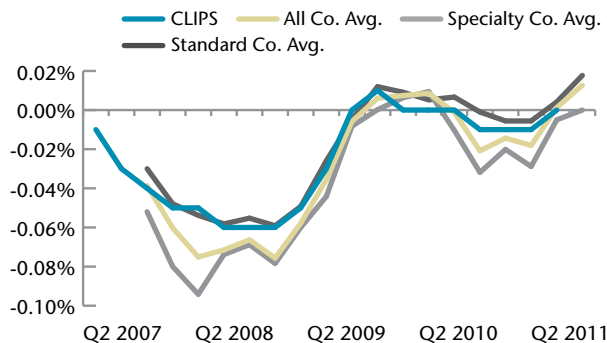


Source: Individual Company Reports, Aon Benfield Analytics

U.S. Primary Rates Show Positive Signs

Although a major loss event hasn't been a catalyst to an industry-wide market hardening, some lines are showing signs of stability. Aon Benfield's summary of rate change shows an all company average of 1.3 percent, with standard lines achieving rate increases of 1.8 percent on average, and specialty lines flat for the quarter.

Exhibit 7: U.S. Primary Pricing Trend

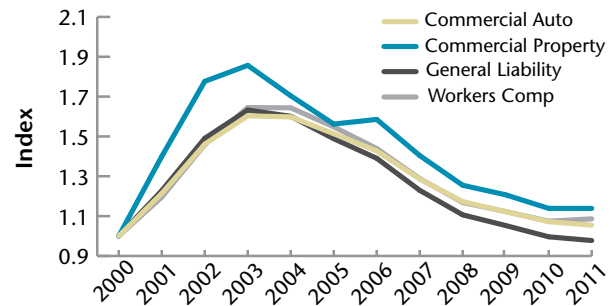


Source: Towers Watson and Aon Benfield Quarterly Rate Monitor Report

Exhibit 8 shows CIAB results that also indicate rates may be nearing the bottom with each of the lines of business included resulting in smaller decreases or rate increases compared to both last year and Q1 2011. Workers' compensation (on the decline since Q2 2004), and commercial property (on the decline since Q3 2006) saw rate increases for the first time.

Exhibit 8: U.S. Primary Pricing Trend

	2010	Q1 2011	Q2 2011
Commercial Auto	-4.45%	-2.24%	-1.01%
Commercial Property	-5.64%	-1.98%	1.96%
General Liability	-5.37%	-2.79%	-0.95%
Workers Comp	-4.29%	-1.55%	3.72%

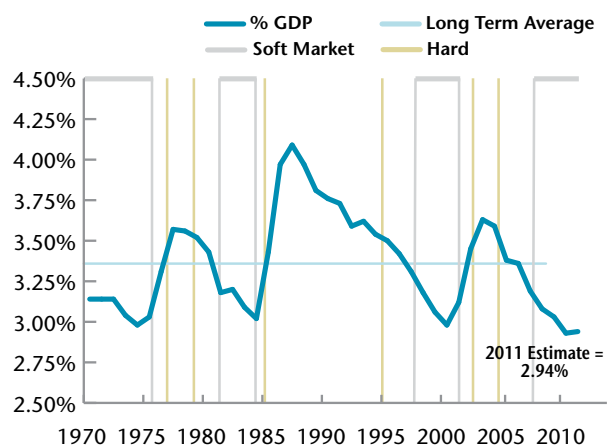


Source: Council of Insurance Agents & Brokers

NWP to U.S. GDP Shows Potential Market Shift

During the last seven years, we have continued to see a decline of net written premium as a percentage of GDP. As predicted in our January report, 2010 had the lowest ratio since the late 60s with less than 3 percent. With prior years showing a cyclical relationship dating back to 1973, it indicates the possibility of a market turn during the next few years. Our expectation is for an increase in this ratio to 2.94 percent for 2011.

Exhibit 9: Industry NWP as a Percent of U.S. GDP

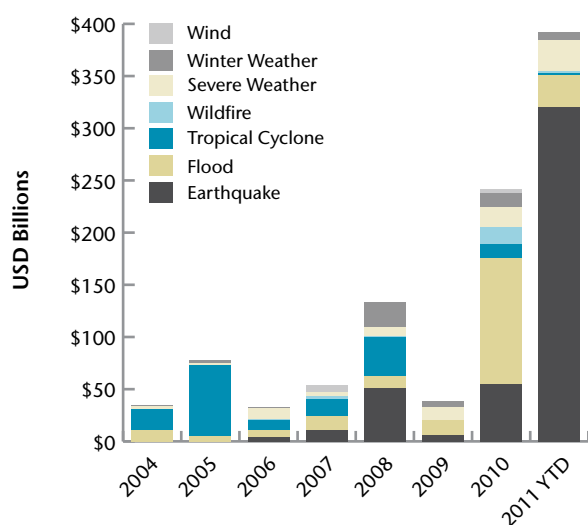


Source: U.S. Department of Commerce and SNL

Catastrophe Losses To Date are the Highest in Recent Years

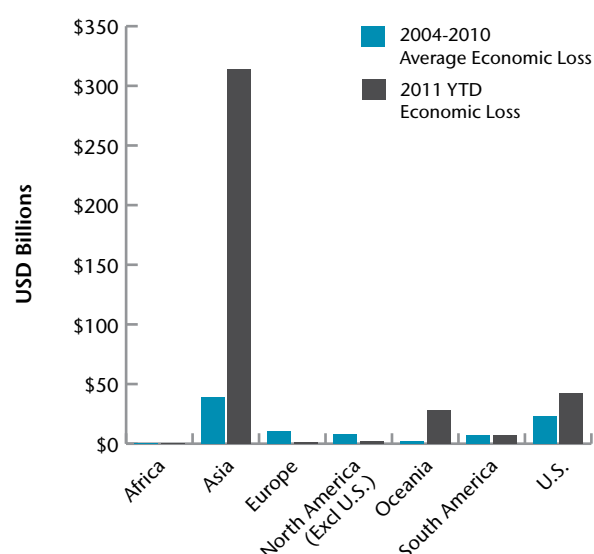
With significant earthquake losses reported in Japan and New Zealand as well as severe weather activity in the U.S., economic losses are approaching USD400 billion to date for 2011. This compares with an average annual economic loss of USD89 billion from 2004 to 2010.

Exhibit 10: Economic Losses by Year by Type



Source: Aon Benfield Analytics

Exhibit 11: 2011 Economic Losses versus Recent Years Average



Source: Aon Benfield Analytics

Earthquake losses in 2011 make up a significantly higher amount of losses on an economic basis compared to prior years where tropical cyclone activity previously contributed heavily to annual catastrophe loss activity. Even excluding earthquake events, year to date losses have surpassed the average of recent years (USD71.1 billion versus USD69.4 billion).

Exhibit 12 summarizes Impact Forecasting’s loss estimates on an economic and insured loss basis for the major earthquake events in the last 18 months.

Exhibit 12: Impact Forecasting Loss Estimates

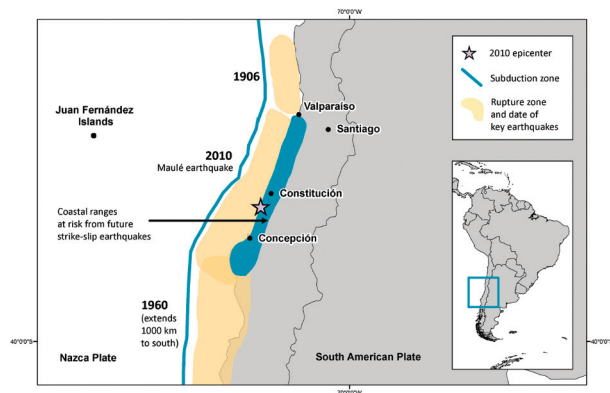
Event	Region	Date	Insured Loss (USD Millions)	Economic (USD Millions)
Darfield EQ	NZ	Sep 4, 2010	5,000-6,000	
Lyttleton EQ	NZ	Feb 22, 2011	10,000-11,000	24,800
Sumner EQ	NZ	Jun 13, 2011	>500	
Tohoku EQ	Japan	Mar 11, 2011	30,000-40,000* <i>*JER comprises 14,250</i>	300,000
Chile EQ	Chile	Feb 27, 2010	8,000-8,500	30,000

Source: Impact Forecasting

Chile Regulatory, Insurance and Reinsurance Systems Proved Responsive

On February 27, 2010 a magnitude-8.8 earthquake struck central Chile, causing approximately USD8.0 billion to USD8.5 billion in loss according to Impact Forecasting. The high magnitude of the Maulé earthquake makes it the eighth largest earthquake to occur since 1950.

Exhibit 13: Map of Maulé Earthquake Affected Area



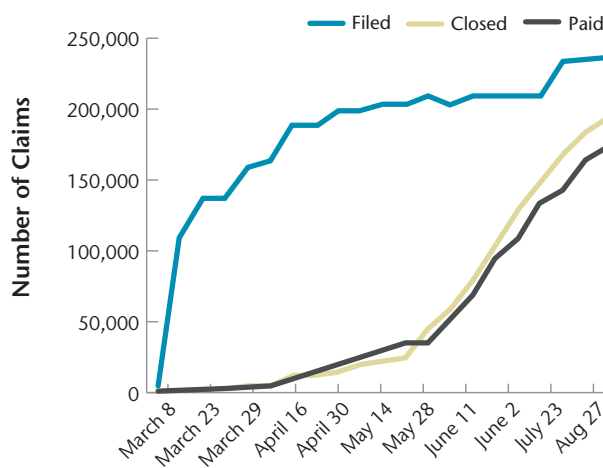
Source: Aon Benfield Analytics

Primary Insurance

In general, the cost of earthquake coverage for primary policyholders in Chile is driven by the terms, conditions and pricing of reinsurance. Unlike many other earthquake-exposed countries, insurance penetration for personal lines is fairly high, with about 35 percent of residential properties and 65 percent of industrial properties purchasing earthquake coverage. In addition, approximately 90 percent of mortgaged residential properties have earthquake insurance, with the bank holding the mortgage as the policy beneficiary. Claims filed by policyholders have been paid quickly. As of a year after the event, 95 percent of personal lines and 60 percent of commercial lines claims have been paid and closed partly due to the fact that the insurance regulator imposed a filing deadline of April 30, 2010 for residential claims.

One source of concern in the industry is the fact that insurance companies do not utilize standard policy wordings, causing some confusion amongst insureds. Despite the traditional deductible for earthquake policies at the event being 1 percent for personal lines and 2 percent for commercial and industrial policies, 33 percent of residential claims closed without payment as the loss fell within the deductible.

Exhibit 14: 2010 Claims Paying Pattern for Maulé Earthquake



Source: Aon Benfield Analytics

The heavy reliance on reinsurance created minimal impact on insurers' balance sheets with no company becoming insolvent after the event.

Reinsurance

Insurers’ balance sheets were not significantly affected by the cost of the direct claims but more by the cost of reinstatement premiums for catastrophe programs. Most companies now purchase reinstatement premium protections; a move that will most likely be formalized as a requirement by the insurance regulator in the near future.

Reinsurance retentions are generally set at a small percentage of capital as insurers are required to establish catastrophe reserves equal to 110 percent of the catastrophe program retention. Under local market practice, few companies expose more than 2 percent of their capital to a single risk and no more than 4 percent of capital to any single catastrophe event, not including the impact of the reinstatement premium.

Overall, reinsurers will pay 95 percent of the USD8.5 billion loss, an amount easily absorbed and paid by the market. Initially, excess of loss reinsurance programs that renewed after the event saw rate increases of 60 percent

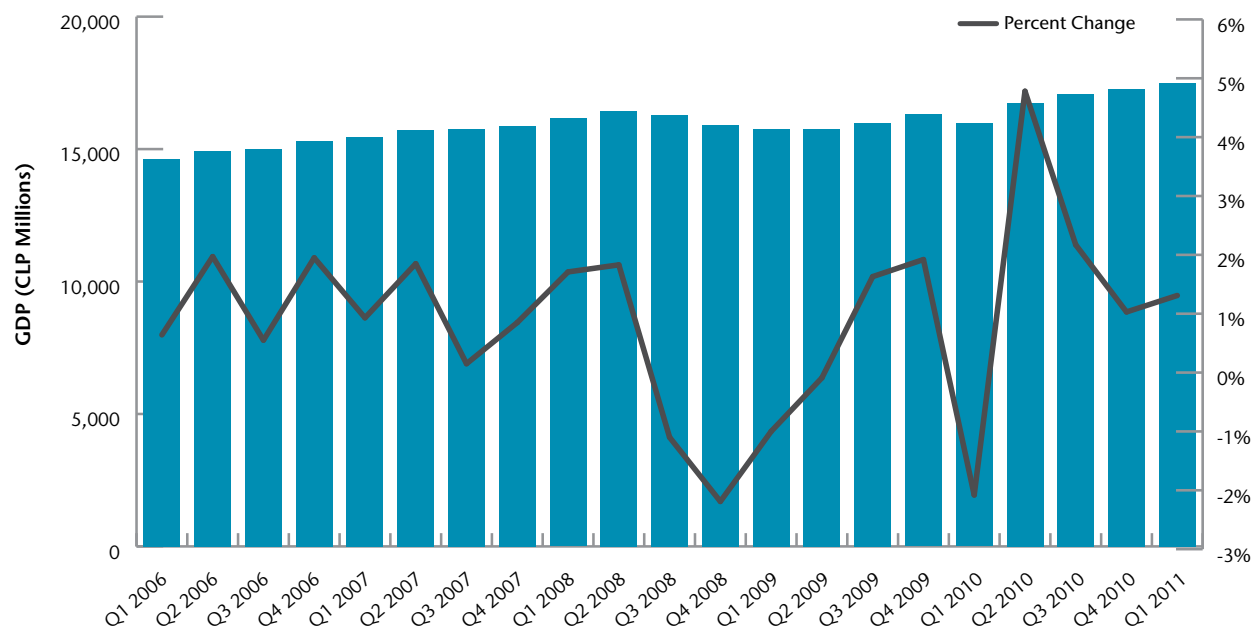
or more. The increases later stabilized at approximately 50 percent for programs renewing with more detailed loss estimations and appear to not affect the global market. The higher cost of earthquake reinsurance to the insurers was being passed on to policyholders raising premium by approximately 50 percent.

Reinsurance remains an integral component of Chile’s risk management program and contingency plan without which the burden of the cost of the event would have fallen on the state and taxpayers. The economic stability of Chile means that it would have most likely bared this cost better than other countries in the absence of reinsurance but because of it is able to enjoy continued growth.

Economy

While the event initially resulted in a reduction of GDP by 2 percent from fourth quarter 2009 to first quarter 2010, by second quarter 2010, adjusted GDP had rebounded to growth of almost 5 percent from first quarter 2010.

Exhibit 15: Chile Historical Adjusted GDP by Quarter



Source: Central Bank of Chile

Banks were protected against significant losses to their portfolio as a result of 90 percent of residential mortgages being insured, but have come under scrutiny after the event due to the high commissions they charge for insurance sold to their mortgaged properties. As a result, they have all voluntarily reduced the commission in anticipation of pending legislation that would require them to do so. The same pending legislation would also require banks to openly tender their mortgage portfolios and show customers that they have a choice regarding from whom they buy insurance. Consumers currently have the right to choose their insurance carrier, a fact that is not often highlighted by banks.

Government

The insurance regulator and the Chilean government are highly involved in the evolution of the insurance market. The strict regulatory insurance environment has forced companies to be fiscally conservative and therefore remain solvent after the event. A high ratio of insured loss versus economic loss further supports the argument that Chile's insurance market has been well regulated by the government.

Following the event, the insurance regulator, often in conjunction with the Chilean government, has chosen to review many of the systems used to support its methodology. This includes commissioning the development of a risk map for Chile, reviewing the minimum reinsurance purchase requirements, analyzing the data to determine the effectiveness of the current construction code and requiring insurance companies to establish a catastrophe reserve.

New Zealand Earthquakes Demonstrate the Value of Reinsurance

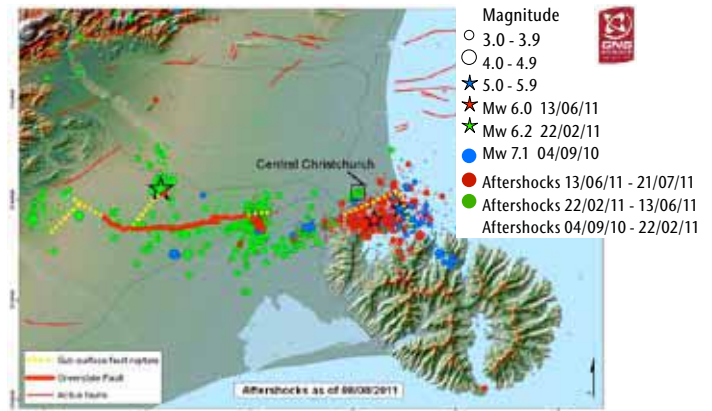
New Zealand, which sits between the Pacific and Indo-Australian tectonic plates, records on average more than 14,000 earthquakes a year, of which about 20 top a magnitude of 5.0. Surprisingly, little was known about the faults that caused the events during the last 12 months. Impact Forecasting estimated that more than NZD30 billion (USD24.8 billion) in economic damage was caused by the Darfield and Lyttelton earthquakes.

While the Darfield earthquake of September 4, 2010 was a higher magnitude at 7.1 than the Lyttelton event at 6.1, it caused less damage and no loss of life because the epicenter was outside the city center and it occurred early in the morning. In contrast, the Lyttelton earthquake that hit Christchurch at midday February 22, 2011 resulted in 190 deaths and more than 2,000 serious injuries.

The Darfield earthquake caused extensive damage to residential risks and widespread liquefaction and lateral spreading close to rivers. The Lyttelton event, occurring just 10 km SE of Christchurch, caused extensive, catastrophic building damage including the collapse of two commercial office buildings in addition to repeated and more extensive liquefaction and lateral spreading.

Exhibit 16 demonstrates the series of aftershocks with those in green depicting shocks following the Darfield event in September, but prior to Lyttelton event in February, those in red occurring after February, but prior to the Sumner event, and those in blue occurring after the Sumner event. The aftershock sequence and spatial localization indicate that the three events are expressions of activity on a larger fault system; the Lyttelton event is considered an aftershock of the Darfield event.

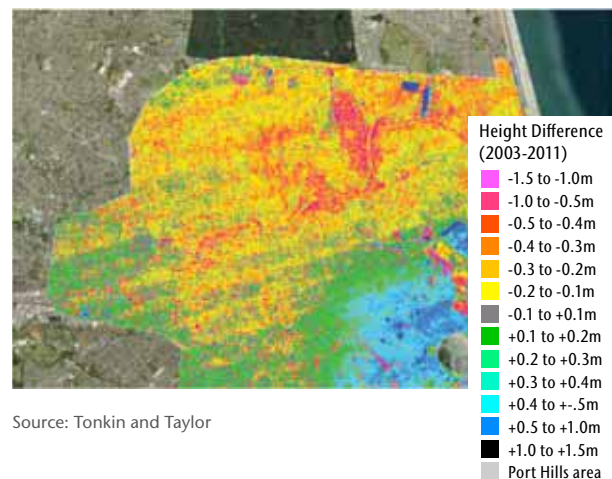
Exhibit 16: Darfield, Lyttelton and Sumner Earthquake Events



Source: GNS Science

Exhibit 17 is an aerial view of Christchurch showing ground surface elevation changes due to the Lyttelton earthquake. The image was produced using a remote sensing technology: LIDAR (Light Detection and Ranging), following the event and comparing with a base reference elevation survey from 2003. The large aerial extent of ground surface deformation is indicative of the large impact of the event on the city.

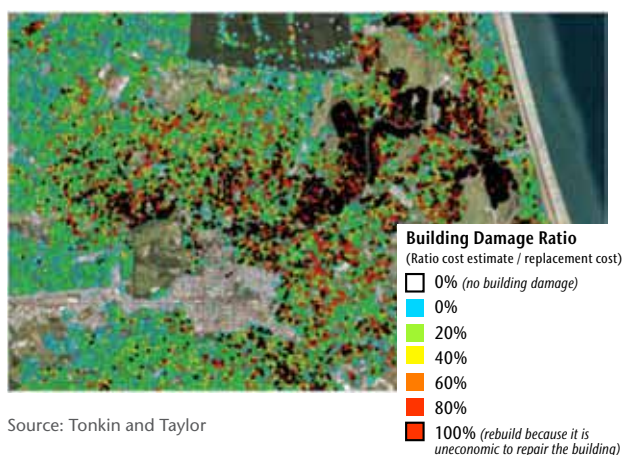
Exhibit 17: Change in Ground Surface Elevation from 2003 to March 2011



Source: Tonkin and Taylor

Residential building damage following the Lyttelton event was extensive: Exhibit 18 depicts the claims activity and percent of damage to buildings within the affected area of Christchurch. Commercial building damage from the Darfield event was mainly to older buildings often made from unreinforced masonry construction; the Lyttelton event saw a much greater spread of damage across the building stock in the central business district. Both events caused significant damage to infrastructure such as roads, pavements and water and sewage pipes.

Exhibit 18: Building Damage Following February 22, 2011 Event



Source: Tonkin and Taylor

Insurance and Reinsurance

The widespread damage from the events caused more than 350,000 claims to the New Zealand Earthquake Commission (EQC) alone, and while loss development for earthquake events can be significant, Impact Forecasting's current estimate for total insured loss is approximately NZD21 billion (USD17 billion). Of the total insured loss, reinsurance payments are expected to contribute more than 73 percent, or USD12 billion for both events.

While payments to date have been slow, this has largely been a function of the complications caused by the series of losses from continued aftershocks (the EQC references 11) and the need to develop alternative reconstruction plans as a result of the cumulative impact of the events.

Economic Impact and Government Involvement

Impact Forecasting estimates that the total economic impact for both the Darfield and Lyttelton events is approximately 12 percent of GDP for New Zealand, and of the total approximately 8 percent is attributable to the Lyttelton event in February. Although significant regional disruption occurred, there was limited impact to the national economy due to transfer of production to other city centers. Rebuilding is expected to add momentum to the economy with GDP growth forecasted at 2.4 percent and 4.5 percent for calendar years 2011 and 2012, respectively. Relatively low interest rates, a strong New Zealand dollar, good commodity prices and recent underinvestment are also stimulating investment in plant and machinery.

The New Zealand government has widely been seen as performing well as they have taken a high profile role and put in place the legislation and organization necessary to oversee the recovery and rebuild. In April 2011, the government established an agency called The Canterbury earthquake Recovery Authority (CERA) to lead and coordinate the recovery effort in Christchurch. The agency reports to the Minister for Canterbury Earthquake recovery, Gerry Brownlee, who is responsible for coordinating the planning, spending and actual rebuilding work. The New Zealand Prime Minister, John Key, has the highest ever approval rating as a result of the government's response following the earthquakes.

Japan Earthquake and Tsunami Market Impact Mitigated by Government Program



Japan and its surrounding regions have endured many destructive earthquakes throughout history. In fact, this area of the world is responsible for nearly 10 percent of the total annual occurrence of worldwide earthquakes. This year’s mega-earthquake and tsunami struck the northeastern coast of Japan on March 11, killing at least 15,689 people and injuring more than 5,700. As of late August 2011, 4,744 people officially remain listed as missing. The main magnitude-9.0 earthquake struck at 2:46 PM local time (5:46 UTC) with an epicenter 129 kilometers (80 miles) east of Sendai, Japan and 373 kilometers (231 miles) northeast of Tokyo at a depth of 32 kilometers (19.9 miles). Ground shaking from the temblor reportedly lasted for two full minutes. Following the main tremor, more than 1,235 aftershocks rattled the region with at least 70 shocks registering above magnitude-6.0. The earthquake was felt as far away as Beijing, China—some 2,500 kilometers (1,550 miles) from the epicenter.

Catastrophic damage was recorded across the northeastern coast of Japan, primarily due to the massive tsunami that washed ashore.

Official statistics indicate that more than 837,000 homes, businesses and other structures were either damaged or completely destroyed. Scientists noted that the tremor was so strong that it shifted the earth’s rotational axis by 10 centimeters (3.93 inches) and Japan’s main Honshu Island was also shifted 2.4 meters (7.87 feet) to the east. According to officials, this is the strongest earthquake ever recorded in Japan and tied for the fourth strongest global earthquake recorded since 1900. Japanese Prime Minister Naoto Kan described the aftermath of the earthquake as the “most difficult crisis for Japan” since the end of World War II.

Insurance and Reinsurance

The Japanese government currently estimates total economic losses from the Tohoku EQ in March of this year to range between JPY16 to 25 trillion (USD185 to 308 billion), or 3.4 to 5.6 percent of GDP. In July 2011, the government reported that JPY23 trillion (USD291 billion) would be spent on reconstruction costs for the affected regions. Impact Forecasting estimates that total insured losses for the event will be USD30 billion to USD40 billion. Of this, approximately USD14.3 billion has been paid by the JER and as of August 3, 2011, more than 96 percent of the 760,000 claims have been settled.

Exhibit 19: JER Claim Payment Historical

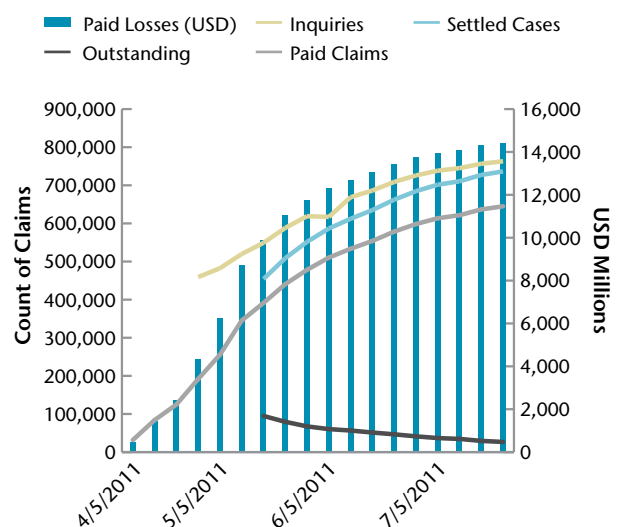
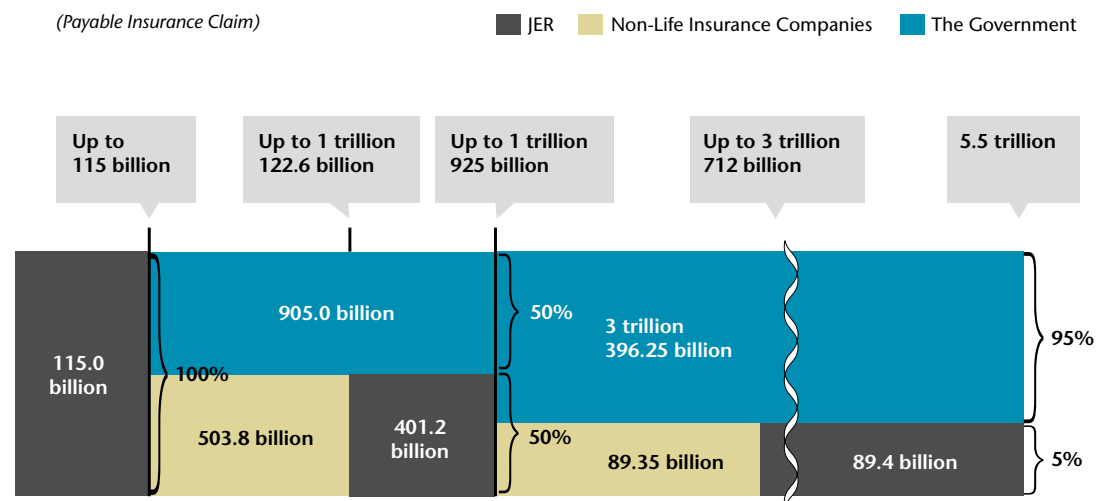


Exhibit 20: Reinsurance Scheme (JPY)



Source: JER, the Japanese Earthquake Reinsurance Pool

Global Reinsurance Market Impact

Despite the significant losses in Japan, the JER will likely pay for 40 to 50 percent of the losses for the earthquake. This, in addition to the coverage provided by the government will result in a lower percentage of loss paid by the reinsurance market than what would have typically been expected for a loss of this size. For example, it is estimated that reinsurers paid approximately 60 percent of the losses from Hurricanes Katrina, Rita and Wilma in 2005. Exhibit 20 reflects the coverage in existence at the time of the earthquake in Japan. Post-event, the retrocession back to the non-life companies was further reduced by the government by JPY500 billion for current and subsequent events.

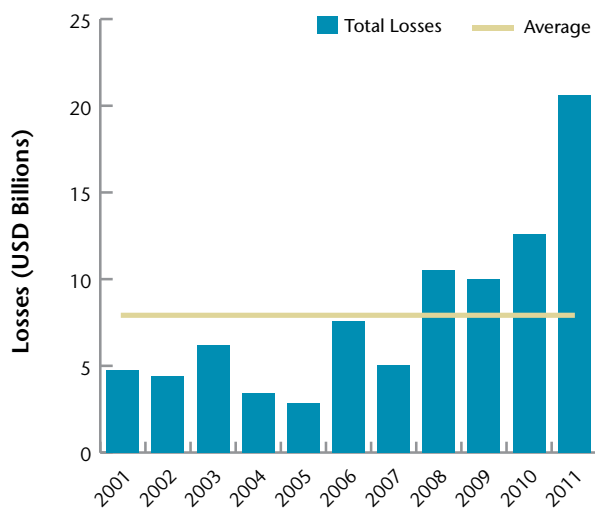
Economic and Governmental Impact

Earlier this summer, GDP change was revised to down 3.5 percent from down 3.7 percent reported earlier in 2011 while many still believe that expansion will occur at some point throughout the remainder of 2011. In addition to the typical infrastructure destruction that occurs following a major natural disaster, Japan also faces potential GDP issues should nuclear reactors that supply approximately 30 percent of Japan's energy not be returned to use. As much as 70 percent of the nuclear reactors in Japan have been offline since the earthquake and tsunami in March. Although the first plant went back online in mid-August, new stress test requirements implemented by the government in July 2011 make it difficult to determine when the remaining plants will return to use. Earlier this summer it was estimated that not returning the plants to use could result in an energy shortage by next summer and a potential hit to future GDP of 5.6 percent.

U.S. Q2 Severe Weather Increase Overshadowed by Major Events in Q1

Q2 2011 brought a significant increase in severe weather in the U.S. with major events occurring in Alabama, Missouri and Tennessee. Nationally, losses are more than four times the long-term mean for severe convective storms. Total insured loss activity to date for 2011 of USD20.6 billion is the highest severe weather activity in the last 10 years and more than double the average in the same period.

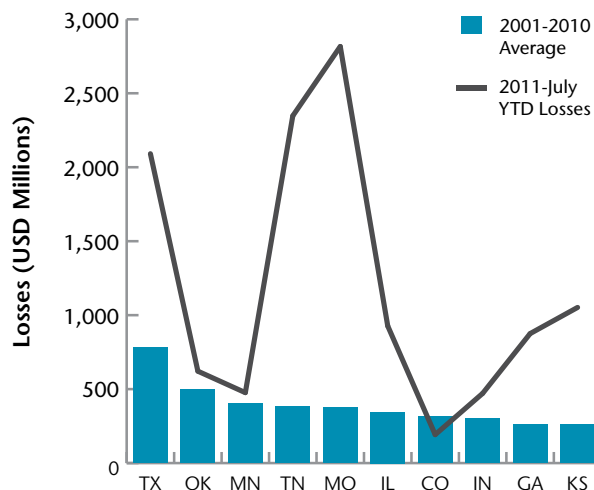
Exhibit 21: Losses by Year and Thunderstorm Activity



Source: PCS

On average, Texas has been the hardest hit state by severe storm losses from 2001 to 2010 and continues to be amongst the top states in 2011. Severe tornado outbreaks continued to affect the southeastern states with more than USD16 billion in loss in April and May alone.

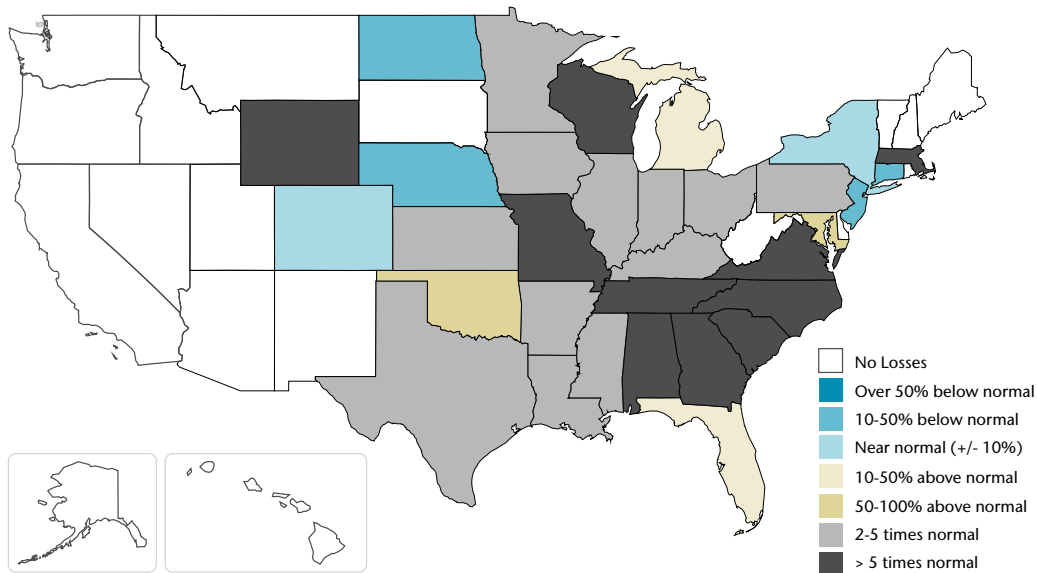
Exhibit 22: Top 10 States Annual Mean Loss Activity (2001–2010)



Source: PCS

Exhibit 23 shows that severe activity has been widespread, with nearly all states in the eastern half of the country experiencing losses greater than the long term average. Losses have been extreme in many states in the southeast with most states experiencing losses that are five times average historical results. By contrast, 2010 activity included a large event in Arizona which has yet to have a loss this year and Oklahoma which also had a large event still landed in the top ten states for 2011 with storm losses.

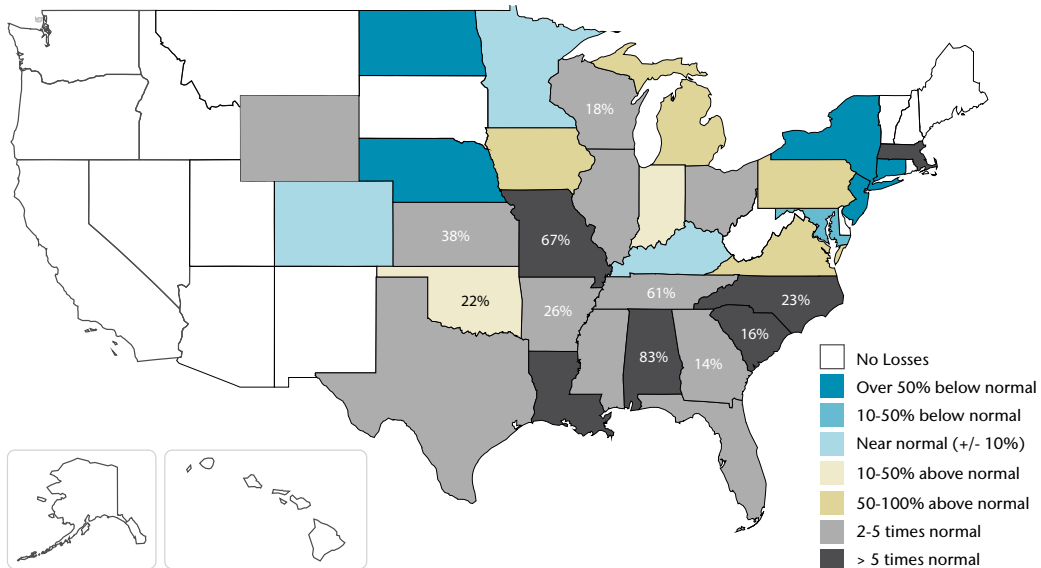
Exhibit 23: 2011 Activity Compared to Historical Trended Average Losses (2001-2010)



Source: PCS

Assuming similar premium to 2010, Exhibit 24 highlights Alabama, Missouri and Tennessee with more than a 50 percent loss ratio impact for 2011 from severe weather events alone compared to historical average annual loss ratio impacts of 2 percent, 4 percent and 14 percent respectively.

Exhibit 24: January through July 2011 Loss Ratio Impact versus Historical Trend-Adjusted Means



Source: PCS and SNL

Atlantic Hurricane Season Update

While Colorado State University (CSU) confirmed its earlier prediction with no change in August, both Tropical Storm Risk (TSR) and National Oceanic and Atmospheric Administration (NOAA) have increased their expectations of events for the season from earlier predictions in May/June and tightened the predictions among the three for major hurricanes. Both TSR and NOAA increased their expectations for tropical storms by two events, with TSR increasing its major hurricane expectation from 3.5 to 4.2 and NOAA revising its indication from 3-6 to 3-5. To date, 10 named storms have occurred in the season and only Hurricanes Irene and Katia have achieved hurricane status.

Exhibit 25: Atlantic Hurricane Season Forecast Summary

	Named Storms	Hurricanes	Major Hurricanes
TSR (August 2011)			
Average	10.5	6.2	2.7
2011	16.1	8.5	4.2
Difference	+5.6	+2.3	+1.5
CSU (August 2011)			
Average	9.6	5.9	2.3
2011	16	9	5
Difference	+6.4	+3.1	+2.7
NOAA (August 2011)			
Average	11	6	2
2011	14-19	7-10	3-5
Difference	+5.5	+2.5	+2.0

Source: TSR, CSU and NOAA websites.

Rating Agency View on Model Change

Prior to Q2 catastrophe losses, the primary challenge facing catastrophe exposed U.S. companies related to updates from a catastrophe model vendor, Risk Management Solutions (RMS), which released version 11.0 during Q1 (AIR released an update in Q4 2010, but the magnitude of the changes was more digestible, thus received less attention). While the pending model change had been known for months prior, the ultimate impact on individual portfolios was well outsized compared to initial industry guidance, which made it challenging for insurance companies to prepare for in advance.

Exhibit 26: Initial Industry RMS Model Change Guidance

Region	Aon Benfield's Interpretation of RMS Model Changes			Aon Benfield Model Change Study		
	AAL	100 Yr	250 Yr	AAL	100 Yr	250 Yr
Texas	95%	105%	98%	110%	105%	103%
Gulf	38%	46%	45%	88%	93%	96%
Florida	10%	8%	0%	32%	28%	15%
Southeast	25%	43%	50%	74%	85%	100%
Mid-Atlantic	107%	104%	97%	163%	153%	142%
Northeast	28%	25%	30%	46%	39%	41%
Large Commercial	N/A	N/A	N/A	82%	64%	56%

Source: RMS and Aon Benfield Analytics

For the most part, Aon Benfield has seen rating agencies provide companies time to analyze and understand the impact of catastrophe model changes. There have been some instances when rating agency analysts defaulted to using a blend of model results within the capital adequacy analysis. However, rating agencies are very interested in management's view of catastrophe exposure and plans to manage this exposure in light of recent model changes. As such, Aon Benfield has seen an increased desire from companies to evaluate catastrophe risk using a multiple model approach and not be reliant to the results of one particular vendor model. We have also seen this lead to an increased use of blending model results for capital management, pricing and reinsurance decisions. Companies (and the rating agencies) find a blended model approach as practical as it provides different perspectives on exposures and it leads to using the model output as a tool and not an exact point estimate. Further, using blended models is easy to understand, reduces the impact of model volatility on business decisions, and avoids potential issues regarding model shopping.

Other companies are taking this opportunity to take a deeper dive into their exposure and adopt a credibility approach which could entail a broader blending of

model results including near-term and long-term results. Through this process, companies have been evaluating the performance of the current versions of catastrophe models against historical losses to help assess the best model approach for their portfolio.

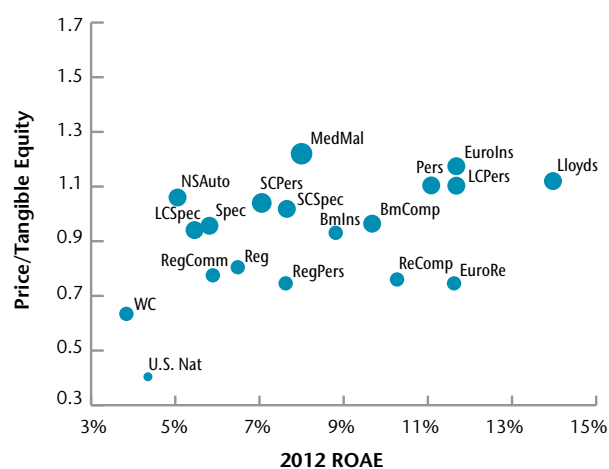
One area that has received particular scrutiny relates to RMS' increase in near-term frequency in version 11.0. The increase in near-term frequency contributed to 59 percent² of the overall model increase for the U.S. industry hurricane loss estimates. Most companies understand and agree with the merits of increases related to inland filling component of the model change, but have struggled with a hike in frequency give recent landfall activity. When near-term model results were introduced in 2006, they were on the heels of unprecedented U.S. landfalls in 2004 and 2005 and the industry (and rating agencies) generally accepted the concepts. However, the next five years (2006–2010) which was the intended to be the perspective for the near-term models did not result in a heightened frequency of hurricane landfalls. Therefore, the further increase in the near-term frequency component is under significant scrutiny, especially in regions like the northeast.

² UBS Investment Research July 19, 2011 and RMS

M&A Activity Update

Valuations of more than half of the publicly traded P&C insurance and reinsurance companies around the globe are below book value and most have been so for several years. These persistently low and sub book valuations have had a profound impact on M&A trends, insurance company capital management and the manner in which new capital enters and exits the industry.

Exhibit 27: 2012 ROAE versus Price/Tangible Equity



Note: Size of bubble equals market cap

Source: SNL

Below is a summary of how valuations remaining persistently below book value are impacting the insurance industry:

1. Increased pressure on management teams and boards to sell—When valuations tumbled during the financial crisis of 2008, many boards and management teams were hopeful of a quick recovery. Now that three years have passed with valuations averaging below book for most companies, owners and managers are adjusting their expectations and are increasingly willing to sell at or near book value. Recent deals announced and completed at or around book include the sale of Brit, NY Magic, Mercer, First Mercury and Transatlantic. Also, CNA bought the publicly traded piece of CNA Surety and Fairfax bought the publicly traded piece of Odyssey Re that it did not

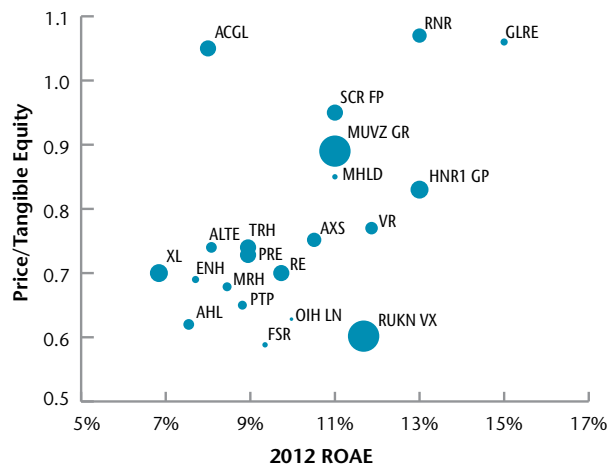
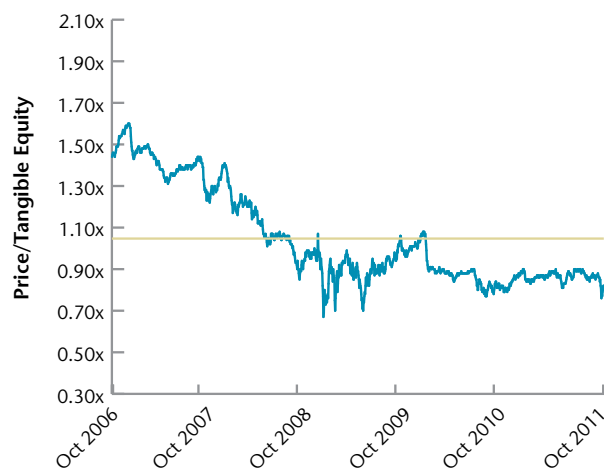
already own at close to book value. It is important to note that even though these transactions were completed at around book value, they generated significant sale premiums, from 25 percent to 50 percent, for the selling investors.

- An IPO is not a viable exit for private equity investors**—Larger private companies formed in the past several years by groups of private equity investors cannot look to an IPO for an exit. Instead, any near term exit or partial exit will come in the form of special dividends, a sale or a merger.
- Post event capital will not enter the industry through traditional, credit-rated carriers**—After start-up costs and the equity compensation awarded to management teams, private equity capital typically enters the insurance market at 1.10 to 1.20x book value. Since this is above today’s average public market valuation levels, investors can no longer depend on multiple expansions to generate returns and instead need to rely only on returns on equity. Start-ups, however, can not leverage their balance sheets in the same way mature companies can because the rating agencies apply tougher capital requirements to new companies.
- After the next meaningful market hardening event capital will overwhelmingly enter the market through sidecars and collateralized reinsurance funds**—Investments in sidecars are self-liquidating and investments in funds go in and come out at book value. There is comparatively little exit risk in these forms of investments and no book value multiple valuation risk.
- Run-off is increasingly a viable exit for investors**—Investors can typically realize valuations of around 90 percent of book value by “running off” insurance or reinsurance companies that write shorter tail business. Historically, companies were only put in to run-off when they lost their credit rating or were otherwise impaired. Increasingly owners are looking to run-off under-valued companies to realize investment gains from current valuation levels.

- 6. **Share buy backs will accelerate**—After a pause following the recent series of catastrophe events in Japan and New Zealand, share buy backs are again accelerating. Through the first six months of 2011, more than 1 percent of capital has been purchased in addition to a reduction in capital from dividends of 2.8 percent. For companies trading below book with excess capital, buying back shares and generating immediate, risk free gains is usually more compelling than considering an acquisition or deploying capital to support organic growth.
- 7. **Companies that were committed historically to organic growth strategies are increasingly considering acquisitions**—Buying mature premium at or below book value is usually more attractive than organically expanding in to new territories and lines of business in a soft market where establishing a beach head is usually accomplished with aggressive pricing.

- 8. **The emergence of hostile takeovers in the reinsurance market**—Low valuation levels have opened the door to hostile takeovers. Buyers will not purchase companies at over book value where there is implicit franchise value if, by doing so, they anger the senior management team that created the franchise value in the first place. When a company can be purchased below book, however, disenfranchising senior management is much less of a concern.

Exhibit 28: Reinsurance Price / Tangible Equity



Note: Size of bubble equals market cap

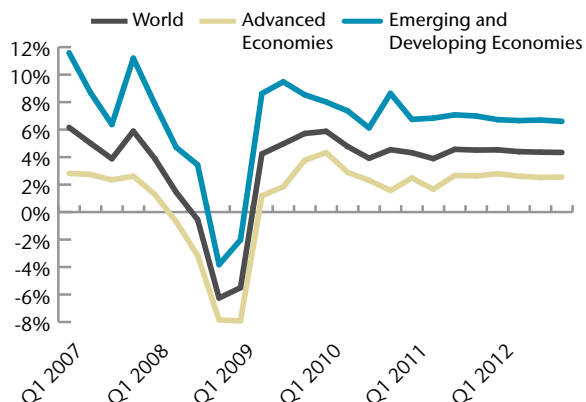
Source: SNL

Financial Markets Update

The relative confidence in the global economy during the first half of 2011 ended abruptly in the last days of July, prompted by an eruption of concerns about sustainability of the sovereign debt of the so-called peripheral European governments and the prolonged controversy over raising the statutory debt ceiling in the U.S., culminating in Standard & Poor's downgrade of the U.S.'s long-term credit rating to AA+.

In its most recent update dated June 17, 2011, the International Monetary Fund (IMF) noted a mild slowdown of global expansion and increased risks. Growth in many advanced economies remains weak, notably in the U.S., which was sparked by factors such as commodity prices, bad weather and supply chain disruption caused by the Japanese earthquake. Growth in the first quarter exceeded expectations in Germany and France and continued strong in most emerging and developing economies. Growth projections remained fairly positive, although the IMF pointed to heightened risks on the downside, with concerns—which in the event appear to have been well founded—about the depth of fiscal challenges in the euro area periphery a major factor. Growth was projected to slow in the second half of the year as confidence weakens, with reduced household and business confidence and other influences such as the disruption following the Japanese earthquake all serving to depress. The developments of recent weeks have only reinforced these factors.

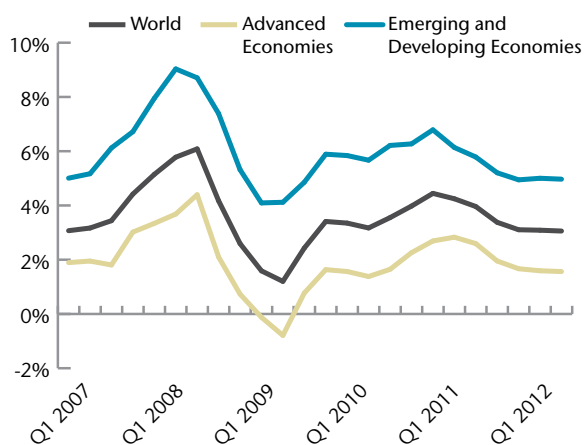
Exhibit 29: GDP Growth and Forecasts
(Quarter over Quarter, Annualized)



Source: IMF World Economic Outlook Update, June 17, 2011

There was also acceleration in the global inflation rate, which rose to 4 percent in the first quarter of 2011, mainly caused by larger-than-expected increases in food and commodity prices.

Exhibit 30: Inflation
(Year over Year, Period Average Consumer Price Index)



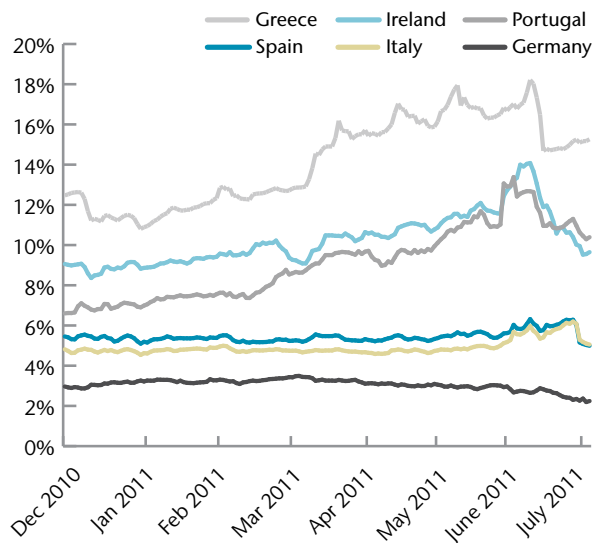
Source: IMF World Economic Outlook Update, June 17, 2011

Increased volatility has been a feature of the financial markets since the middle of the year, evidenced by rising sovereign credit default swap spreads in certain euro area economies, retreating global stock prices, and falling long-term bond yields in the major advanced economies, trends which have been accentuated in recent weeks. Underlying negative sentiment have been concerns at the insufficient pace of progress in repair to the banking system, as well as the risks of leveraging in various market segments.

The European sovereign debt crisis continues to evolve. Action taken by EU leaders in late July to improve the Greek government's debt sustainability and refinancing profile provided financial markets with temporary relief, but fears soon emerged that debt relief may prove insufficient and that contagion risk remains.

The borrowing costs of Portugal and Ireland remain at levels suggesting markets think they too are likely to default within the next five years. More importantly, the yield on 10-year Italian government debt has fallen from a high of 6.3 percent but remains over 5 percent.

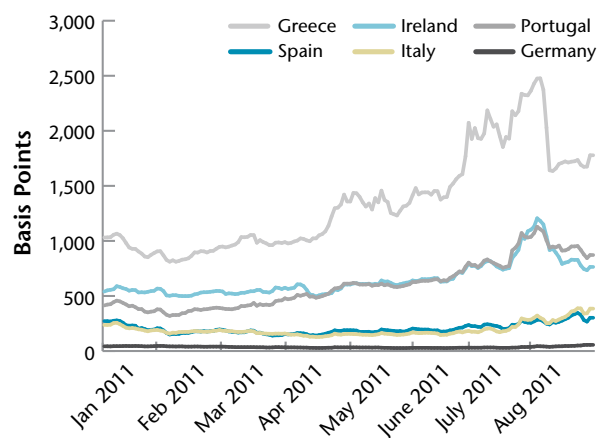
Exhibit 31: Ten-Year Government Debt Yields



Source: Aon Benfield Analytics, Bloomberg

The sharp rise in credit default swap spreads reflects the concern of investors that further action is needed to address fiscal deficits and bring borrowing under control.

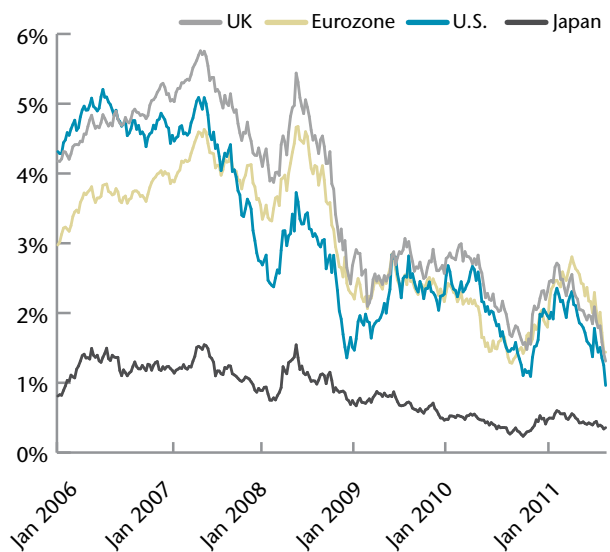
Exhibit 32: Sovereign CDS Spreads



Source: Aon Benfield Analytics, Bloomberg

Governments around the world have continued to target low interest rates as a key policy measure to promote economic recovery. The key U.S. Federal Funds Rate has been kept at a record low of 0.25 percent since December 2008 and the U.K. Bank Rate has been at 0.50 percent since March 2009, although the European Central Bank raised its Marginal Lending Facility to 2.00 percent from 1.75 percent at the end of April 2011.

Exhibit 33: Five-Year Government Bond Yields

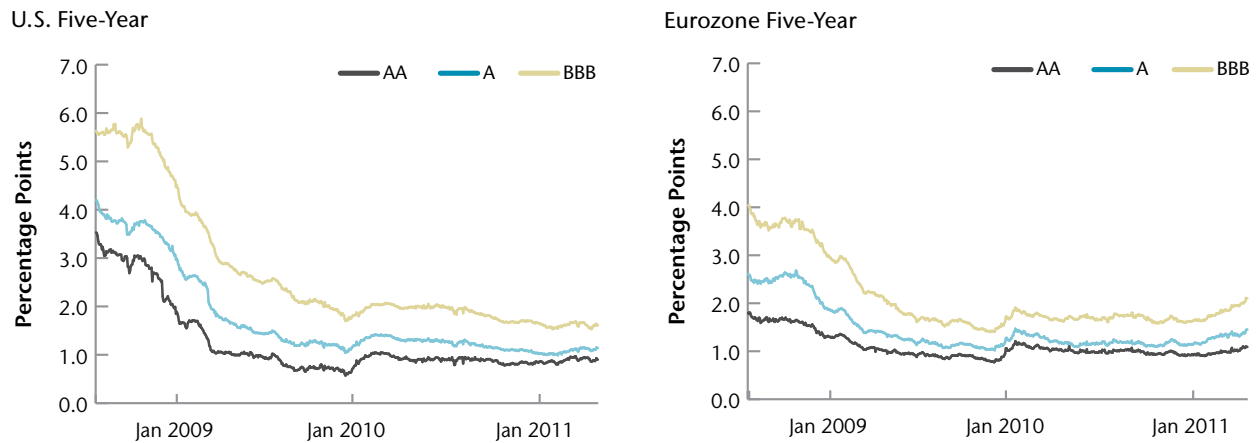


Source: Aon Benfield Analytics, Bloomberg

With growing economic confidence in the early months of 2011, bond yields continued on an upward trajectory, maintaining a trend started in the fourth quarter of 2010, with yields on U.S. bonds peaking at 2.3 percent in mid-April. At the same time, yields on U.K. and Eurozone debt reached highs of 2.6 percent and 2.8 percent, respectively. Yields in Japan topped out in February, to reach 0.6 percent. As worries resurfaced about the state of the global economy, yields fell again, and dropped sharply from late July.

Despite the turbulence in other sectors of the financial market, the U.S. corporate bond market has stabilized, with the spread over government of AA rated issues remaining relatively flat, while that on BBB rated issues continues to narrow. It was a different matter in Europe as credit concerns resurfaced, and spreads on A and BBB rated issues started to widen again.

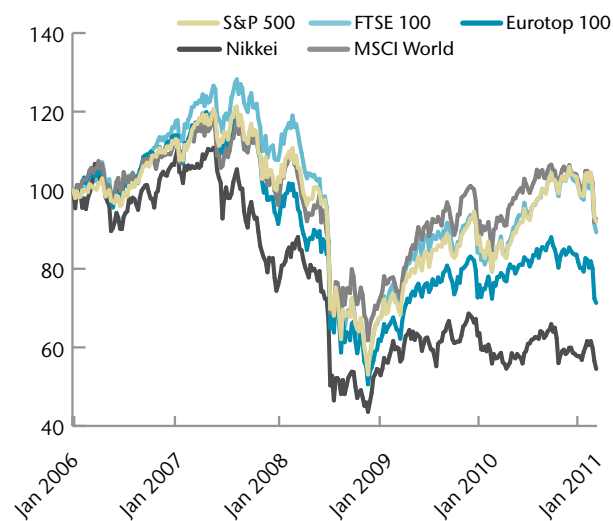
Exhibit 34: Five-Year Corporate Bond Spreads over Government Debt



Source: Aon Benfield Analytics, Bloomberg

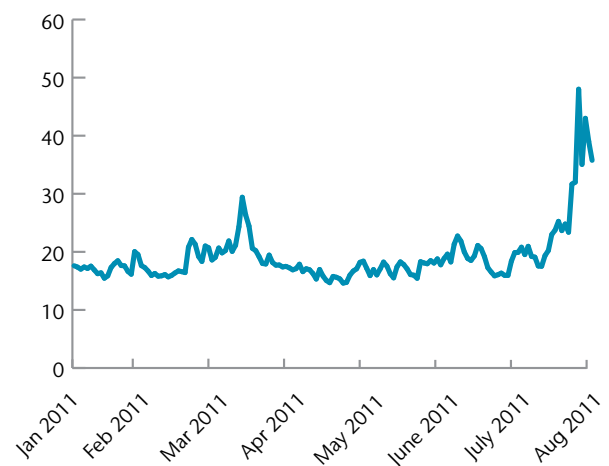
Equity markets made a positive start to 2011 and stabilized in the second quarter, before taking a nosedive from late August with the onset of worries associated with the U.S. federal debt ceiling and the stresses in the Eurozone and the weak outlook for economic growth. The S&P 500 index rose 6 percent during the first quarter to 1330, but at mid-August the index was down 6 percent since the start of the year. Stock markets in Europe (Eurotop 100) and the U.K. (FTSE 100) both rose 2 percent in the first quarter but were down 14 percent and 10 percent respectively at mid-August. Markets remain weak and volatile as evidenced by the sharp rise in the CBOE S&P 500 volatility index during August.

Exhibit 35: Equity Markets Index (January 2006 = 100)



Source: Aon Benfield Analytics, Bloomberg

Exhibit 36: CBOE S&P 500 Volatility Index



Source: Aon Benfield Analytics, Bloomberg

Banks Asset Leverage on Steady Decline

Our analysis of the 20 largest banks globally reveals that total asset leverage, as measured by total assets to shareholders' equity, has been steadily declining since the financial crisis high of over 36x in the third quarter of 2008. At the end of the second quarter of 2011, it stood at less than two-thirds of this amount, at just under 23x. As a further measure of progress, this is also below the pre-crisis level of 29x.

Excessively leveraged bank balance sheets heightened the risk of bank insolvencies and the natural response of regulators is to increase the required capital. The Basel Committee formulates broad supervisory standards and recommends statements of best practice in banking supervision in the expectation that domestic regulators will implement them. Based upon the Basel II accords, the FDIC currently requires a maximum asset leverage ratio of 25x for a bank to be "adequately capitalized".

For a bank to be "well capitalized" the maximum asset leverage ratio is 20x. From January 1, 2013 the more onerous Basel III will become effective and the required asset leverage ratio is expected to become stricter and change to 16.7x.

Although progress has been made in the reduction of asset leverage, for the portfolio of banks in our analysis only 50 percent of these meet the current criteria for being "well capitalized" at the end of Q2 2011. Further, the introduction of Basel III will require additional capitalization to meet the new criteria as only 6 of the banks in the portfolio met this updated criteria at the end of Q2 2011. However, provided the current trend of declining asset leverage continues, then banks appear to be on pace to reduce leverage to levels required under Dodd Frank and Basel III of 14 to 15 times within 8 to 12 quarters.

Exhibit 37: Top 20 Largest Banks Total Leverage

	6/30/07	9/30/07	12/31/07	3/31/08	6/30/08	9/30/08	12/31/08	3/31/09	6/30/09	9/30/09	12/31/09	3/31/10	6/30/10	9/30/10	12/31/10	3/31/11	6/30/11
BNP Paribas SA	36.4	36.2	36.0	39.1	42.1	45.2	48.6	47.6	46.8	39.3	33.5	34.0	34.6	32.2	30.0	29.1	28.3
HSBC Holdings PLC	18.0	18.4	18.7	19.4	20.1	23.0	27.0	23.4	20.5	19.6	18.8	18.3	17.8	17.3	16.9	17.0	16.8
Deutsche Bank AG	53.4	51.1	54.5	67.4	62.4	59.2	71.7	62.5	50.5	48.0	40.9	42.7	46.4	50.8	39.0	36.9	37.0
Mitsubishi UFJ Financial Group Inc	25.1	24.9	22.9	23.3	22.3	24.4	25.6	26.2	27.5	29.2	32.2	28.7	28.0	24.3	23.5	24.1	23.6
Barclays PLC	55.2	53.9	52.7	56.9	61.3	58.4	56.1	48.0	41.0	34.5	29.2	30.6	32.0	30.6	29.3	29.1	28.9
Royal Bank of Scotland Group PLC	24.3	30.1	34.7	32.5	30.5	34.7	40.8	40.0	32.7	32.8	21.8	22.4	20.6	21.6	19.3	19.1	19.3
Bank of America Corp	11.5	11.7	12.0	12.5	12.4	13.4	13.0	14.0	11.5	11.3	11.5	11.0	11.0	11.0	10.7	10.6	11.0
JPMorgan Chase & Co	12.2	12.3	12.7	13.1	14.0	16.4	16.1	15.0	13.8	13.2	12.9	13.6	12.4	12.9	12.6	12.7	12.8
Credit Agricole SA	33.2	33.8	37.2	37.6	40.5	35.7	42.4	40.4	36.7	39.6	36.4	35.9	38.4	36.5	37.2	33.9	33.9
Industrial & Commercial Bank of China	16.7	16.4	16.1	16.6	17.1	16.6	16.2	17.3	18.6	18.1	17.5	17.5	18.4	17.8	16.4	16.5	16.5
Citigroup Inc	17.5	18.6	19.3	20.2	19.3	20.8	27.3	26.2	23.7	13.4	12.2	13.3	12.5	12.2	11.7	11.4	11.1
Mizuho Financial Group Inc	44.4	33.2	38.1	41.1	41.4	43.7	52.9	52.5	64.9	80.1	128.7	95.3	58.6	57.4	52.4	52.5	40.8
Banco Santander SA	19.8	19.8	17.7	17.8	18.5	19.0	18.3	18.9	18.1	16.4	16.3	16.4	16.9	17.8	16.2	16.8	16.8
China Construction Bank Corp	18.8	17.0	15.7	15.4	15.5	15.3	16.2	17.6	18.0	17.5	17.3	17.1	17.8	17.0	15.5	15.2	15.2
Bank of China Ltd	14.8	14.5	14.3	14.4	15.0	14.7	15.0	16.5	17.4	17.0	17.0	18.1	18.1	17.8	16.2	16.6	16.6
Societe Generale SA	39.1	39.2	39.3	36.7	34.5	36.0	37.7	35.7	33.7	31.0	28.7	29.5	29.6	30.1	28.4	28.6	28.0
Agricultural Bank of China Ltd			-7.3	-12.5	-30.7	136.3	24.2	24.6	25.1	25.5	25.9	25.7	27.4	19.2	19.1	19.0	19.0
Sumitomo Mitsui Financial Group Inc	34.1	32.9	28.3	25.9	30.4	31.7	31.3	35.0	35.4	38.0	55.4	33.4	32.2	34.1	26.0	26.7	26.5
Lloyds Banking Group PLC	31.0	30.0	29.1	31.4	34.1	38.9	46.4	34.7	31.8	27.3	23.7	22.9	22.0	21.8	21.5	22.2	21.8
UBS AG	49.5	51.5	61.7	136.2	46.9	43.0	61.9	59.5	47.7	37.3	32.7	31.7	31.7	30.6	28.1	27.7	26.2
Average	29.2	28.7	27.7	32.2	27.4	36.3	34.4	32.8	30.8	29.5	30.6	27.9	26.3	25.7	23.5	23.3	22.5

Source: Aon Benfield Analytics

Sector Analysis by Geography

The following sections provide an update on significant reinsurance market segments, by region.

Asia Pacific

Australia

Following significant catastrophe loss activity over the past 12 to 18 months, resulting in approximately AUD25 billion (USD26 billion) in losses, Australian property reinsurance is in a hardening phase. Pricing impacts at last renewal varied by cedent, however risk adjusted increases were generally in the range 15 percent to 70 percent. Significant pressure is being applied to retention levels, pricing on loss-affected layers and minimum rates on line charged on upper layers. Notwithstanding the above pressures, ample reinsurance capacity remains available for Australian programs.

Casualty risk adjusted rates are largely flat and the class continues to benefit from an increased supply of reinsurance capacity as reinsurers attempt to diversify away from loss-affected property classes.

China

Although the world economy is hampered by debt crises from many developed countries, China's GDP grew by 9.3 percent for the first half of 2011. Chinese non-life insurance maintains strong growth with total gross written premium of RMB244 billion (USD38 billion) in the first half year of 2011, up 16 percent compared with the same period in 2010 according to the Chinese Insurance Regulatory Commission (CIRC).

Peoples Insurance Company of China, Ping An and China Pacific remain the top three non-life insurers holding 67.2 percent premium market share at the end of June. The three insurers achieved premium growth of 12, 35 and 19 percent respectively.

Despite several major catastrophe losses in international market in the first half of 2011, impact to the catastrophe excess of loss treaty pricing has not been significant and overall spend increases appear mainly due to continuous increase in exposures and fast growing retained premium income.

Reinsurers continue to show interest in China with ample capacity available in both the non-proportional and proportional segments.

Due to the positive performance of non-marine proportional treaty business in 2009 and 2010, the renewal terms and conditions are basically maintained or slightly improved for insurers compared to expiring, especially in financial terms (commissions) to reflect the encouraging development of the treaty performance.

Coverage requested by insurers is largely unchanged and only few marine related clauses such as Sanction Clause have been introduced by reinsurers.

Since 2009, the China Insurance Regulatory Commission has continuously asked for the improvement in solvency situation of insurers, as the market is growing so rapidly as to be potentially unsustainable by insurance companies.

Hong Kong

Reinsurance pricing is largely stable with programs renewing in 2011 excess of loss treaties renewing within +/- 5 percent on a risk adjusted basis depending on program result. Most lines of business (except liability due to the long tail nature of the coverage) remain highly dependent on proportional programs to increase their underwriting capacity. Natural catastrophe perils are covered under proportional treaties but with event limits on property & engineering classes. Natural catastrophe exposure is not a major concern of insurers and not many insurers purchase catastrophe cover. The Insurance Regulator is expected to be independent by 2013 and will enforce stronger rules including risk based capital analyses to control the solvency of insurers.

With abundant treaty capacity, reinsurers continue to compete for an increased share of the market, particularly in Hong Kong and Singapore, resulting in potential reinsurers, including Lloyd's of London, finding it difficult to participate. The Sanction Limitation and Exclusion Clause, which removes reinsurer liability in the event that providing the coverage or paying the claim would expose the reinsurer to sanctions, prohibitions, or restrictions, was added to all marine treaties in 2011.

India

Primary rates have shown signs of levelling off and insurance market efforts to increase minimum deductible levels have been successful.

In general, April 1 renewals for 2011 were challenging due to recent loss activity within the Asia Pacific region and loss making proportional treaties, which have continued to have difficult placements resulting in a number of companies choosing to supplement capacity through increasing retentions and buying additional limit for their excess of loss purchases.

Quotes and placements of excess of loss programs were delayed due to the Japanese earthquake with some placements struggling to complete ahead of inception. Catastrophe pricing on a risk adjusted basis was flat to up 5 percent. With increases in spend a number of companies choose to increase attachment points.

Indonesia

The Indonesian market remains very competitive with approximately 90 insurance companies and over 100 registered brokers. Despite some growth in the market due to the aggressive economic growth, insurance premium growth continues to lag economic growth and rates continue to be driven down due to excessive capacity.

Minimum capital requirement of USD4 million will be increased to USD7 million in 2014 and is expected to reduce the number of companies and the hope is that rates will slowly begin to rise. While still very low compared to international companies, the increase in minimum capital requirements is expected to eventually lead to consolidation of the numerous companies in the market but not within the next two to three years.

Japan

Insurers continue to support their customers following the Tohoku loss in March. The well-known steep reduction from the large economic loss, to the (still substantial, but manageable) insurance loss, to the (still substantial but smaller) reinsurance loss, as well as the current financial conditions, are natural considerations as thinking now turns to the 2012 renewals.

Original earthquake claims for homeowners business have been settled very quickly with insureds by both the non-life sector and the mutual companies. Since householder losses from the non-life sector are covered by the government scheme, they do not fall to the reinsurance market. Losses from the mutual sector do affect the reinsurance market and the response of the reinsurance market in paying claims has been, almost without exception, outstanding. Reinsurance claim payments have progressed smoothly and at an impressive pace with many reinsurers having offered early payment or done their best to speed the process.

Korea

At the April 1 renewal, many insurers in Korea considered or increased their treaty limit in order to cede more risks to the treaty. This is mainly due to the Korean Financial Supervisory Service's (FSS) future guideline to change the insurer's ranking to be based on net premium rather than gross premium.

Due to the increase in treaty limit, demand for additional capacity increased for many insurers. However, due to the Japan earthquake and other catastrophe loss in Asia before April 1, property event excess of loss prices had gone up 5 to 30 percent, making it more expensive for insurers to purchase coverage to the limits needed to be compliant with the FSS. Property risk excess of loss prices were flat to down 15 percent as there were no significant risk losses in Korea.

Philippines

Following the Tohoku Earthquake, major reinsurers for the Philippines market elected to discontinue providing coverage on a pro-rata basis leading to property exposure coverage being covered on XOL basis. This resulted in more catastrophe limit purchases and risk-adjusted price increases from 30 to 50 percent.

Other than above, prices for companies who had previously purchased excess of loss continue to generally be flat on a risk adjusted basis.

Singapore

The Monetary Authority of Singapore (MAS) has implemented the Reinsurance Management Strategy (RMS), and insurance companies submitted their RMS for the first time by June 30, 2011. The market is gearing towards a more analytical way of managing their risks and reinsurance protection. This marks a change in Singapore as previously there was no standard method adopted by companies to manage risks. However, we do not expect a drastic change in buying.

Reinsurance pricing for property business remains stable despite the flood losses in June and July 2010, which were covered under fire policies. The fire incurred loss ratio for reinsurers in 2010 was 23.2 percent. No significant risk losses have occurred in 2011 and market perception of the country as a non-catastrophe exposed territory remains resulting in few treaties having event limits.

Original rates for motor insurance continued to increase gradually in 2010. Industry incurred loss ratio for motor has further decreased to 74.3 percent compared to 74.6 percent in 2009 for insurers and to 58.7 percent from 86.0 percent in 2009 for reinsurers.

Taiwan

There have been no major catastrophe losses in 2011 nor have there been any reported losses affecting risk excess of loss programs. The soft pricing trend on the primary side has bottomed out. Last year's attempts to introduce a tariff pricing for natural perils for larger property risks were successful, with a tariff implemented on July 1, 2011. The full impact of the tariff will have to be reviewed in 2012 as the majority of large property risks cancelled and renewed their insurance prior to July 1, 2011. So far, our clients are optimistic about the natural perils tariff for 2012.

The increased quoting of catastrophe aggregate covers is expected to continue into 2012. Due to the recent earthquakes in both Japan and New Zealand, Taiwanese companies are reevaluating their amount of coverage. Currently, most Taiwanese companies do not buy to the relative industry norm of a 250 year return period and we foresee that they will be seeking quotes

for coverage at least equal to the 1 in 250 year return period. That said, budgetary pressures may not enable companies to purchase more conservative coverage.

Reinsurance market pricing for companies with good loss history and increased exposures achieved a 5 to 10 percent risk adjusted rate decrease throughout 2011 and expectations for next year are that pricing will be firmer. Also, it will be based on any new catastrophe events that occur in the later part of 2011, which could cause further hardening of the market. Prior to these events, companies were already facing budgetary constraints that caused the purchase of insufficient catastrophe coverage. As the tariff will not have any impact on their income for the 2012 renewals, excess funds might not be available to purchase additional catastrophe coverage even though it seems to be the most prudent thing to do post the 2011 natural catastrophe events.

Thailand

Floods in Q4 2010 have had a major impact on the renewals for most companies in 2011, the majority of which renew at January 1. While insured losses are small from a global perspective (USD50 million), the local economic impact is far more severe. In addition, further flooding has occurred in Q1 2011.

Per risk reinsurers remain concerned with the aggregation of reinsured portfolio exposure from a single fire loss. This concern stems from the Sri Thai Superware fire loss last year.

A Risk Based Capital Framework rollout is currently in progress in Thailand. A test run is being done currently by the Office of Insurance Commissions, with the official implementation date set at September 30, 2011.

The Thailand government has announced the implementation of a crop insurance program for rice growers, commencing with the 2011 main season rice crop. This new program is referred to as the *Thailand Rice Disaster Relief Top-Up Scheme*. The scheme is fronted by eight domestic insurers, backed by a quota share reinsurance agreement. The contract commenced on July 1, 2011 and terminates on June 30, 2012 ensuring coverage through the latest harvest period.

Europe, Middle East and Africa

Austria

In contrast to 2010, when some of the group catastrophe programs were affected by CEE flooding events, programs remain free of losses for 2011.

In light of the partly significant restructuring of retentions for insurers over the past two renewals, minimal additional structural changes are expected for 2012. Due to the loss-free status of all programs, it is expected that pricing on a risk-adjusted basis will remain flat despite global catastrophe loss activity. Upward changes in some commercial catastrophe models are expected to have little influence on the overall renewal.

Discussions continue with regulators regarding the parameters of the Solvency II formula. As a result of discussions with Aon Benfield, there is increased awareness of the FMA (Finanzmarktaufsicht – Austrian supervisory authority) regarding the relevance of catastrophe models for the Austrian market. They also see the critical aspects in particular in respect of the correlation matrix as suggested in the original formula. Even prior to the changes made to the Solvency II formula, Austrian insurance companies complied with the requirement for coverage to the 1 in 200 year PML.

Pressure on excess of loss rates in motor third-party liability is expected to decrease compared to the prior year due to slight improvement in rates (1 to 2 percent) by many companies on primary insurance. For property, all proportional instruments will continue to be under due diligence by some of the leading reinsurers, which will further support the trend to seek additional non-proportional capacity.

Belgium

Tariff increases have been applied to retail business (essentially motor) during the last 3 years. This is not yet the case for industrial business where capacity is plentiful.

Property cat activity has been benign up to now and we do not expect negative impacts on rates other than the possible global effect of recent property cat claims outside Europe. Currently we are in the process of evaluating the possible impact of RMS version 11.0 on our client's portfolio data of last year. We expect the recent interest in multicat aggregate protections to be confirmed.

Property per risk, workers' compensation, motor third party liability and general third party liability treaties are mainly priced according to the cedent's statistics and we do not expect major changes for the coming renewal. Our market analysis of large losses shows that top layers should not be negatively affected in the near future.

Central and Eastern Europe

Following exceptionally poor results in 2010 with high frequency of catastrophe losses across the CEE Region mostly affecting the Czech Republic and Poland, this year is so far free of significant losses.

Industrial property shows continued pressure on rates, as the segment is still profitable. Severe competition in Motor Third Party Liability business has reduced rates to a low level of profitability and there are signs of increases in rates in some countries.

The increased importance of the CEE region attracted vendor modeling agencies such as AIR and RMS who have expanded their wind and earthquake models to include the CEE region for the first time where previously clients relied more heavily on Aon Benfield's Impact Forecasting model. That said the market acceptance of the two new models is difficult to predict at the moment.

The standard formulas for Solvency II published by EIOPA have caused some debates and the results of QIS 5 exercise have resulted in 5 CEE countries in the bottom 50 percent of the overall EU results (Poland, Latvia, Slovenia, Bulgaria and Hungary).

Increased net retentions have occurred only when forced by prohibitive pricing on bottom layers following property catastrophe loss experience. Reinsurance capacity is plentiful and there are no changes in reinsurance market participating in the region.

Rates during the first half of 2011 on some Russian, Romanian and Bulgarian Property and Motor renewals were flat or showed very slight rate reductions based on an exposure adjusted basis for contracts with expected claims development.

France

Results in France for 2011 differ between life and non-life business. The saving segment of life business has had a negative trend for the first half of the year, which is expected to continue throughout the end of the year due to the current state of the financial markets. In contrast, accident and health is still a growing sector, particularly for individual contracts with good technical margins.

Results for non-life personal insurance improved year over year. Rate increases have been implemented by nearly all companies in 2011, both on motor and fire policies, and rates are expected to increase again next year. In addition, following two years of extensive claim activity for natural events, 2011 has been claim free.

While primary results are positive for 2011, recent frequency of natural events has forced clients to evaluate the effectiveness of their catastrophe reinsurance structures.

Despite international losses, we expect flat risk adjusted pricing to continue in France assuming no additional major events due to the continued competition by reinsurers for business that is uncorrelated with peak zone exposures. Nevertheless there is uncertainty in respect to reinsurance market pricing attitude on the top end of catastrophe programs as minimum ROLs are currently very low and it is expected that reinsurers will require an increase in these minimums.

Rates for motor liability reinsurance are also expected to remain stable. Structures have remained stable for the last two years resulting in positive results for reinsurers and some insurers are evaluating increasing retentions in order to minimize ceded margin. Should this occur, we expect that it could have a positive impact on price for insurers.

In the coming year, Solvency II's revised catastrophe model should not generate a significant increase of required catastrophe capacity for most of the ceding companies (with the exception of some Bank-Insurers which are expecting significant growth of their exposures as a direct consequence of the evolution of their market share). As has been the case in recent years, adjustments to catastrophe capacity will ultimately depend on the rules for capital requirements. The recent changes in appreciation of exposures due to a new catastrophe model version could influence the level of required capacity. This has yet to be determined as many clients may decline to use the new model, as the high variation of results from one year to another could create major discrepancies for the company's internal Solvency II model.

It appears that Solvency II could create new demand for reinsurance in the coming months on the Life side particularly for "saving products". Companies could face a significant need for additional capital and reinsurance could be the most effective product, particularly in a period when the financial market is unstable.

Germany

The German insurance industry suffered large fire per risk losses in 2011 as well as regional heavy rain and hail events. Traditionally extended elemental perils are only covered to a smaller extent in Germany which in the end reduces the impact of the heavy rain events on the insurance sector and instead passes the burden of the remainder of the loss onto homeowners.

Discussions continue regarding the release of the new RMS model for Germany which shows some significant changes in results for insurers' portfolios, especially regarding the loss frequency. Whether this will have a major impact on the reinsurance rates remains debatable as a heightened frequency of events was already incorporated post-model. Nevertheless the new model has the potential to lead to some amendments in the structure of reinsurance programs. As in the last few years, we expect insurers to continue to evaluate aggregate covers and other solutions to cope with the loss frequency. Despite concerns regarding changes

driven by new model results, we expect there to be sufficient reinsurance capacity to meet the needs of German insurers for all lines of business.

In Germany, 68 percent of all companies supervised by the BaFin participated in the latest Solvency II QIS 5 study while only 50 percent of the smaller insurance companies participated. Compared to previous studies, heavy loadings for manmade losses in general third party liability were introduced to the standard formula. The underwriting risk of non-life companies, which is approximately 53 percent derived by catastrophe risk before any diversification effect, seems to be on the high side. Most clients view the flood exposure as overestimated in the standard formula whereas the storm exposure seems to be reflected realistically.

Third party liability niche business is attracting additional capacity of those reinsurers who try to diversify their portfolio. That said, heavy industrial business and pharmaceutical exposures still have limited capacity.

The German motor market contributes approximately 36 percent of the total non-life premium (EUR55.1 billion for 2010) and shows signs of hardening. However, original rates are still low and cautious rate increases are on average absorbed by the decrease in market premium due to the rebate system. On the reinsurance side the motor third party liability market curve shows a slight increase in rates at the low end of the programs, which is typically driven by individual loss experience. Exposure-driven higher layers of programs have remained fairly stable on a risk adjusted pricing basis over the past few years.

Greece

The economic crisis has negatively impacted the insurance sector more in Life than in Non-Life insurance. However, as the crisis deepens, we expect a further negative impact in the private insurance market.

While the market experienced minimal loss activity throughout the first half of 2011, a fire occurred in July causing approximately EUR30 million (USD43 million) loss, a very significant single loss for the size of the property market, the total volume of which is estimated at around EUR40 million (USD57 million) annually.

Reinsurance premiums are also being negatively affected due to the recession in the direct market, the increase of retentions of cedents, the smaller number of cedents (mainly due to acquisitions and insolvencies), and the reinsurance policy of international groups electing to reinsure more globally and less regionally.

Israel

In 2011 Israeli companies suffered substantial losses that will have a significant impact on the treaty and facultative loss ratio, leading to increased prices from international markets (mainly for catastrophe capacity) on most of Israeli renewals.

While the local market entirely depended on the international market in the past, it is evident the local competition still exists and that these markets are not currently following the lead of international reinsurers.

On the treaty side, companies are still enjoying the terms obtained in last renewal season. In comparison, on the facultative side, local markets are competing on net prices and are covering the difference in conditions on terms imposed by the international markets.

At the moment only accounts that suffered substantial losses last year are paying increased prices, with the remaining 2011 accounts renewing at risk adjusted flat pricing or achieving some price decreases. While there is capacity available for the Israeli market, some reinsurers are attempting to increase prices. Company responses have varied including working with other reinsurers, increasing retentions and co-participations, and buying less limit in an effort to maintain stable budgets for reinsurance.

Italy

When seen in the wider context of the ongoing macroeconomic difficulties faced by Italy, it is hardly surprising that the insurance and reinsurance segments are undergoing a difficult year.

On the direct side, in non-life, the situation is characterized by a continuing lack of growth in premiums. The disposable income of the average Italian consumer is insufficient to foster demand for non-life

products, other than those relating to the much maligned compulsory motor third party liability branch, sales of which continue to make up for over half of all non-life premiums. Recent poor results in the sector, together with subsequent hikes in rates, have also further diminished appetite for this segment.

Life business, on the other hand, continues to fare better, and the recent trend towards increased sales of investment type life savings products is continuing with the latest available figures showing that overall premiums in this segment are up around 20 percent compared to the previous year.

The situation in the direct market is not expected to alter materially in the future. The larger well established companies, with some notable exceptions, are concentrated principally on maintaining their existing portfolios, as well as ensuring adequate capital levels to comply with Solvency II. Competition is particularly fierce in the small and medium enterprise business segment. Smaller or startup companies, on the other hand, are struggling for growth in line with business plans.

Due to the presence in the market of a large number of existing, as well as potential new reinsurers, any significant growth in top line figures will be realistically very difficult to achieve. Expectations for loss ratio figures at the end of the year are flat compared to 2010 as long the second half of 2011 follows the pattern of the first half with an absence of large catastrophe losses, the exception being the continued upward trend in the frequency and severity of hail events in the agricultural sector.

Current reinsurance capacity is more than sufficient to cover the requirements of the majority of lines of business with significant reinsurance cessions, especially bearing in mind such cessions will in all probability continue to decline due to a policy of higher retentions adopted by many larger cedents, and a decrease in the number of overall cedents themselves. Reinsurers wishing to write a significant book of reinsurance business in Italy will be more successful if they are willing to consider all lines programs, rather than concentrating on picking and choosing their preferred lines.

As for products, innovation is still relatively scarce, notwithstanding the imminent introduction of Solvency II regulations, which should nevertheless foster demand for tailor made reinsurance contracts which assist in saving capital and optimizing returns.

Middle East

Primary rates remain competitive in all classes throughout the Middle East. As a result, reinsurers are doing further evaluation on commission levels, with a couple requiring event limits for natural perils, something previously not required.

Overcapacity is still the driving force for the competitive state of the market, but countries such as Jordan and Saudi Arabia now face the prospect of enforced mergers and acquisitions either from financial necessity, or due to changing regulatory requirements.

Once again motor rates remain comparatively flat, with the bodily Injury awards controlled under Islamic law guaranteeing no surge in motor liability claims. This same control of third party awards and the (current) existence of a broadly non-litigious society have made the casualty sector attractive, and there has been an increase in activity in this area.

Growth is also seen in the medical, life and PA sector, with competition for business fierce, although results here vary from region to region and carrier to carrier.

Regardless of the talk of a worldwide hardening of the reinsurance markets, clients have been able to achieve reductions in overall spend, retention, or both often by offering an existing placement to an alternative leader and market. This does not point to an overall hardening in this region, regardless of those poor results that affect a number of participants in each country as the fact that this can be done indicates willingness for reinsurance capacity to be competitive.

Reinsurance areas that have seen a tougher stance being taken are those accounts with significant non GCC/Arab exposures, where the reinsuring participants are less likely to be from the domestic market, and more from the International arena.

Expectations for 2012 will be dependent on the outcome of the 2011 U.S. Hurricane season.

Netherlands

Despite combined ratios often exceeding 100 percent, the insurance market in general remains soft and insureds and direct brokers continue to push for flat renewals as opposed to rate increases. However, on the facultative property side we do see pressure on rates when earthquake or hurricane exposure is involved. Facultative (corporate captive) clients have started to review cat models, a useful tool in respect to their overall risk management for both the Corporate Group as well as specifically for their Reinsurance and Insurance Captive. From this they might purchase higher (sub) limits on their catastrophe exposures.

No major property catastrophe events have affected the market so far in 2011. Many clients are evaluating the impact of RMS version 11.0 on their portfolio and we expect increased interest in aggregate protections, second event covers, and additional reinstatement(s) as a result of the changes.

With regards to Motor General Third Party Liability, due to the 6th Directive, the legal insured limits will increase as a result of indexation.

RMS released the Risklink version 11.0 Euro windstorm model in mid-July. Full implications for our clients have yet to be determined but Aon Benfield has already carried out significant model testing. Our early conclusions from this analysis are that the new model significantly over-estimates loss potential at the lower end of the curve. At higher return periods, we are pleased that RMS has taken note of our previous assertion that post loss amplification (PLA) had been overstated for The Netherlands. However, we are still evaluating the degree to which PLA has been reduced in the new model. Given the questions we have identified regarding RMS version 11.0, we are not recommending that our clients use it to form their views on purchase requirements.

Nordic and Baltic Countries

Following six years of benign cat loss activity in the region, the Copenhagen area of Denmark experienced heavy summer cloudburst flooding in early July. This will significantly impact most of the local and regional

Danish catastrophe programs. We expect the insured market loss to be between DKK3 billion (USD580 million) and DKK3.5 billion (USD675 million). Regarding the release of RMS version 11.0 in mid-July, we have noted significant differences to version 9.0 being the last major release in the region. These differences vary widely from country to country and at the time of writing we are discussion with RMS for clarity on these differences, in addition to carrying out our own analysis.

Pakistan

January 1, 2011 renewals proved difficult due to floods of 2010 which impacted the results of the Pakistani market. The reinsurance prices of property catastrophe excess of loss capacity increased by 8 to 10 percent following the floods.

The government's plan to support and subsidize premiums for crop insurances for subsistence farmers is still under consideration. In line with the directions of the Securities and Exchange Commission of Pakistan (SECP) insurance companies will need paid-up capital of PKR300 million (USD3.5 million) by 2011.

Portugal

2011 continues to be a challenging year. The macro-economic environment is clearly having a negative impact on growth for risk related insurance business both in life and non-life. Private savings are growing as a direct consequence of the uncertainty raised by the crisis but it seems that most of these funds will fall within the banking sector rather than insurance. All of this can be seen through the premium figures at May 2011: down 38.3 percent for life and down 0.2 percent for non-life. That said, the 38.3 percent decrease in revenues for the life sector relates mainly to financial products that were previously sold as insurance and are now being converted back to pure financial products. Despite the decrease in revenues, overall profits at the mid-year mark have increased by 12 percent when compared to the same period last year.

For life insurance, results were sustained through the corresponding reserve releases as a direct consequence of the significant decrease in revenues. For non-life, mid-year profitability is almost exclusively due to property insurance as the other lines of business show a slight reduction of profitability (excluding property, an increase in losses of 0.6 percent). Capital remains at an adequate level with a 174 percent solvency margin, according to the rules presently set by the controlling authority.

On the positive side, primary rates have grown in a few selected segments, particularly in Motor (which represents almost 50 percent of the gross non-life premiums) and workers' compensation, although more diluted in the latter. A lack of major claims in the first half of the year is also a positive factor. Despite this trend in some premium rates, premium production change remains fairly modest with motor up 1.1 percent and workers' compensation down 3.7 percent as of May 2011. Competition on the property side remains fierce and health insurance, following many years of strong development, now shows a more limited growth (up 2.4 percent at May 2011 from May 2010), a direct result of the economic conditions of Portugal.

Following two major mergers in the last two years, further consolidation or change of ownership is quite possible in Portugal particularly considering that the insurance state group, Caixa Seguros, which represents almost 30 percent of the market, may be privatized soon. Movements are expected to occur not only with bank related insurers but also with other groups, including foreign ones.

As virtually all treaties renew in January 2011 presented some improvements for cedents both in capacity, particularly on the property side, and in conditions (small increase in some commissions for instance).

With no major catastrophic events having affected Portugal to date, 2011 mid-year results are better than in 2010 both on the direct side and in reinsurance as last year the market suffered losses from the heavy downpours in Madeira.

International catastrophic events earlier this year had no effect on capacity in Portugal and despite potential pressure on property catastrophe prices; we expect that the positive results of reinsurance contracts in the region to override any global market considerations.

Despite negative expectations by many reinsurers in the recent past, claims in the motor branch continue to settle at controlled levels. Although it is not limited to Portugal, we expect inflation to become an issue in the near future.

South Africa

Given the natural disasters on the worldwide stage, there is growing concern whether companies are buying sufficient catastrophe cover. We expect to receive requests for increased purchases by cedents as well as pressure on reinsurance rates given the relatively low ROLs that catastrophe capacity has historically been secured at for the region.

Retentions are relatively low in comparison to other areas and we expect this will continue as there is still low activity at these levels and no challenges from reinsurers for increased retentions.

Prospective new markets continue to review South Africa as a potential growth area, but have been reluctant to enter due to low rates and lack of commercially available modeling. There has been no significant reduction in capacity from existing markets.

Following July 1, 2011 renewals, South Africa saw an upward movement in rates of 5 to 7.5 percent on a risk adjusted basis.

Spain

Results for 2011 in the reinsurance market have been generally positive in most lines of business with solid margins continuing for reinsurers in motor, liability lines, engineering and credit where experience has improved in the last few years following the losses of 2008.

For many insurers, property classes have experienced negative results due to large risk losses in Spain and the impact of natural catastrophe losses in Latin America in

2010 which continued to affect Spanish interests in the region. Price increases of 10 to 30 percent were experienced throughout 2011 renewals for treaties with loss activity.

Primary results in 2011 are good with relatively little large loss activity. Nevertheless a continued soft market on the direct side has meant that margins are now largely eroded and combined ratios in many classes are in the high 90's. Liability classes remain strong despite competition and have been minimally impacted from the financial crisis. Motor insurance, the largest element of the non-life market, is experiencing an aggressive price war with several direct writers attempting to gain market share. The consequent deterioration of margins and the more than likely modification in the next couple of years of the "baremo" law resulting in an increase to bodily injury pay-outs, could reduce or eliminate profits for the segment.

Switzerland

New reinsurers continue to domicile in Switzerland as a result of the attractive fiscal parameters, good infrastructure and skilled professionals in the Swiss insurance and reinsurance market.

Reinsurance capacity remains abundant, the market remains soft and a hardening of conditions is not likely, unless Switzerland gets affected by severe events in the near future. Competition is still fierce on the direct side in Switzerland and rumors of mergers are passed around again with insurers trying to optimize their general costs.

Turkey

The Turkish Insurance market is a growing dynamic industry with a 6-month growth rate of 25 percent compared to the same period last year. However, due to the depreciation of the Turkish Lira from the last renewal, overall exposure is expected to remain similar in Euro terms. As a result, we do not expect overall purchase limit and the retention levels to change.

Capacity also remains stable despite recent loss activities in other territories and model changes that may put pressure on renewals.

U.K. and Ireland

The U.K. property catastrophe market has seen prices harden slightly during 2011 due to worldwide catastrophe losses. Budget pressures have reduced the amount of limit purchased slightly for the market as a whole with retention levels remaining relatively stable. Prices in the first quarter were down five percent or more on a risk-adjusted basis however by July 1, prices were flat as recent international losses increased significantly.

While RMS released the Risklink version 11.0 Euro windstorm model in mid-July, full implications for our clients have yet to be developed; early indications are that occurrence and aggregate losses have increased significantly at all return periods. Aon Benfield continues to work with RMS to fully understand the rationale for the changes and convey this message to clients in order to evaluate any potential changes in risk management strategies.

While the recent riots in the U.K. have in excess of GBP200 million (USD330 million) worth of damage to homes and businesses, according to the Association of British Insurers, they will have no impact on the reinsurance market following the government invoked Riot Act on August 11 resulting in almost all losses paid by insurers being subrogated back to the metropolitan police authority.

U.K. Motor reinsurance pricing has risen considerably in premium terms due to concerns about bodily injury claims inflation in particularly Periodical Payment Orders (PPO's) and an impending Discount Rate decision which, if a reduction is ordered, will result in rises on all bodily injury outstanding amounts. This has coincided with a time of severely worsening motor insurance claims, in large part due to low cost injuries, which has increased original rates considerably. The effect has been that reinsurance rates have been maintained or showing small increases at recent renewals. This trend will continue with final decisions depending on individual level of deductible and experience.

Americas (Ex-U.S.)

Canada

In primary insurance, there continues to be extensive capacity in the large, industrial commercial market resulting in price competition with no obvious end in sight. New provincial regulation to the Ontario automobile product has brought improvement in results that are welcome, but generally considered temporary.

The predicted consolidation of a fragmented market is taking place with RSA's purchase of GCAN and Intact's purchase of AXA resulting in Intact having 15 percent market share. In addition, the Economical Mutual Insurance Company announced its plans to demutualize and will be the first mutual property and casualty insurer to do so in Canada. This is of significant interest to the Canadian insurance market as the regulations are being written to allow for this demutualization.

Finally, due to the regulatory changes of Part XIII of the Insurance Act and regulation B3, more international insurers are domesticating portions of their reinsurance placements.

From a reinsurance perspective, Canada remains an attractive market and capacity remains plentiful. Reinsurers continue to offer capacity both on a registered and unregistered basis; however, due to consolidation and the capital strength of insurance companies, we expect the gradual increase in retentions of recent years to continue. Stable catastrophe limit purchases are anticipated with no significant catastrophe model changes effecting Canada.

These factors set the stage for a competitive domestic reinsurance market with adequate capacity available despite the fact that the Canadian industry may have experienced its second largest catastrophe insured loss year in history from the Slave Lake fire.

Caribbean

The major challenge for the region in the short term is RMS version 11.0, which has resulted in significant increases in the 100-year and 250-year return period numbers for many islands. This has potentially significant implications for reinsurance, local regulators and for companies Rated by A.M. Best in particular.

Overall we don't expect reinsurance buying patterns to change although there may be increased retentions in some of the non-property classes in line with stronger balance sheets.

Overall the reinsurance market for Caribbean business remains stable with capacity showing little movement through April and July renewals despite international losses. However, the market remains relatively narrow with only a few new entrants in the last 12 months.

Chile

Following the 2010 earthquake and resulting primary rate increase, a number of insurance companies are looking to expand into the market. Terms and conditions for primary business remain stable.

Retentions remain conservative as a result of the significant regulatory impact of allocating internal capital for catastrophe events. Reinsurance continues to be a more attractive way of managing catastrophe exposure.

Overall pro rata capacity remains stable with any loss in capacity from existing reinsurers being filled with new market entrants. Terms and conditions for these programs remain stable.

Model miss for Chilean earthquake remains a concern and many catastrophe modeling firms have begun calibrating their models based on recent loss activity. That said, we are unaware of any new model releases in the new future.

Columbia

2011 summer renewals saw risk adjusted rate increases of 5 to 7.5 percent for catastrophe programs and up to 50 percent for risk programs following severe flooding in the first half of 2011. Economic losses are estimated at USD5.8 billion. As a result of the flood events, insurers are looking to increase the current hours clause from 168 to 500+.

Primary pricing in Columbia is not expected to change materially following the recent catastrophes, but increased pressure is expected on deductibles.

While regulators continue to expect the industry to manage exposure up to fifteen percent of the main zone aggregate, retentions remain similar to last year, and limits increased around ten percent.

Pro rata still shows lack of capacity as there is no limit per event.

Mexico

Pro-rata terms and conditions remain constant for 2011. Excess of loss capacity remains stable with new entrants actively replacing any reinsurers lines withdrawn from prior renewals. Despite pressure to increase rates for mid-year renewals, final pricing renewed at flat to up 5 percent on a risk adjusted basis compared to the prior year.

Sector Analysis by Specialty

The following provides an update on the following significant reinsurance lines of business: Global Re Specialty, U.S. business segments and Facultative.

Global ReSpecialty

Accident, Health and Life

Although significant insured losses were incurred by reinsurers as a result of this year's catastrophic events in Australia, New Zealand, Japan and the tornados in the U.S., Accident and Life catastrophe programs were generally unscathed due to high attachment points and other mitigating factors. Accordingly, most June 1 and July 1 renewals saw some risk adjusted rate decreases, though not to the same magnitude of prior years with the maximum relief in the low to mid-single digits. More disciplined underwriting in light of industry losses has slowed down the pace of reductions in general. Additional capacity continues to flow into the market as reinsurers are still over capitalized and seek to deploy their capital to maintain premium levels. New markets continue to be interested in growing their shares in Latin America to diversify exposures, particularly in Brazil, Mexico and Columbia. The recent turmoil in the financial markets remains a concern that could exert pressure on capital levels, but this is a fluid situation. Recent changes in early 2011 to wind catastrophe models have had little to no effect on the PMLs for Accident and Life portfolios.

Aviation

Aviation losses to date have been incredibly low for reinsurance markets. Without frequency or severity events it is difficult to see rates holding. If direct rates do fall buyers will begin to look to reduce percentage of income spent on reinsurance. In contrast, exposure is increasing by all exposure metrics used to monitor aviation risks and we expect a combined increase of 7 percent compared to 2010. Geographical exposure is changing rapidly as Brazil, Russia, India and China economies grow while U.S. and European economies stagnate. Claims frequency has increased in developing nations and probably reflects the exposure growth seen over the last five years. Claims severity in the U.S. remains a concern but with little or no frequency rates remain depressed.

Capacity is available for all levels and types of reinsurance and provides accretive risk transfer for this volatile class. Primary layers test demand but generally only when deductibles are below USD200 million or if clients security criteria restricts marketing. Middle layers attract huge capacity and non-aviation specialists will deploy aggregate wherever possible. Catastrophe layers can now be placed below 1.5 percent rate on line.

Deductibles and vertical limits have remained stable since the Air France loss in June 2009, although new entrants have secured very low retentions when presenting a viable business plan. Overall capacity outweighs demand. Rates, regardless of wider market losses, appear unlikely to increase. It could be argued that reinsurers are focused on maintaining income with two driving factors: little loss activity with reinsurers reporting above average returns on a combined ratio basis and diversification benefits gained against core property and casualty lines.

Solvency II regulation and capital modeling are becoming more prominent with reinsurers but have yet to hold enough weight to drive an aggregate reduction.

Throughout 2011, rates have softened five to ten percent on a risk adjusted basis; meanwhile July was more difficult to achieve reductions as pressure was applied by reinsurers that had suffered significant losses from non-aviation lines.

Credit, Bond and Political Risks

Despite the continuing global debt issues, results of Credit & Surety business have continued to improve in the last twelve months. Loss ratios have fallen to levels pre-2008, and major insurers have announced significant increases in profits in the first half of 2011. The market has largely avoided many of the larger and high profile insolvencies.

In the underlying market the improved results have led to increased competition amongst underwriters. Reinsurance pricing has also softened in 2011, and the majority of insurers now enjoy better treaty terms. Available capacity in the reinsurance market remains strong, continued increases in supply and improved results have been contributing factors to reductions in pricing.

Although political problems in Middle East & North Africa have caused concern for the market, claims activity has not been as widespread as may have been feared. The greatest potential for claims relates to the events in Libya. That said, the developments are not seen as being a major problem for the market as a whole.

Marine and Energy LMX and International

Subsequent to the January renewal season, there have been a number of energy losses affecting the market (Maersk Gryphon, Devon Energy, Petrobras, Jupiter I).

While the total was estimated at USD1.4 billion, with Maersk Gryphon being the most significant, the overall impact to the reinsurance market is not as marked as the impact from Deepwater Horizon. That said, the rating environment will likely remain firm for covers that have an energy component and in some quarters, markets to consider their market attachment level for 2012 as a result.

Marine pricing has remained stable as reinsurers seek to balance their portfolio with less volatile lines. Of a greater challenge to clients is the need to be explicit with respect to energy liability business written into their primary accounts. Lloyd's have been particularly tough on syndicate business plans that include energy liability business and packaged policies in particular.

While the hull, cargo, and liability portfolios have not had the large single market losses to cause significant effect to these portfolios, there will potentially be some impact from the above mentioned energy losses. Further we would note that the Australian and New Zealand catastrophe events did not create substantial losses within the marine portfolio, a significantly different outcome than what was experienced in Japan. With the effect from the Japan loss unknown, marine loss amounts may still be contained in comparison to the EQ magnitude and tsunami severity. Although this event impacted the Japanese renewal it had little influence elsewhere.

International business (excluding LMX) is a targeted area for many reinsurers that is generating its own competition. Nonetheless, we are seeing clients show

some loyalty to reinsurers due to past years downward trends in exposures and reinsurance costs. Additionally, more territories are seeking reinsurers to be registered in their market, which is increasing complications for reinsurers.

The retrocessional market has been equally impacted by a number of the above losses, in particular from reassured's who write a combination of excess of loss and proportional treaty business.

Non-Marine Retrocession

The value of retrocession products have certainly been demonstrated this year as a number of clients made significant recoveries from the 2011 catastrophe events. More importantly, in the immediate period following a major catastrophe, when reinsurers are seeking to understand, quantify and advise senior management, investors and or shareholders of their exposure to the event, the comfort of releasing a net figure (retro retention plus reinstatement costs) has been an advantage to those publicly listed reinsurers buying well-constructed programs. This news management effect continues to benefit the reinsurer as complicated losses develop and has proved to be a significant strategic advantage for those who use these products.

The release of RMS version 11.0 in February is now starting to filter through reinsurers portfolios and influencing the decision making process from both a buying and selling perspective primarily for U.S. exposures. The more recent European windstorm release has again produced dramatic changes to return period numbers and will cause ongoing additional capital strain for some reinsurers.

RMS Model change results have had a wide range effect on the pricing of retrocession products from UNL and an Index perspective. ILW pricing reacted quickly to the changes in modelled exposures, whereas UNL pricing shifted more reluctantly. This phenomenon was due to various reasons but predominantly as a result of increased demand of ILWs post January. UNL pricing is a more fundamental and stable element of a reinsurers portfolio (i.e. less opportunistic).

Retrocession pricing for global cover was flat to down 7.5 percent (subject to 2010 loss experience) for January renewals. Although January is the largest renewal of retrocession, there remains a significant amount of capacity which is traded later in the year. Pricing through the first and second quarters steadily reacted to the market environment as loss results clarified, further losses occurred and the model change started to impact retrocessionaires pricing models.

On the basis of potential price increases for UNL retrocession and ILWs, a number of ILS funds have been set up to target this opportunity. A significant amount of capacity was raised post Japan earthquake and was successfully deployed.

We expect buyers to seek products that help manage net retentions as pressure on current attachment levels increase in addition to addressing the increased frequency of global catastrophe events which erode annual profitability and retained earnings. We also expect emphasis on products that dilute the impact of model change to manage portfolios during the remainder of 2011 and into 2012. Meanwhile, reinsurers will study the benefits of “diversification” against the cost of retaining and/or buying cover.

Specialty Casualty

There have been no noticeable signs of price hardening so far in 2011, with more than adequate capacity remaining in the Company and Lloyd’s market for both general and employers’ liability and the professional and financial lines segments. However, the most recent economic events have started to impact capacity and conditions in the financial institutions arena. Pricing levels for general liability and employers’ liability remain competitive with many reinsurers quoting at expiring price as an opening offer. Both segments’ reinsurance remain benign and appear to be immune from large catastrophic loss events especially if we discount United States exposed pharmaceutical exposures and related class actions. New entrants are expected to cover both general liability and employers’ liability as a part of their strategy, which should increase capacity dramatically but is not expected to depress pricing by any meaningful degree over the next half year.

The financial and professional lines segment has remained competitive with abundant insurance capacity during 2011 and a relatively favorable current claims environment. However, prior year claims have started to halt reductions in original price on financial lines accounts, although this has failed to make a meaningful impact in the professional lines area.

The financial institutions market, despite seeing some additional insurance capacity, has remained more conservative with limited rate reductions due to claims from the many financial crises in the past few years. Past losses have taken their toll with some reinsurers reducing lines and the availability of reinsurance capacity tightening.

Commercial has continued with little change, no major new entrants and a small number of exits with reinsurance capacity widely available. However, concern is growing that results are now marginal and that a turn in the market will be forthcoming. One interesting view point is whether the commercial book will see a greater impact from a prolonged financial crisis due to the inability of commercial entities to meet their own debt obligations with the consequence of there being a greater frequency of insolvency events.

Financial institutions business in the primary market has been under the microscope for a few years now and with capacity under pressure this market could well see some significant corrective action in the coming months that will gain momentum throughout 2012. Reinsurers’ appetites have changed in light of recent economic events, causing them to attempt to quantify their exposures. It does not necessarily follow that insurable claims will result from this crisis but there is clearly a shift-change in the expectation of company default and D&O claims and PI/fraud actions within the markets. Correspondingly, limits have reduced, either as a result of original line sizes being curtailed or due to the relative increase in reinsurance deductibles.

The reinsurance buying atmosphere has remained fairly constant. However, from a financial institutions perspective, buyers’ concerns during the ongoing financial difficulties means increasingly restrictive proposals are being purchased.

While there is no direct correlation that losses will result from the current financial situation, it would be a brave insurer that retains their position gross in the current uncertain environment. Therefore, demand for financial institutions reinsurance increases, which poses a problem in mobilizing adequate capacity prepared to support new purchases or more recent market entrants, especially as there was a reduction in Florida reinsurance capacity through January renewals.

Variable Annuities

Sales of variable annuities increased over 10 percent in 2010 to over USD140 billion. Several large U.S. companies developed new products with lifetime income guarantees which led to even more soaring sales during the first two quarters of 2011. Customers were happy to participate in positive stock and bond market returns while protecting the downside with lifetime income guarantees resulting in sales increases in 2011 up 20 percent over 2010. Some companies have seen 50 percent increases over its own sales figure. As a result of consolidation in the market over the last 18 months, the U.S. market is now dominated by relatively few life insurance companies. Hedging strategies have become even more sophisticated and will prove interesting to see how they hold up during the current turmoil in the financial markets. The reinsurance market continues to be relatively limited with traditional reinsurers wary of market risk and policyholder behavior risk. Several banks are providing packaged hedging/reinsurance solutions but also on a limited basis at terms some companies find out of line with their own pricing.

United States Business Segments

Property Catastrophe

While a significant portion of the 2011 hurricane season remains, severe weather activity in Q2 affected a number of regional and national reinsurance protections. As expected, rate increases occurred on layers experiencing losses, while layers without losses were flat to down 5 percent directly in line with our guidance in April.

One trend that emerged for mid-year renewals is that companies with decreasing exposure found it difficult to achieve commensurate price reductions simply due to the optics of reduced premium on similar layers of a program.

Reinsurer capital remains stable and at adequate levels for insurers seeking additional capacity.

The impact on demand of the RMS version 11.0 change has yet to be completely realized but early indications show that overall demand will not change significantly. Many insurers had already implemented a multi-model approach to evaluating catastrophe risk which served to mitigate the impact of a single model on risk management discussions for buying reinsurance and pressure from rating agencies to secure additional capacity.

Property Per Risk

Exposure change will continue to have a direct influence on the cost of programs. Beyond exposure change, experience and catastrophe exposure will remain key drivers of pricing. The catastrophe losses in the first half of 2011 and the release of RMS version 11.0 are the most frequent point of discussion among clients and reinsurers. Programs with good experience and moderate catastrophe exposure should continue to get modest reductions. Programs that have experienced losses and/or add to key zone catastrophe accumulations will likely be asked to pay similarly modest increases.

Data quality will be a heightened area of focus. Clients with well-articulated underwriting plans that are supported by good data, modest catastrophe exposures and good results will continue to have ready access to additional limits if desired.

Medical Professional Liability

The 2011 reinsurance market for U.S. medical professional liability business remains stable with ample capacity in the U.S., London, Europe and Bermuda. The medical professional liability insurance market continues to post excellent results given favorable prior year loss development and historically low levels of loss frequency. The insurance market continues to exhibit soft pricing and significant competition, but rate decreases are moderating.

Reinsurers continue to hold their core books of business with flat to slightly decreasing rates on an exposure and experience adjusted basis.

The outlook for 2012 includes ongoing favorable industry results from continuing loss reserve releases and significant competition. Medical professional liability insurer challenges include the accelerating consolidation of medical providers (physicians, hospitals and facilities) and the impact of ongoing healthcare reform.

Lawyers Professional Liability

Lawyers professional liability treaty reinsurance pricing for 2011 is stable on an exposure neutral basis. Treaty reinsurance capacity is plentiful from active markets in the U.S., London, Europe and Bermuda. Facultative reinsurance capacity remains relatively limited, but exhibits signs of increasing, with stable to slightly decreasing pricing.

The lawyers professional liability insurance market is showing signs of deteriorating results given increasing claim frequency and severity especially in certain states and for certain areas of practice such as corporate/commercial transactions, real estate, litigation and financial institutions. Increasing loss adjustment expense has also served to drive higher claim severity.

The outlook for 2012 includes a generally soft insurance market with significant competition from commercial and specialty lawyers professional liability insurers. Certain insurers will attempt to achieve rate increases and/or refine underwriting approaches to improve results.

Directors and Officers Liability

During the first nine months of 2011 pricing for D&O and Professional Liability treaty reinsurance remained relatively stable for portfolios that continue to perform profitably on an overall basis. Reinsurers have been willing to ride out the soft underlying insurance market with their core clients. Aside from the pricing issues, reinsurers have been willing to entertain improvements/broadening of other terms and conditions for clients exhibiting profitable track records, well balanced and diversified portfolios with a history of reinsurance

partnership. Expansion of covered lines of business, territorial expansion, and relaxation of certain treaty exclusions are some examples of the broadening.

Over the last several months we have seen a modest expansion on the reinsurance supply side. Reinsurers who have been sitting on the sidelines over the last several years in the wake of the Subprime/Credit crisis are beginning to exhibit signs of renewed interest/participation. Treaties that are more structured in nature are receiving more favorable attention from reinsurers than those that are unlimited in nature and or more prone to systemic losses.

As we move forward into 2012 we will be watching a few underlying trends/issues to gauge how the reinsurance market will react. First, while the continued pressure on underlying D&O insurance rates will be a focal point for reinsurers, the underlying trends in the frequency of securities class action claims, a strong predictor of ultimate loss ratios, continues to be very favorable. Other looming concerns are the global debt crisis and the potential effects a double dip recession may have on corporate America. These global economic concerns have reinsurers looking more closely at the markets for the next potential systemic exposure.

General Casualty

For 2011, casualty excess of loss reinsurance program renewals saw flat to 2 percent reductions for rate change on treaties with good loss experience. Proportional renewals achieved flat to an increase of 1 percentage point in ceding commissions on treaties with good loss experience. Further, there has also been some trend of a bundling of coverages previously reinsured separately.

Aon Benfield has seen clients conflicted over whether to keep larger net retentions in order to retain more income versus buying more coverage as their direct business continues to be under rate pressure leading to increased loss ratio picks; some reinsurers have reduced capacity as a result. Many portfolios, both new and existing, continue to operate at profitable levels and reinsurers are attempting to analyze business plans and support those clients that can demonstrate profit

through actual loss experience and/or from a rating strategy that enables profit even in a challenging insurance market. Companies with actual experience continue to have an advantage in terms and conditions and new operations have faced greater difficulty in securing capacity from the highest quality reinsurers.

Workers' Compensation

To discuss the workers' compensation marketplace we will view the market from three vantage points. The first view will be the primary market, the second view will be the working layer reinsurance market and the third view will be the catastrophe workers' compensation market.

The primary workers' compensation market is a mature soft market. At the end of 2010 the overall combined ratio including state funds was 122 percent. The changes in 2011 have not been significant so the predicted loss ratio for 2011 is in the 127 to 130 percent range. The most concerning part of the recent developments is the fact that for the first time in 13 years we experienced a frequency increase of 3 percent in 2010. The long term trend of frequency declines has helped to mitigate the increases we have seen in medical and indemnity severity. If frequency continues to increase base loss cost rates are difficult to project and even more difficult to be implemented politically.

We have had a long term trend in severity increases in workers' compensation claims. That trend did not continue in 2010 as severity leveled in both medical and indemnity. Most believe that the leveling of severity is caused by the advent of Medicare set-asides which has resulted in large claims being delayed or not settled in the prior year's normal pattern. We think the same pattern will continue through 2011 and beyond. This does not mean that severity has subsided; it means that it is more difficult to see.

In addition to increased frequency we have two work force scope issues that will continue to pressure workers' compensation rates. Obesity and the aging work force will bring new variables to the loss side that we have not dealt with in the past. If we compound

those factors with the current economic conditions we will have an aging work force working longer into their lives. As a result, making and implementing adequate loss cost rates will be a challenge in our near future.

We are starting to see some reaction to the losses, and the frequency and severity trends in the primary market. Five states in 2011 — Montana, Illinois, Kansas, Oklahoma and North Carolina have enacted law reforms that were all aimed at reducing workers' compensation loss costs. If these reforms are truly implemented and other states follow we could see an opportunity to reduce the overall combined ratios.

The workers' compensation working layer reinsurance market has become a bit more conservative in 2011. We have seen the frequency and severity trends push up the technical pricing on many portfolios and as a result the recent renewals have been flat to up 3 to 5 percent. The renewal changes were dependent on states and loss ratios of the portfolio. Capacity for the renewals was still adequate with USD20 million MAOL's readily available. It should be noted that contract terms were far easier to negotiate than prices. One notable new entrant to the working layer business was the Lloyds market. It does not appear that they have any intentions of burning their way in but their presence is a welcomed addition to the market.

The catastrophe workers' compensation market remains competitive and with more than ample capacity. The industry has had very few claims in the catastrophe area and as a result rate on lines continue to erode. California catastrophe layers have been coming in around 2.25 to 2.50 percent ROL and non earthquake perceived states are in the 1.5 to 2.0 percent ROL area.

Surety

The surety market has continued to produce better than expected results throughout 2011 however S&P's recent downgrading of U.S. debt, a sluggish construction economy and possibility of a double-dip recession has created significant anxiety as respects the future performance of this line during 2012.

In light of the proposed spending cuts coming out of Washington, along with state budget deficits, sureties remain concerned that public work will remain scarce and contractors will not be able to increase backlogs during 2012. The longer the economic downturn persists, the more difficult it will become for contractors to weather this storm. Continued high unemployment in the construction sector suggests no immediate end to these challenging economic times.

Top line revenue for many sureties has fallen over the last two years as limited spending in the U.S. for infrastructure improvements requires fewer bonds. With the European debt crisis stagnating overseas growth and Latin American economies cooling off, even global sureties will find growth hard to come by during 2012.

Primary pricing, terms and conditions for contract surety remains fairly stable however increasingly large bid lists continue to result in less operating margin for the winning contractor. New competition in the commercial surety sector has eroded terms and conditions. For the best rated credits, primary pricing has been reduced and collateral waived. Many sureties are increasing their commercial capacity in an attempt to stave off new entrants in this space.

Contractor failures have risen modestly, but many contractors are winding down their businesses in an orderly fashion and have not caused serious issues for sureties. Despite the competition, commercial surety results have been stellar and no increase in loss ratio is apparent.

With regard to surety reinsurance, many sureties increased treaty retentions over the past several years in an effort to maximize net retained income. Reinsurance pricing remains favorable from the buyers' perspective.

Terrorism

The first eight months of 2011 have seen significant developments in the threat presented by terrorism. The death of Osama bin Laden and the continuing unrest in the Middle East and North Africa have created at least the perception that the terrorism threat has been elevated.

In addition to this increased threat from conventional terrorism, the risk of cyber terrorism is on the rise. Through June 2011, approximately 20 cyber attacks on U.S. private and public sector targets have been identified by cyber-security agencies and 2011 is already viewed as the worst year ever for security breaches.

Despite these developments, the terrorism reinsurance market has not been altered in a significant way. There remains substantial unused capacity for U.S. terrorism risk. Clients continue to secure "domestic terrorism" coverage, i.e. coverage for events perpetrated by domestic agents, through mainframe property catastrophe cover. In addition, workers' compensation catastrophe covers continue to offer substantial terrorism coverage. Avoidance and mitigation of the exposure and reliance on the federal backstop are key components in carriers' strategy to deal with terrorism exposure. Program limits in excess of USD500 million, theoretically up to USD1 billion, can be achieved for conventional terrorism. Limits available for coverage including nuclear, biological, chemical and radiological (NBCR) perils are lower but still into the hundreds of millions.

The oversupply of stand-alone terrorism reinsurance capacity has kept pricing at recent historic lows. Conventional terrorism cover on an aggregate all lines basis is available at mid-single digit rate on line. Terrorism coverage including NBCR is available at slightly higher single digit ROLs.

In addition to the evolving factors mentioned at the outset, there are three other factors that have the potential to introduce turmoil to the terrorism market:

- > **TRIA:** The stability in the terrorism reinsurance market has been guaranteed by the 2002 establishment of TRIA and its successor bills. The Obama administration has periodically cited the legislation as a target for reduction in budget discussions with the recent focus on federal spending amplifying those discussions. Any reduction or elimination of TRIA would dramatically alter the dynamics of the U.S. terrorism reinsurance market.
- > **Rating Agencies:** Increased scrutiny by rating agencies on the terrorism threat and clients' management efforts to address it could serve to dramatically elevate demand.

- > **U.S. Event:** Lastly, any significant terror event on U.S. soil would also change the supply/demand dynamic. Clients should continue to be aware of the changing landscape and consider stand-alone terrorism coverage to augment their management of the evolving exposures.

Facultative

The first half of 2011 will go down in history as being one of the worst on record for the Facultative market due to the severity of losses. With substantial Facultative market losses from natural catastrophes such as the Australian Floods and Cyclone Yasi, New Zealand quake II, the Japanese' quake and tsunami and the United States tornadoes, the Aon Benfield Facultative Index (ABFI) indicates that the direction of facultative reinsurance rates in the global facultative market in H1 2011 has varied by region and line of business.

Property

The facultative reinsurance market has seen specific examples of rate increases being applied to property facultative catastrophe renewals in the APAC region and to a lesser extent in North America, while elsewhere, in those areas that had not suffered devastating losses, we have seen a continuation of facultative market softening.

Even allowing for the fact that the United States was in mid-tornado season, the volume and strength of the tornadoes by the end of H1 has been unprecedented; consequently, property facultative catastrophe rates in the North American domestic market at the end of Q2 saw an increase of up to 4 percent (although those accounts that had clean loss records in many cases saw flat renewals) while property facultative non-catastrophe rates in the North American domestic market increased 1 percent. These contrast dramatically to the 15 percent reductions seen in both catastrophe and non-catastrophe facultative rates in the corresponding quarter in 2010. Property facultative rates for U.S. business placed into the London market increased 10 percent (catastrophe) and 5 percent (non-catastrophe) in Q2, largely due to the recent

tornadoes and the Midwest floods. In addition, insurers are now beginning to use the RMS version 11.0 model, resulting in aggregate issues and concerns that may impact market capacity going forward.

Following the significant disasters in Australia, New Zealand and Japan, catastrophe property facultative rates increased in the region by the end of H1 2011, with domestic markets seeking facultative rate increases of up to 25 percent for Australia & New Zealand. Elsewhere in Asia, domestic markets looked for an average 10 percent increase for property facultative catastrophe business. Property facultative non-catastrophe business in the region's domestic market also come under pressure with increases of 10 percent seen for Australia & New Zealand and the rest of Asia. In London, facultative accounts that incurred losses were particularly impacted, with some New Zealand property facultative catastrophe renewal businesses quoted increases of more than 100 percent with lower limits.

In Japan, the important April 1 renewal process was overshadowed by the devastating Tohoku earthquake and tsunami, resulting in facultative renewal negotiations being interrupted while insurers and reinsurers reviewed the position and tried to assess the impact; although uncertainty remains for reinsurers and insurers, by the end of H1 some property facultative catastrophe business had been quoted at a 30 percent increase in the domestic and London markets. Rating on property facultative non-earthquake business edged up by 2.5 percent domestically and internationally. In addition, due to well publicized supply chain disruptions resulting from the Tohoku earthquake, which have impacted businesses not just in Japan but also around the world, contingent business interruption (CBI) exposure and coverage has become a major topic of concern to reinsurers and we expect there to be a renewed focus by underwriters on the topic of CBI in negotiations going forward.

In Europe, French domestic markets saw property facultative catastrophe rates increases of up to 5 percent, with some French facultative reinsurers moving away from multi-year policies, often a sign that they believe property facultative catastrophe rates will continue to increase. Non-catastrophe facultative rates were flat in France. In the Nordics, the domestic insurance market in general is quite stable, with no major losses having occurred and local combined ratios still healthy yet moving slowly upwards. The Netherlands domestic market saw property facultative catastrophe rates increase by 5 percent with non-catastrophe facultative rates remaining flat. Moving away from Europe, catastrophe and non-catastrophe facultative rates in the Middle East domestic markets fell by 3 percent and in Africa non-catastrophe facultative rates fell by 2.5 percent and remained flat for catastrophe business. The London market looked for 10 percent increases for property catastrophe facultative business emanating from Europe, 7 percent increases for Middle East facultative business and flat for African facultative business. For non-catastrophe facultative business, the market was flat across EMEA compared to 10 percent reductions this time last year.

Casualty

U.S. domestic carriers have continued to offer facultative rate reductions of circa 1 percent by the end of H1. The London facultative market has been more aggressive for U.S. casualty business in Q2 offering reductions of up to 5 percent as they sought to retain and attract business. On average, domestic market casualty facultative pricing outside of the U.S. fell nearly 2 percent in Q2 2011 compared to 4 percent in Q2 2010. London facultative underwriters offered smaller reductions than the domestic counterparts for international casualty business at 1 percent, in line with last year.

2011 Property Catastrophe Renewals Recap

Aon Benfield is pleased to confirm our guidance for U.S. renewals in July was again predictive. While reinsurers suffered losses internationally, pricing in the U.S. was reflective of the fact that losses for many reinsurers were well within earnings maintaining a strong capital base and supply to support pricing at current levels.

Exhibit 38: United States July 2011 Renewals

United States	ROL Changes	Capacity Changes	Retention Changes
Property Lines National	-5% to Flat	+5%	+5% to +10%
Property Lines Regional	-5% to Flat	+10%	Stable
Florida 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%

Source: Aon Benfield Analytics

In addition, we provide a general update on price change for the rest of the world for 2011 renewals.

Exhibit 39: 2011 Non-United States Renewals

Rest of the World	ROL Changes	Capacity Changes	Retention Changes
Europe			
Northern (wind dominating)	-5%	+3%	Stable
Southern (quake dominating)	-5% to -7.5%	+10%	Stable
U.K. and Ireland	Flat	Stable	Stable
Japan			
Earthquake	+20% to +50%	Stable	Stable
Wind and Flood	+5% to +10%	Stable	Stable
Australia	+15% to +70%	Stable	Stable to +25%
New Zealand	Experience Driven	Stable	Stable
Canada	Flat to +5%	Stable	Stable to +10%
Latin America			
Chile	Flat	Stable	Stable
Colombia	Flat to +5%	Stable	Stable
Mexico	Flat to +5%	Stable	Stable
Caribbean	Flat to +5%	Stable	Stable

Source: Aon Benfield Analytics

Assumptions: No changes in insured catastrophe exposures. No significant catastrophe model changes. No significant catastrophe losses occur before negotiations are completed. Rate of change measured from the expiring June through July 2010 terms.

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