Sailing close to the wind
August 2008
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FOREWORD
This time last year few commentators and analysts were forewarning us of the true financial implications of the collapse of the sub-prime market. Here we are, twelve months later in an extremely challenging economic environment, having witnessed the slowdown in the economies of most Western countries. Many of the international banks have been obliged to strengthen their balance sheets and some well-known financial institutions have failed.

Against this background the marine industry has continued to thrive. Shipyards and Shipowners have continued to out-perform, with innovation driving many projects to greater heights and lengths! Commodity prices have remained high as there continues to be concern over the availability of a number of raw materials and world trade values have continued to increase.

Prompted by the economic climate, those serving the marine industry are now tackling old issues and inefficiencies. The insurance market is providing new products and services, struggling for greater operational efficiencies and there is more discussion of industry-wide problems such as the global crew shortage. We at Willis are playing our part to drive these improvements.

The continued trend towards a softening market in many countries has been fuelled by new entrants and general maritime results. However, over the next 12 months we will see more insurers changing their underwriting philosophies as the cost of capital impacts the insurance industry.

Therefore, in order to analyse the impact of these changing and challenging circumstances, my colleagues and I are pleased to offer you this latest Willis Marine Market Review.

Alistair Rivers
August 2008
INTRODUCTION
The business of underwriting is both capital and skill intensive. Neither of these assets can be simply switched off or even put to one side and reactivated at a more attractive point in the underwriting cycle. Before concentrating on the individual Marine markets we must first look at the bigger picture summed up so well by the Chief Executive Officer of AMLIN, Charles Philipps:

“On the plus side, the London Market has never been so well positioned to manage the cycle. In particular, the Lloyd’s market has made huge progress over the last decade. Having clawed its way back, battered and bloodied, in the 1990s from a solvency crisis that few, initially, would have predicted it would survive; it has slowly, steadily and methodically rebuilt its brand in global markets. It has grown its capacity, brought new investors into the U.K. insurance sector, achieved the first ever insurance market rating, has built on that position and has gripped the issue of market process reform.

In underwriting terms, key differences between now and the last soft market include a radical improvement in the depth, breadth and quality of management information within the market. Combined with such initiatives as the U.K.’s move to risk based capital and the successful implementation of Lloyd’s Franchise Performance regime, the market’s ability to manage the cycle has improved out of all recognition.

Such developments have been further underpinned by increased divergence in the cyclical position between classes, the increased scrutiny by rating agencies and the greater involvement of capital markets in the sector.

What has yet to be truly tested, however, is the ‘human factor’. Now, as never before, it is vital that those within the London Market – both at board and the underwriter level – resist the pressure of softening markets to slip back into the bad underwriting habits of the past.

Abandoning underwriting discipline at this point would be disastrous and not just for results. The very progress that has been made over recent years means the market has run out of excuses for getting it wrong. There will be no easy market process scapegoats to blame, no compelling arguments for why the market will do better next time – and there will be no second chance for the London Market’s future credibility and reputation.”

When Marine underwriters in London raised prices in late 2001 and 2002 following ‘9/11’, the Scandinavian underwriters saw this as an overreaction. By offering stable pricing they increased their market share at the expense of the London market.

Today, while all Marine underwriters would prefer higher premiums, it seems to be the Scandinavian market which feels that it cannot survive without them. Unusually the leading Scandinavian hull underwriters are actually turning away business in their determination to raise prices.

In the words of Paul Springman of Markel “this is the first time in three or four years we’ve heard about any product line moving anywhere other than down”.

Willis Marine Market Review August 2008
Shipping market

Despite the looming recession that threatens the global economy, so far the shipping market has remained buoyant. The emerging economies of China and India continue to lead demand, as they import raw materials to drive their expanding economies. This demand for key raw materials has bolstered the dry bulk sector, particularly Capesize, pushing prices and freight rates to all-time highs.

In recent years, the demand-driven shipping market has led to a boom in the number of newbuildings ordered. Many of these newbuildings will be delivered in 2010. These additions may flood the market, especially if there is not adequate scrapping of old vessels. Recently newbuilding orders have fallen, yet shipyards are still so busy that repairs are costly and often delayed. Exorbitant metal prices have also pushed up the cost of repairs. In order to avoid time off hire, repairs are being delayed and shipowners are keener than ever to eliminate accidents. However, the global crew shortage means it is difficult to ensure that crew are always experienced and well trained. This leads to an increase in accidents due to human error. Inevitably, the global crew shortage will be exacerbated by the launch of further newbuildings and the increase in the world fleet.

In order to fund newbuildings, shipping companies are looking at various finance options. In light of the U.S. sub-prime chaos, banks have limited lending but the tangible nature of shipping has resulted in it being a more favoured asset. Due to current market conditions, companies may no longer opt for public share issues. Recently, both Wah Kwong Maritime Transport Holdings and ZIM Integrated Shipping Services postponed IPOs in favour of alternative financing options because of the uncertainty and instability in the global capital markets.

Another economic factor to consider is the soaring price of oil; this has necessarily had a knock-on effect on the cost of bunker fuel. According to industry sources, bunker prices have tripled within the last three years and bunkers now constitute nearly half of total vessel costs, thus seriously eroding the profit margins of shipping companies and increasing pressure to cut other costs such as insurance premiums.

Overall the current market appears buoyant. However, the performance of the shipping sector is linked with the health of the global economy. Therefore, the rising price of oil and the threat of a global recession may lead to more careful consumer spending, an economic slow-down, and lower trade volume. This would result in decreased demand for tonnage. Nevertheless, in the face of the current demands of China and India, such a global downturn seems only a distant concern.

Hull rates

Shipowners are benefiting from relatively ‘flat’ insurance rates, with ‘as expiry’ premium levels common. Some fleets and accounts with good records have been achieving improved terms by means of enhanced performance related continuity credits.

Owners always have the option of switching insurers, especially as there is plenty of capacity in the market for all but the very highly valued cruise ships. Those who do seek alternatives to their incumbent insurer can sometimes secure significant savings as underwriters find it easier to assess new business, rather than reward existing clients with better terms, irrespective of their relative merits.

Inevitably, one of the outcomes of inadequate premiums is that all claims are heavily scrutinised. In addition, the current high values of vessels mean that underwriters’ exposures have grown. According to CEFOR, the average claim per vessel has doubled since 2003. Within some underwriting organisations large claims have to be referred upwards by the underwriter which at best causes delay and at worst can mean that a claim is
contested for commercial rather than technical reasons. This makes the selection of leaders vitally important.

The increases in vessel values require additional premiums. However, this higher exposure has until recently been purchased by owners very cheaply. Now underwriters are trying to achieve more proportional adjustments to ensure they receive an appropriate level of premium for the increased risk.

Since the beginning of 2008, there has been a divergence in underwriters’ behaviour: all aspire to higher premiums but only some are insistent upon them.

The hardening market trend is predominantly being led by mono-line marine hull underwriters. These underwriters are under particularly intense pressure and are therefore desperate to increase rates. In contrast, the composite syndicates in Lloyd’s seem to be under less strain.

A number of the leading Lloyd’s and Company underwriters, led by Simon Stonehouse, Joint Hull Chairman and hull underwriter from the Brit Syndicate have publicly made speeches calling for increased deductibles, but the market has never done exactly as it is told!

So far, rates have remained low and the market has remained stable. However, it is likely that over the coming year the market will begin to harden especially for those with less than immaculate records.

**Underwriting markets**

**Norwegian Hull Club** has led the charge for increased premium by trying to impose increases on all Hull business. In order to push this through, they have been prepared to lose 35% of their book, albeit not their core favoured domestic clients.

**Gard** has followed suit but to a lesser extent and are being very selective on new business.

**Bluewater** has had very disappointing results and this has led to the rating agencies downgrading their security.

**The Swedish Hull Club** has pushed for increases on all business. They have issued a report focusing on increased repair costs and claims levels, and have contrasted this with the low level of premiums. This is the justification behind their argument for the need for premium increases. Furthermore, the Club are not currently interested in pursuing new clients.

**Thomas Miller** has withdrawn its hull vehicle DEX from the market and the current portfolio will be handled by Groupama Transport who are already the capital providers for DEX.

**MSMI** have had a difficult year from a claims perspective. As a consequence, they have been requesting premium increases from their members. In general, the members have been willing to accommodate such requests in light of the specialist service provided.

**The London Market** has seen very little new capacity apart from Wurttemburgische being re-launched in Lloyd’s as Antares Syndicate.

**Far Eastern** markets we would suggest have not fared well following their aggressive entry into international business, over the past three to four years, at very competitive premium levels. Hong Kong, Korea and Japan are not the force they were.

However, Singapore is a strong emerging market, where a number of operations have started up, many backed by Lloyd’s syndicates. This market can be very competitive on the right business particularly where there is any ‘local management’.
SUPERYACHTS
The expansion in the Superyacht industry has shown no sign of abating over the past 12 months. The builders’ order books are still full for the next four to five years, values are increasing and the ‘global credit crunch’ has not yet had any adverse effect, as seen in the graph below.

Due to the extremely good loss ratio enjoyed by the specialist insurers over the past five years or so, 2008 has so far seen many new markets wanting to write this business. The new markets with the most capacity include: Fortis, Norwegian Hull Club, Gard, Groupama and Axa. These insurers have joined the traditional ‘players’ such as Lead Yacht, Underwriting Risk Services and the GSC Syndicate in Lloyd’s.

The USD 10-30 million market is now extremely competitive and this has led to a significant softening of hull rates. We estimate that there has been a reduction of between 15% and 20% since this time last year. Rates have remained a little steadier for USD 30 million+ yachts.

Yacht management companies remain very influential and the major companies are now offering their owners the complete package including sales, charter, management (both yacht and financial), newbuild project management, crew hiring and firing and other services.

The issues which remain outstanding within the industry are the same as 12 months ago, only now they have been exacerbated by the increased demand. There is a severe shortage of good crew: it is easy to understand why this is a growing problem when the new larger Superyachts require over 100 crew. Build times are another problem, as they are increasing due to the very high demands and expectations of owners. There is a limited number of berths, particularly in the Mediterranean. Other problems the industry faces include environmental issues, such as the type of paint used.

As previously mentioned, so far the global economic slowdown has not yet impacted the Superyacht market. However, it is likely that at some point there will be a knock-on effect, not at the very top end of the market but in the USD 5-10 million range. The charter market may also begin to suffer.
PROTECTION AND INDEMNITY
**Background - Renewal at February 20, 2008**

The background to the 2008 Protection and Indemnity (P&I) renewal was fairly bleak.

The Pool claims record for the 2006/07 policy year was the worst ever. The 2007/08 year was still undeveloped but all the signs indicated it was heading towards a similar level.

Retained claims performance showed some variance between Clubs, but largely mirrored the adverse Pool development.

Adding to these underwriting problems, the investment climate in 2007/08 was also extremely uncertain. In the previous year exceptional investment income results had offset the record underwriting deficits, in 2007/08 however a more marginal contribution from investment income was expected.

The above factors led to a range of General Increases being announced, averaging at the highest level for five years (+16.15% + International Group reinsurance adjustments).

**‘Cash Was King’ – Negotiation of Renewal at February 20, 2008**

The renewal discussions themselves were uncharacteristically confrontational.

It was clear that the underwriters’ need to obtain premium increases conflicted with the ship operators’ need to limit further increases to their cost base. These contradictory forces lead to the most adversarial renewal negotiations for over 10 years.

This may seem surprising as the general increases announced were materially lower than in the early 1990s and 2000s. The adverse claims development was evident, and it was obvious that the underwriting deficits were unsustainable in a mutual market. However, while acknowledging this, ship operators were faced with increasing costs in all areas (bunkers, crew wages, maintenance, dry-docking etc.) and so naturally fought hard to mitigate any premium rises for their fleets.

The combination of these issues led to delayed renewal offers and generally a much later conclusion of negotiations than normal.

The other key trait of the 2008 renewal was that for the Clubs ‘cash was king’. It was clear that securing premium increases was the fundamental consideration across the market. Clubs resisted entering into debates about deductible structures. As a result, there was little value offered in terms of premium savings in exchange for increased retentions.

Our estimate of the actual premium increase pushed through by the market was between 13% and 14% on mutual P&I. Within this average figure, possibly because of the style of the renewal, there was a notably wider range of individual results depending on fleet, record and Club than would normally be expected.

In contrast, Fixed Premium P&I, Charterers Liability, Energy Related P&I and Freight Demurrage and Defence areas of business were far more stable. If increased at all it was only by ‘inflationary’ rises.

**Winners and Losers – Renewal at February 20, 2008**

As ever, immediately post-renewal, there is an almost obsessive analysis of tonnage movements between Clubs. In a mutual environment this is not necessarily the best measure of performance, but it is a tangible benchmark.

February 2008 saw slightly more movement between Clubs than normal. In total, more than seventy fleets were involved in some sort of tonnage redistribution, but in the majority of cases these were only partial movements of tonnage and/or consolidations of fleets.
The North of England and Standard Club topped the tables for the number of winning fleet movements.

At the other end of the table, perhaps as expected, the American Club and West of England experienced net losses. Rather more unusually these Clubs were in good company, with Britannia and the Shipowners’ Club who would normally be towards the top of the table, also losing tonnage.

The Gard was notable for making good gains, but also for losing one of their biggest premium contributors (RCCL).

It is too simplistic to view the above as the financial winners and losers in the market. Only time will tell whether the tonnage movements were wise or not.

For example, it is arguable that Britannia’s hard line on their large general increase may well leave them better placed financially than a number of their competitors going forward, although it lost them tonnage at this renewal.

Similarly, those Clubs which rapidly increased in size must exercise caution in order to ensure that their financial strength grows by at least the same rate.

Changes in International Group Reinsurance – Renewal at 20 February 2008

As expected there were no material changes to the Retentions or Structure of the International Group (IG) reinsurance programme at 20 February 2008.

The key issue for the reinsurance renewal was also cost.

Despite a relatively flat reinsurance market, the reinsurance rates were increased by an average of 9.77% and all types of ships were impacted. The largest percentage increase was on dry cargo ships (+12.65%), dirty tankers faced the smallest percentage increase (+7.4%) while clean tankers and passenger ships increased by 9.76% and 9.27% respectively.

Even though when translated to direct premiums the reinsurance increases were relatively modest (average direct premiums increased between 1% and 2%) they came towards the end of a challenging season. The increases were therefore perceived as an unexpected ‘sting in the tail’ of an already difficult renewal.

As implied above, the driving factor behind the reinsurance increases was not the reinsurance market itself but the requirement to address the losses of the International Group Captive (Hydra).

Hydra reinsures each Club’s share of the upper Pooling layer (USD 20 million excess of USD 30 million), together with each Club’s 25% share of the first layer of the IG’s reinsurance programme (USD 500 million excess of USD 50 million). Unlike the costs of the IG Pool itself, Hydra is funded by a proportion of the IG reinsurance premium allocated to each vessel.

The surge in large claims in 2006 would have effectively wiped out Hydra’s reserves: the projected total claims cost on Hydra for the 2005 and 2006 years combined was USD 162 million, whereas net premiums into Hydra totalled USD 119 million.

In order to avoid potential insolvency, an unplanned refinancing was effected in April 2007 through a USD 50 million capital call shared across all the IG Clubs. This refinanced the captive, but did not prepare it for the continuing high claims levels as experienced in 2006. With similar claims levels developing in 2007, the decision was taken to increase annual premiums into Hydra from February 20, 2008. This had the obvious knock on effect of increasing the IG reinsurance rates per vessel.

One of the very few ‘bright spots’ in the reinsurance results was the reduction in U.S. Voyage Additional Premiums (-10%).

The impact on the reinsurance cost by type of vessel is outlined overleaf.
The following graph shows the progression in U.S. Voyage Additional Premiums.

**IG Reinsurance – Cost Changes by Vessel Type**

![Graph showing cost changes by vessel type over time]

**IG Reinsurance – U.S. Voyage Additional Premiums – Cost Changes**

![Graph showing U.S. voyage additional premiums over time]

Vessels with SBT
Vessels without SBT
2007/08 Financial Results

At the time of writing, all of the 13 IG Clubs have provided at least some form of initial indications of their 2007/08 financial year results, pending publication of their full Reports and Accounts later in the year.

These early ‘tasters’ from the Clubs provide only the briefest summary of the financial highlights, but they are not entirely useless. Of the 13 Clubs, seven have indicated that they will report overall surpluses (including investment income) for the 2007/08 financial year, while the remaining six have suggested that they suffered overall deficits.

Widespread underwriting deficits remain, but in most cases investment income results do not look as dire as some feared.

A full analysis of the actual financial results of all the Clubs will be included in the Willis P&I Review later in the year when all of the Clubs have actually published their Reports and Accounts and the initial indications can be double checked.

In the meantime the graph below outlines the provisional overall results released by the Clubs prior to release of their formal Accounts.

As mentioned above, seven of the Clubs are expected to report overall surpluses for the 2007/08 financial year. Of these only two (Skuld and Steamship) are expected to show even modest underwriting surpluses. For the remaining five (American, Gard, Japan, North of England and Standard) investment income was sufficient to compensate for underwriting losses.

The six Clubs expected to report overall deficits (Britannia, London, Shipowners, Swedish, U.K. Club and West of England) either experienced extremely adverse underwriting results or very low investment income (or a combination of both).

As continually emphasised by Willis publications, there continues to be a material variance between the best and worst performing Clubs in the market.

The above summary of results is obviously not the whole story and overall surpluses/deficits for a single year are easy to misinterpret.

Clubs are of differing sizes and financial strength to start with. In terms of percentage increase or decrease in Free Reserves, the Steamship represents the best performing Club in 2007/08 (nearly an 18% increase) whereas the worst performing is the London Club (27% reduction).
The London Club’s woes stemmed from a USD 30 million underwriting deficit combined with a terrible investment result (almost no investment income).

The Steamship also had a reduced investment result (but still managed a 4% return). Their small technical surplus resulting largely from a combination of increased premiums and reduced back years’ claims. The Steamship’s entire investment result therefore contributed directly to the Club’s Free Reserves.

The scale of Britannia’s overall deficit is also slightly misleading. Britannia (unlike the majority of the market) does not include their 2007/08 budgeted deferred call in their reported figures. If the full deferred call for 2007/08 was made this would represent an additional contribution of USD 45 million. Thus, if Britannia reported as other Clubs and in line with the market norm their USD 32.5 million deficit would be eradicated.

The Gard surplus mentioned in the graph relates solely to the P&I class of the ‘Gard Group’ (i.e. it excludes the Gard Marine and Energy classes).

**IG Market – Financial Summary**

In the Willis 2007/08 P&I Review we suggested that a 6% return on investment would be sufficient to offset a similar underwriting deficit to 2006/07. Feedback from the Clubs following February, 20 indicates that, on average, investment income may well be close to this level of return. The combined market result is therefore likely to achieve close to (though probably marginally below) an overall break even position.

The Willis 2008/09 P&I Review will include a more complete analysis of the Clubs’ positions, but initial results suggest:

- The 2007/08 claims are at a similar high level to 2006/07 (though there are some variances in the development of back years’ claims).
- The investment income is reduced, but is by no means as disastrous as many feared.
- There is variation in individual Club results, but the International Group combined is probably going to show a very marginal deficit overall.

Our estimate of the projected overall market result is outlined in the graph overleaf.
Looking Forward

It is still very early in the 2008/09 policy year and predictions about claims and investment income at this stage can only be tentative.

In the last Willis P&I Review we stressed that the overriding characteristic of the pattern of large P&I claims is their volatility. As if to underline this, so far in 2008, Pool claims appear to be strangely absent. By mid-July not a single Pool claim had been reported in the current policy year. At the same point last year, the market was already aware of twelve Pool claims. This lack of very large claims is highly unlikely to persist. All the factors driving the increase in major claims continue to be present and inevitably the current hiatus will not last.

This anomaly serves to emphasise the difficulty in predicting the pattern of large claims in the current market.

By contrast, all indications suggest that retained claims continue to be following the upward trend of the last two years. Barring another unexpected material ‘step up’ in claims levels, the increases in premium at the 2008 renewal will have gone some considerable way towards eroding the underwriting deficits across the market.

In terms of looking forward, the real ‘wild card’ will be investment income. We expected last year to be difficult, but the global economic challenges in 2008 make the investment climate in 2007 look positively benign.

As highlighted earlier, all Clubs are not equal and the discrepancy between them is expected to become more marked in the run-up to the renewal in 2009.

It is likely that the general increases announced before the 2009 renewal will be lower than 2008. We expect however that the average will still be over 10%. Similarly we anticipate that the variation in the range of published increases between the strongest and weakest Clubs will be more pronounced.

As mentioned following publication of all the Clubs’ Reports and Accounts later in 2008, the Willis P&I Review will analyse the financial results in more detail. With more solid information at that stage, it should enable more accurate comments on future trends. The full Willis P&I Review will also provide an update on the key market issues.
LIABILITIES
In the Lloyd’s Annual underwriter Survey (February 2008) the key issue for the industry in 2008, as identified by the sample of underwriters who responded, was ‘Managing The Insurance Cycle’.

This issue is particularly relevant for the Marine Liability market, where underwriters are keen to ensure that the current downturn in premiums and rates does not develop into a collapse.

Marine Liability business has historically been a favoured class for underwriters, having delivered solid profit levels over the past decade or so.

### Marine Liabilities Loss Ratios

<table>
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<tr>
<th>YEAR</th>
<th>PERCENTAGE</th>
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<tbody>
<tr>
<td>1997</td>
<td>49.40%</td>
</tr>
<tr>
<td>1998</td>
<td>70.22%</td>
</tr>
<tr>
<td>1999</td>
<td>87.22%</td>
</tr>
<tr>
<td>2000</td>
<td>60.89%</td>
</tr>
<tr>
<td>2001</td>
<td>82.75%</td>
</tr>
<tr>
<td>2002</td>
<td>34.75%</td>
</tr>
<tr>
<td>2003</td>
<td>41.34%</td>
</tr>
<tr>
<td>2004</td>
<td>73.64%</td>
</tr>
<tr>
<td>2005</td>
<td>26.52%</td>
</tr>
<tr>
<td>2006</td>
<td>41.78%</td>
</tr>
<tr>
<td>2007</td>
<td>45.36%</td>
</tr>
</tbody>
</table>

Source: Lloyd’s Audit Code ‘G.

Underwriters in this sector had, up to mid-2007, been able to maintain a degree of rating discipline with small reductions being offered on some accounts.

However, during the second half of 2007 increased competition between underwriters, additional market capacity and pressure from assureds enabled brokers to obtain larger reductions on accounts which underwriters had considered to be adequately rated and profitable.

During the January 2008 renewal season, the average reduction being offered was in the region of 10% and there has certainly been an increase in the use of other incentives such as profit and continuity commissions, prompt payment discounts and long term deals (frequently subject to an annual review clause). Also premium savings are often achievable where different types of coverage are packaged together – an example would be where liability coverage is placed under one policy together with physical damage and business interruption insurance.

Underwriters have been able to maintain prices on some accounts where specialist coverage is being offered or where minimum premium levels apply. However, on other large premium income accounts much greater reductions have been achieved where significant reserves of ‘clean’ premium have been generated over a number of years and where there is now pressure to achieve premium savings.

It is difficult to see the current situation changing before the end of 2008 and therefore it is likely that rates will continue to fall up to the end of the year – unless the current soft market is halted as a result of a lack of capacity or by exceptional claim events.

It is clear that concerns relating to the issue of Environmental Pollution coverage are increasing in the minds of both underwriters and assureds. With this new focus on environmental issues, the adequacy of current limits and coverage needs to be carefully considered.

The Lloyd’s Survey also identified ‘Increasing Competition From Other Insurance Centres’ as being a major issue for underwriters in London. It is certainly the case that overseas and local markets are competing on a more regular basis on facultative Marine Liability business that would traditionally have been placed in the London market.

To counter this problem, a number of Lloyd’s syndicates and companies have set up their own separate underwriting centres away from the London market.
which are intended to attract domestic business and are able to provide local servicing. Singapore currently appears to be a favourite location – an example of this is Mark Trevitt of Travelers, who moved in late 2007 from London to Singapore to write a book of Marine Liability/Ports business.

The underwriter merry-go-round has continued into 2008 with one of the most high profile moves being Stephen Barr’s departure from Talbot Syndicate to start underwriting a new book of Marine Liability business at Marketform Syndicate.

It is clear that managing the insurance cycle will be the main challenge for the Marine Liability market in 2008 – as 67% of Lloyd’s underwriters believe that insufficient progress was made during 2007 in this respect. If Marine Liability rates and premiums continue to fall at the current rate during the second half of 2008 and into 2009, then this sector may well be in danger of losing its favoured status.
CARGO
Market Overview and Trends

In the 2007 Marine Review, we reported that the cargo market was experiencing unprecedented rate reductions due to increasing capacity and competition.

In 2008, there has been a continuation of the softening market, with no apparent end in sight. Cargo owners can now obtain wider coverage, reduced deductibles and higher limits – at the same or even lower premiums than in 2007.

Fuelled by a weak U.S. Dollar, commodity prices and world trade volumes continue to rise. However, from a cargo market perspective, we have seen a 20% reduction in gross cargo premiums since 2002, against a 25% increase in world trade volumes.

Despite the falling premiums, cargo insurance is still showing profitable results for insurers. We detail below the 10 largest cargo losses advised to Lloyd’s of London for the period April 1, 2007 to March 31, 2008. While this only includes claims where Lloyd’s of London participate on the account, it highlights the fact that there have been no losses which would impact the market as a whole:

<table>
<thead>
<tr>
<th>TYPE OF LOSS</th>
<th>LOCATION</th>
<th>AMOUNT (USD)</th>
</tr>
</thead>
<tbody>
<tr>
<td>GA AND SALVAGE FOR COPPER AFTER VESSEL GROUNDED</td>
<td>CHILE - INDIA</td>
<td>30,000,000</td>
</tr>
<tr>
<td>VESSEL SANK CARRYING STEEL PRODUCTS</td>
<td>XINGANG - IRAN</td>
<td>29,800,000</td>
</tr>
<tr>
<td>JACK-UP RIG GROUNDED WHILST TOWED</td>
<td>USA - ANGOLA</td>
<td>10,000,000</td>
</tr>
<tr>
<td>STEEL BARS MISSING FROM WAREHOUSE</td>
<td>RUSSIA</td>
<td>9,000,000 +</td>
</tr>
<tr>
<td>HURRICANE DAMAGE TO WIND TURBINES</td>
<td>TEXAS</td>
<td>8,750,000</td>
</tr>
<tr>
<td>SHORTAGE OF OIL FROM RAILCARS</td>
<td>KAZAKHSTAN</td>
<td>8,600,000</td>
</tr>
<tr>
<td>RISER PIPES LOST OVERBOARD IN HEAVY WEATHER</td>
<td>USA - KOREA</td>
<td>6,900,000</td>
</tr>
<tr>
<td>CONSTRUCTIVE TOTAL LOSS AS ADVENTURE LOST</td>
<td>TAIWAN - RUSSIA</td>
<td>6,100,000</td>
</tr>
<tr>
<td>THEFT OF COPPER BETWEEN MINE &amp; PORT</td>
<td>TANZANIA</td>
<td>5,700,000</td>
</tr>
<tr>
<td>TOTAL LOSS OF GASOLINE FOLLOWING LIGHTNING STRIKE</td>
<td>SOUTH AFRICA</td>
<td>5,600,000</td>
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The above, together with the lack of any significant losses due to natural catastrophes has done little to dent the market’s confidence. Even the recent hail loss affecting Volkswagen and Porsche vehicles in Emden, Germany, is expected to have little or no impact on the marketplace.

Despite being estimated to be in excess of USD 110 million, the loss is shared amongst a number of continental insurers with no involvement of other markets writing cargo accounts. The fact that such large exposures can be written by a small number of insurers means that even substantial losses only affect small pockets of the global marketplace, therefore doing nothing to reverse the downward trend.

The most notable development that these losses demonstrate is the effect that increasing commodity prices are having on underwriters’ exposures. The largest loss was a General Average claim for USD 30 million – with little damage to the cargo itself!

In an effort to maintain their premium income from cargo business, underwriters have broadened the scope of products on offer. Stock Throughputs have continued to prove popular, with the boundaries being pushed even to include additional risks such as retail exposures.

Package arrangements are becoming more popular, with cover for business interruption, working equipment, trade disruption, hull, CEND and charterers liability being added to basic cargo policies.
While many of the new entrants into the market struggled to meet their premium income expectations in 2007, the Asian cargo market remains healthy and profitable for most underwriters. Combined with the regional company underwriters such as AIG, Allianz, Asia Capital Re, Ace, Chubb, Federal, Groupama, Liberty, QBE and RSA, we estimate that the capacity of the Singaporean cargo market is now between USD 250 million and USD 300 million.

**The marketplace**

**U.S.**
Capacity continues to grow in the U.S. market. However, there have been no significant new entrants over the past six months which perhaps suggests that the appetite of capital providers has reached a plateau.

**Asia**
George Street Singapore has become the home of Lloyd’s syndicates in Asia. Amlin is one of the most recent entrants into the Singapore cargo market with the following syndicates now actively writing cargo in the region:

<table>
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<tr>
<th>SYNDICATE</th>
<th>SINGAPORE</th>
<th>HONG KONG</th>
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<tr>
<td>WATKINS SYNDICATE</td>
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<tr>
<td>KILN MARINE SINGAPORE</td>
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<td>SYNDICATE 1965</td>
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<td>CATLIN SYNDICATE</td>
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<td>ALBA SYNDICATE</td>
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<td>ASCOT UNDERWRITING</td>
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<tr>
<td>CHAUCER SINGAPORE</td>
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<tr>
<td>TALBOT ASIA</td>
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<td>TRAVELLERS ASIA</td>
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<td>AMLIN</td>
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<tr>
<td>CV STARR</td>
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Domestic underwriters are widening the scope of their coverage to try and recapture business being placed overseas. As a reaction to the popularity of Stock Throughput policies, property insurers are seeking to include inland marine in their coverage along with import and export.

During the past 12 months the U.S. market has been offering 50-60% reductions on selected accounts in an attempt to win them back from overseas markets.

The Council of Insurance Agents and Brokers report that insurance premiums declined by an average of 13.5% during the first quarter of 2008, following a fourth quarter decline of 12% in 2007. The major broking houses offer no sign that the market cycle is ready to turn.

Willis International Trade and Logistics are ideally positioned to take advantage of the opportunities presented by the current market and are at the forefront of innovative program design.

The move to globalise the cargo market is accelerating, with underwriters transferring capacity away from London in an effort to maximise their involvement with vibrant domestic markets. This has resulted in the formation of regional underwriting hubs in Asia, Europe, Latin America (Miami) and the Middle East.

In light of the above and the perceived profitability of cargo business, it is no wonder that we see cargo underwriting capacity growing worldwide, creating a fiercely competitive market and some of the lowest cargo premiums on record.
So far 2008 has seen a continuation in the movement of personnel. Notably, the transfer of Lee Vanderson, who underwrote the largest cargo book at Lloyd’s, to head up Reith Singapore, underlines that Syndicate’s commitment to Asia.

In 2007, 20-25% reductions in rates were commonplace, but obviously this simply cannot continue indefinitely. Already 2008 has seen more moderate reductions of 10-15%, although bigger reductions remain available for the larger accounts.

Middle East
The transfer of capacity to the Middle East is creating yet another regional underwriting hub.

Although still in the early stages of growth, the marketplace is developing, unsurprisingly with a strong focus on oil and construction risks.

The market is still strongly regulated and brokers have only recently gained admission.

No particular country has so far emerged as the front runner and currently the market is spread between Bahrain, Dubai and Oman. The market is dominated by insurance companies but the role of Lloyd’s is expanding. There is no reason why we should not expect a repeat of the Asia experience.

Europe
The larger European insurance carriers such as AXA, Allianz and XL have begun to centralise the underwriting of international cargo business, either back to their European head offices or, in the case of Allianz to London.

Several of the U.K. insurers see potential for further growth in Europe, especially in light of over-capacity in the home market.

RSA have commenced a strategy of developing marine cargo-specific operations in Belgium, France, Germany and the Netherlands and further expansion is planned.

Starr Marine have employed Simon Plumridge from AIG to manage their expansion in Europe and already they have secured the services of Serge Vanderstappen and Michael Zanetti as European managers.

From a rating perspective, larger European carriers have become increasingly competitive and have won several global accounts from the London market.

The large composite companies still have the advantage over Lloyd’s when it comes to packaging risks and offering truly global programs. This will no doubt change soon given the competitive nature of the market and the appetite of Lloyd’s for new sources of income.

London
With the growing strength of domestic markets and competition for international accounts from both regional hubs and the continental market, London is going through a period of dramatic change.

Insurers and brokers alike, are looking to position themselves to meet the challenges of the rapidly changing marketplace, whilst maintaining their budgeted expectations for growth and profitability.

London is increasingly moving away from the smaller transactional risks and focusing on its strengths of global experience, expert knowledge on key industries such as automotive, construction, pharmaceutical, metals and oils and a focus on high risk and capacity exposures.

 Whilst the domestic and regional markets are strong on transactional accounts, they still cannot match the depth of experience that London provides on complex and problematical accounts.

The subscription market provides clients with a large amount of capacity, with
underwriters sharing accounts that insurers would not be prepared to accept on a 100% basis.

However, London insurers realise they can no longer sit at their boxes and wait for accounts to be shown to them and are increasingly being pro-active in developing direct relationships with the assureds and working on a partnership rather than transactional basis. Risk management and loss prevention services are now offered by a large number of insurers and are seen as an integral part of the value-added product now being offered.

This drive to improve the service given to clients and the increasing competition to grow premium income has seen another year of changes to the landscape of the London cargo market.

AIG have completed their takeover of Reith and whilst not officially announced, there are three new insurers looking to start cargo underwriting before the end of 2008. The transfer of personnel between brokers and underwriters continues at a rapid pace, with perhaps the most notable move being that of David Roe, previously head of cargo at Marsh London, leaving to join Ascot following the transfer of Lee Vanderson to Singapore.

Other changes include Huw Davies moving from Marsh to O’Farrell, Helen Steadman moving from Marsh to Mitsui, Richard Golder from Amlin to Catlin, Tim Garrett from AIG to Beazely, Andrew Thorp from AIG to CV Starr, Allan Brooks from CNA to Zurich, Johnathon Eaton from Aon to AIG.

In summary, there can be no better time for cargo owners to take advantage of the high capacity, the broad coverage and the competitive pricing.

Our team at Willis is well positioned to take full advantage of the opportunities on offer in the global marketplace and has the expertise to deliver innovative products and solutions to our clients.
CLAIMS
Recent case law has again highlighted the importance of warranties, both to assureds and insurers. Our own claims expert outlines the issues and developments concerning warranties and the law that surrounds them in the following article:

Warranties: They do what they say on the tin!

In recent years there has been much debate about the role of insurance warranties under English and Scottish law. For many years, there has been wide consensus within the insurance community that English Insurance Law may be in need of reform and the impact of warranties is central to these proposals.

Warranties as originally conceived, under common law, were promises made by the insured to insurers to guarantee that the risk had been accurately described to them. The use of warranties in Marine Insurance has moved far from this original concept. A good example of this would be a premium warranty that requires premium to be paid on or before a certain date: this has no connection to the risk underwritten.

The Marine Insurance Act 1906 characterises a warranty as a condition which must be exactly complied with, whether it be material to the risk or not. The remedy for a breach of warranty is severe and again defined within the 1906 Act as “…the insurer is discharged from liability, as from the date of the breach of warranty”.

It is imperative that a warranty is compatible with the operation of the vessel and that the consequences of non-compliance are clearly understood by the assured. The breach does not have to be material to, or causative of, the loss. Two recent cases to pass through the English courts highlight the pitfalls.

Firstly, G.E. Frankona Reinsurance Limited -v- CMM Trust No.1400 - “The Newfoundland Explorer” [2006]. The Claimant was a Yacht owner, whose USD 3 million yacht caught fire due to an overheating generator while safely moored at a marina in Fort Lauderdale. The Owner was at home 15 miles away and the rest of the crew dismissed as the yacht was laid up. The marine policy contained an express warranty: “warranted fully crewed at all times”. The claim was denied by the insurers on the basis that the warranty was breached. The courts held that the yacht owner was to keep at least one crew member on board the vessel 24 hours a day (barring one or two emergency situations that would allow the craft to be unmanned).

Secondly, Pratt v Aigaion Insurance Company SA (The “Resolute”) [March 2008]. Pratt, the claimant, was a trawler owner, who returned from a day’s fishing to North Shields, U.K., safely moored, discharged her catch and the crew readied the vessel for the following day’s fishing. The Owner/Master and crew then made the craft secure and left to meet family or partake in a well-earned drink. During the evening a fire was reported on the vessel, investigations concluded that it was caused by a faulty deep fat fryer or fridge. The insurers declined the claim on the basis of a breach of an express warranty: “warranted Owner and/or Owner’s experienced Skipper on board and in charge at all times and one experienced crew member.” The claimants argued strongly, that it was obvious that the warranty was directed to periods of navigation and, if applied literally, would be absurd compared to the accepted practice in the trawler industry as the Skipper and one other crew member would have to permanently reside in a crew cabin measuring 6ft by 9ft.

The Court held that there was no ambiguity to the warranty, “on board…at all times” meant “at all times” 24 hours a day, 365 days a year regardless of the impracticalities of the Owner/Skipper actually strictly complying with the warranty. Accordingly, the claim failed.
It can be seen from these two legal examples above that English law may be in need of review. Most other jurisdictions have accepted, to varying degrees, that there must be a clear link between the breach of warranty and the cause of the loss for insurers to rely solely on a breach of warranty to deny liability.

In July 2007, the Law Commission of England and Wales issued a consultation paper that dealt with, amongst other matters, warranties within consumer insurance. The paper sought responses from consumer groups, lawyers, brokers and insurers. At the end of May this year, the Commission published a summary of responses. These concluded that the Commission’s proposals had little effect on consumer insurance but would have a significant effect on business insurance and particularly marine insurance, requiring the more extreme provisions of the Marine Insurance Act to be repealed.

It is now planned for the Law Commission to produce a further consultation paper on commercial/business insurance warranty reform. These proposals are therefore unlikely to come before Parliament for a further three to four years.

A Classification Warranty is a more common express warranty on a policy of marine insurance; this requires a vessel to be fully classed and class maintained during the entire policy period. Classification is a continuous process and failure to meet survey dates or requirements will result in a vessel losing class status. There can often be an innocent explanation for missing an inspection and the situation may be speedily resolved. However, the delay in survey may lead to a break in the continuity of the vessel’s class record enabling a technical breach of the warranty. Insurers would then be entitled to discharge themselves of any future liability under the policy after the date of the breach. In these circumstances it is essential for insurers to be advised immediately and obtain agreement from them that cover is continued.

Until the law is reformed, assureds should remain fully aware of the implied and express warranties in their policies, ensuring that they are clear, sensible, workable and relevant. The consequences of non-compliance should be fully understood and suitable processes employed to ensure that insurance cover remains complete.
Following the traumatic events of 2004 and 2005 in the Gulf of Mexico, Marine reinsurers have enjoyed two years without a major Marine-related multi-interest loss incident. For Marine catastrophe reinsurers, riding on high premiums inflated by payback for the hurricanes, 2006 and 2007 have been excellent performers.

By contrast there has been an abundance of small and medium-sized losses, which have affected reinsurers’ results to varying degrees, always depending on the level of the original insurer’s (i.e. the reassured’s) retention. Vessels are running to capacity, as are shipbuilding and shiprepair yards. Oil has never been more expensive, political situations and tensions are often unpredictable, and earthquake activity is much publicised in China, Japan, and Iceland (and in Market Rasen in the U.K.) These are all factors which are keeping insurers occupied and emphasising the need for insurance and reinsurance. The threat of a meaningful claim is ever present, especially as recent claims activity has been bubbling just below the (reinsurance) surface.

This contrasting claims picture has inevitably led to a range of expectations and pressures. The reassureds have paid substantial increases in the past few years to recompense the large losses (sometimes in spite of having little involvement in the losses themselves) and to satisfy reinsurers’ re-evaluation of the cost of catastrophe coverage. As profit margins are being squeezed by smaller claims, reassureds are seeking improved terms (in the form of meaningful premium/cost reductions). Their ambitions are often at odds with reinsurers’ approach: requests for hugely enhanced information, broad application of modelling tools, pressure for internal capital allocations, constant management, supervision, and control, and Solvency II are all creating a less sympathetic – perhaps somewhat more defensive – reinsurance market.

In general, at the beginning of 2008 there were premium reductions of about 5-7.5% for the larger multi-class programmes and, 10-15% for specific, local, indigenous accounts. These reductions were always subject to past claims experience and to the renewal information: there was little tolerance for a poorly performing lower Excess of Loss layer, which was eroding a major proportion of a programme’s profitability. Reinsurers are seeking a sensible retention level, as well as pricing, to ensure that the insurer (reassured) is not merely passing all or most of the liability to reinsurers.

As an example, pre-set monetary budgets, set in the latter half of 2007, were in some cases so optimistic that retentions had to be increased several fold to ensure that financial targets were met. The prevailing focus on performance for all classes is compelling Excess of Loss reinsurers to differentiate their interests, and therefore their underwriting, from the needs of their clients, the insurers. Hence, we see excellent reinsurance results (in so far as Marine reinsurance results are discernable within the accounts of multiline reinsurance companies), while the results of the Marine insurance business are often marginal at best.

Retrocessional coverage (retro) continues to be limited and expensive. Whereas retro may have once offered a trading advantage to its reinsuring clients, it is now purchased as a necessity, either for internal management requirements or for external balance sheet, and hence rating considerations. Likewise as the Energy reinsurance market softens, Gulf of Mexico coverage is being included to an ever greater degree – within Whole Account programmes. The number of Gulf of Mexico hurricane Energy specific protections are reducing – whether written on an orthodox or parametric/finite basis or as a sidecar.
Reinsurance prices are not reducing in line with the original business and the Whole Account or Limited General markets have become more tolerant.

The core focus for insurers in 2008 is the management of attritional losses. There are many enquiries for low-level protection and there is a distinct dearth of sympathetic or innocent reinsurance capacity. Rates and terms (specifically the level of annual aggregate deductibles) are being related to claims experience, risk exposure and current worldwide Marine conditions. A good example is Protection and Indemnity coverage, which has customarily been well supported at low levels (as a true thermometer of a genuinely wet Marine portfolio); the results have been indifferent in the recent past, as claims activity has increased markedly. It is increasingly apparent that reinsurers are seeking to maintain profitability and results are now a core focus at the expense of some long-term relationships.

For 2009 reinsurance will continue to react firmly to any deterioration in contract performance, any large loss and also to increased exposure (higher hull values and oil prices), but will continue, in the absence of a large Marine catastrophe loss, to come under pressure to reduce pricing. Reinsurers are certainly showing a firmer resolve and are likely to continue to do so.
Marine is inherently a global business from both a shipping and a cargo perspective. As a result of this, we have Marine Associates based all over the world. Several of our colleagues have contributed with Letters from their Region, giving us a snapshot of the local markets and current trends.
**Letter from New York**

Well, another year has passed and it is more of the same: rates very competitive, coverage being enhanced, new capacity entering the market and everyone fighting over the same business. All very positive for the assureds.

With rates so competitive one would have thought that it was not the right time for new capacity to enter the market. We have, as advised in last year’s review, had new capacity enter the market and rates became soft as they fought to establish their positions. These carriers have done an excellent job of solidifying their positions and are now firmly established.

This year we have three new entries into our marine market. The first is Max Specialty which is made up of a senior group who left the Firemen’s Fund and is headed up by Michael Miller. The second entry is Valiant Insurance which is lead by Joseph O’Connor and the third is Catlin Insurance U.S. with Vincent Liotta at the helm.

These entries complement each other as they are, at least in the initial stage, targeting different lines. Max Specialty is looking to the Inland Marine and Ocean Cargo placements, although they do have the capabilities to write Hull, P&I and Marine Liabilities. Valiant Insurance is concentrating on Hull, P&I and Marine Liabilities whereas they do have the capability to write Ocean Cargo. Catlin Insurance U.S. is looking to write all lines of marine business, excluding bluewater hull. Their aim is to target that business that stays in the U.S. and is not seen in London where Catlin is a major player in the marine market.

Major changes in management positions see Harry Yerkes joining the American Hull Syndicate as Chief Operating Officer, to take over from Fred Robertie when he retires later in the year. Raymond Stahl left Ace after many years to join AIG Global Marine to start up their recreation group. John Barnwell has now been made the National Cargo Manager at the Firemen’s Fund.

The year in general saw ocean cargo rates continuing to drop as competition for business grew, with rates dropping by up to 50% for those accounts which had not been re-marketed in recent years. Rates generally dropped 10-15% on top of the major reductions of recent years.

The U.S. Marine Liability market continues to remain stable. The first quarter of 2008 saw the majority of primary and excess policies renewed at the expiring premiums with rate reductions few and far between. The second quarter is starting to see some very minor reductions (5% or less) on premium accounts with clean loss records. The Marine Liability market tends to lag behind other marine markets in terms of rate fluctuations, due to the “long tail” nature of liability business.

Hull and Machinery rates vary with bluewater accounts renewing ‘as expiry’ or with minor reductions. Brown water accounts are seeing reductions in the range of 5-10%. However these percentages are discarded when the renewal is subject to a serious remarketing exercise: the account can be considered as new business and underwriters are aggressive when pricing those specific accounts they have targeted.

We do not know what the rest of the year will bring, but we have recently seen the U.S. Marine Liability market be very aggressive in taking an account which has been placed in the London market for several years.
Letter from Norway

We have the following active underwriters writing international hull business.

- Norwegian Hull Club
- Gard
- Codan
- Nemi
- Gerling
- Trygg Vesta
- Swedish Club
- Inter-hanover
- Markel, Stockholm

Norwegian Hull Club is leading the charge in their push for increases on marine hull business, and they have taken a tough line resulting in the loss of a number of accounts. We see ‘general increases’ from NHC in the region of 10-15% on accounts with good statistics.

Gard has gained a number of new claims lead positions as a result of NHC’s firm stance on increases. Gard’s growth is well founded and they appear to be in a strong position going forward. Unlike other Underwriters, Gard do not impose blanket general increases though they are seeking rises. Instead, Gard examine the fleet’s individual record before applying any increases.

Bluewater is struggling as it has been downgraded. Reports suggest that they will try to continue as an agency with a new carrier but this might be difficult.

Nemi has also encountered some difficulties. The rating agencies are concerned with the financial health of their ultimate parent company.

Codan has re-staffed their office in Bergen after many of their key employees left for Vega insurance last year. They have brought in Geir-Arne Heggeland from NHC as their General Manager and Geirmund Sangedal from Royal Sun as senior underwriter. Codan remains an important underwriter and they are considering further expansion.

Swedish Club has adopted a similar position to NHC, imposing increases on hull business. They are not as active in 2008 as they were last year and they are reviewing their strategies. They have just appointed a new Managing Director, which may lead to a change in underwriting policy.

Markel has opened an office in Stockholm with well known people such as Staffan Sahlin and Ove Staaf heading up the operation.

Vega is still not up and running although they hope to be operational by September. However, with the current difficulties in the capital markets, they may struggle to reach their target of USD 120 million. Already they have lost three employees, and more may follow if they are not operational soon.

In conclusion, the Scandinavian marine market continues to flourish, albeit with a determination to raise premiums sufficiently to meet increased claims.
Letter from Singapore

Tiger Tiger Burning Bright - View from a Topical Isle

Last year’s letter from Singapore focused on the steady stream of international interest and subsequent establishment of new marine ventures: from underwriters to brokers and P&I clubs to adjusters. The concern from the ‘old school’ underwriting fraternity here, that the new influx of ‘kids’ would drive the rates down, has now largely subsided. It happened and it was inevitable but it has dramatically improved the responsiveness and service levels of most underwriters.

There is an increasing appetite to lead business here. This was dramatically and very publically demonstrated when ACR took the lead from Gard on the massive Evergreen account. Also, it is reflected in the movement of key personnel: several main players have been transferred, often from Lloyd’s – enabling more important underwriting decisions to be made here.

So, now we are on the map and the recent Tradewinds Marine Risk Forum in May attracted a global mix of speakers. Strangely noticeable was the distinct lack of Lloyd’s Asia underwriting representation, especially given their appetite for marine business. London underwriters were well represented. Delegates from Brit and RSA eloquently unveiled a series of concerning statistics, challenging the current deductible and pricing levels, and the lack of qualified crew. The consensus was clear: if underwriters cannot force a change, they will become victims of their own policies.

However, one particular broker (struggling either with the heat or the local Tiger Beer) claimed despite his client’s atrocious figures he had successfully managed to negotiate a reduction that he openly described as “so ridiculous” that it was clearly “underwriting suicide” and he seemed genuinely perplexed as to what was going on. Could one argue brokers are simply becoming too good at driving the rates down or has underwriters’ hunger been to the detriment of their technical rating?

The continuing ‘high’ throughout the shipping industry is obviously boosting overall world tonnage but even though the premium base is increasing, Simon Stonehouse (of Brit Insurance and Chairman of the London market’s Joint Hull Committee) pointed out to the Tradewinds delegates that current insurance rates are 35% of what they were in 1994.

So it would seem that for now we do remain in a buyers’ market. This was especially pleasing for the local shipping community who were represented by MISC, NOL and PCL to name a few.

Simon Wilson, Managing Director of Lloyd’s Asia, is pleased with the growth of the market ‘hub’ here. The market has grown from three to fifteen syndicates in the last 18 months but Marine still only represents a small share of the overall premium base: 10% for cargo and 3% for hull. Wilson predicts there will be fewer new entrants into this market – only one further syndicate is currently in the pipeline for 2008/9. This trend clearly reflects the soft market and is likely to continue throughout 2009. Last year, Lloyd’s Asia’s gross received premiums topped USD 126 million. It is still too early to tell but 2007 figures are looking very healthy at present – around 10% loss ratio.

One of Wilson’s aims this year has been to promote the Lloyd’s brand and to attract a quality skill base into the market. We saw a successful road show in Kuala Lumpur recently which attracted all the major insurance companies and brokers. Many syndicates were represented with the purpose not only to promote the syndicates but also the Lloyd’s Asia market as a whole.

Working with GIS, insurance companies, and brokers, Lloyd’s Asia is heavily promoting local graduates into the industry with the hope of creating future foundations. Although Lloyd’s syndicates have been criticised in the past for raising local salaries, this initiative will hopefully make insurance a more attractive career proposition in the future.
Wilson feels the key to success in this market will be in its ability to mature into a fully independent hub. In general, Singapore is not particularly claims efficient. Therefore, claims leadership and efficient servicing is key to the market’s success. With only two of the current syndicates having dedicated marine claims directors, there is clearly room for improvement.

As mentioned above, the biggest impact on the effectiveness of Lloyd’s Asia, seems to have been the arrival of genuine market leaders who have the ability and authority to lead business. The arrival of established names such as Chris Wilde (Chaucer), Mark Trevitt (Travelers) and recently Lee Vanderson (Ascot) are likely to further enhance the Asia position.

Trevitt is the first dedicated Marine Liability underwriter at Lloyds and recently AIG appointed Catherine Mangan as Vice President for Regional Marine Liability. Trevitt feels that while other classes have established themselves, this is largely as a result of a similar build up on the broking side. He believes that the marine liabilities market has the biggest potential in the region with an estimated USD 750 million of Asia Pacific liability business available and currently very little is written here. By 2013 China will have 6 of the 10 largest ports in the world. Closer to home, Malaysia’s increasing port infrastructure will give Singapore a run for its money.

The players outside Lloyd’s who have traditionally written marine liabilities here such as AIG, Swiss Re, Munich Re and QBE are now joined by the likes of Watkins, Catlin, Ascot and Talbot who are predominantly writing as following markets.

Currently the market capacity is estimated at USD 150 million locally with net loss ratios at about 45%. While Trevitt feels there is regional competition from the likes of the TT Club in Hong Kong and ACE in Australia, the success of the markets here will depend on the support and build up of dedicated regional brokers specialising in the sector.

Last year’s feeling was that the cargo market could not fall any lower. Ever increasing demand for higher limits have continued to force rates down further.

Lee Vanderson of Ascot is bullish in his attitude that Ascot will increase their cargo book here by a further 30% in 2008, despite the current position in the cycle. Cargo represents 30% of his overall book here and he is keen to expand other marine lines. Particularly sceptical that Indian oil cargoes will remain at their current levels, he sees major opportunities in the Chinese market. Vanderson predicts that rates are going to get thinner, even though there is little meat on the bone to sustain a claim, let alone a pack of hungry underwriters it needs to feed.

The General Insurance Association’s (GIA) total premium income statistics for cargo have remained worryingly stagnant for the last four years. The vastly increased throughput, oil, steel and other commodity prices have in part hidden these percentage reductions. It certainly seems that buyers will continue to gain from attractive rates in 2009, albeit lower in percentage terms than the last 12 months. Statistically cargo figures prove it is still a profitable account given a gross loss ratio here of only 25% for 2007.

Marine construction rates remain competitive although there have been several losses in the region. There was notably a spate of launch problems in Vietnam but most of these losses have been picked up in the treaty markets and had little effect on facultative rates. Probably we are at the bottom of the cycle but we will have to wait for a major loss before yards need to worry about increases.

The Hull and Machinery account, as predicted last year, has continued to soften. A few 25% reductions at the start of the year did not become the norm. On average, Jonathan Ranger of Watkins Syndicate says, he has seen rates slide
between 10% and 12.5% in 2008. Yet, he notes that over June and July the trend has seen signs of changing, where several offers for regional facultative RI have gone unsupported.

GIA statistics for hull and machinery also show premiums down by 12.5% and gross loss ratios for 2007 at 43%, so on a net basis the class is marginal. The clear push from some European markets, especially Norway, to increase rates is likely to spread East eventually. However, while loss levels remain low and capacity is stable, our advice would be to negotiate hard now and lock in as far as possible because a hardening hull market in Asia is almost within sight.

A note from Hong Kong

The insurance market in Asia continues to grow in line with the ever increasing volume of trade coupled with the thirst of China, particularly in the shipbuilding sector. Arguably Hong Kong has missed out on this growth as Lloyd’s hubs have established themselves in Singapore and more recently Shanghai. However, Hong Kong remains well positioned to service the Pearl River Delta in Southern China, Taiwan and South Korea.

The conservative view is that Singapore and Shanghai will remain the epicentre of the Asian insurance market. It is foolish however to underestimate the ‘thirst of the Dragon’ and to this end global insurers have so far continued to feel the need to have a presence in Hong Kong. Not only because this is often where the risk originates but also because many shipowners like to correspond with local insurers to provide a local claims service.

Due to this demand, in 2008 the market capacity in Hong Kong has increased. Asia Insurance restarted their bluewater hull underwriting cautiously and conservatively. Starr Marine and ACR (Asian Capital Reinsurance) have set up offices in Hong Kong – expanding their marketing activities.

Following the success of its operation in Singapore, Catlin has also spread their wings and has opened in Hong Kong. Other Lloyd’s vehicles such as Kiln have followed. Ming An continue to have a strong presence but only in facultative reinsurance. Axa and Groupama have much more autonomy and unlike some other underwriters they are not required to refer risks to their parent companies.

Even though there has been significant expansion in Hong Kong, obviously the more complex and high capacity programmes will still be spread globally with the more established markets leading such placements.

Although the market capacity has increased there has been a hardening of the market with Swiss Re, Groupama and Swedish Hull Club all restricting the business they write, and charging increased rates.

Further supporting the establishment of Hong Kong as an important marine base, several P&I clubs have strengthened their presence in Hong Kong and improved their claims service by increasing the number of Hong Kong employees:

- Swedish Club
- West Of England
- Gard
- Charterers P&I

Another important development was the Standard and Poor’s rating of BOCGI (Bank of China Group Insurance), who were upgraded from BBB+ to A-.

Finally, we are pleased to welcome Lucci Leung who has joined Willis from Allianz.

In the coming year, we expect to see continued growth in Hong Kong and further support for this ever maturing market.
WILLIS QUALITY INDEX®
Willis is committed to excellence — especially when it comes to placing our clients’ business with carriers who can best meet their needs.

The Willis Quality Index® has been developed to capture, analyze and share vital carrier information. It is key to promoting superior relationships with our major trading partners globally, whilst enhancing our clients’ ability to make better informed carrier choices. By sharing information with carriers, we are committed to raising standards and service levels for our clients.

**What is the Willis Quality Index?**
The Willis Quality Index combines qualitative opinions from Willis Associates across the globe with quantitative data and measurements from our various tracking systems.

**WQI Carrier Survey**
Through the WQI Carrier Survey, carriers are evaluated by Associates on a five-point scale to record their views on four key areas of service, including:

<table>
<thead>
<tr>
<th>Area</th>
<th>Key Performance Measures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Underwriting</td>
<td>Commerciality, pricing, coverage, responsiveness, continuity</td>
</tr>
<tr>
<td>Policy Administration</td>
<td>Timeliness, accuracy, policy wordings, credit terms</td>
</tr>
<tr>
<td>Claims Performance</td>
<td>Attitude, settlement, technical support, timely approval, timely payment</td>
</tr>
<tr>
<td>Service</td>
<td>Loss control, risk assessment, general service</td>
</tr>
</tbody>
</table>

**WQI Quantitative Metrics**
Quantitative metrics are also sourced from a range of Willis internal systems. Performance is measured relating to:

- **Policy Administration**: including speed and quality of policy issuance
- **Claims Performance**: including the time taken to agree and settle claims

Note: quantitative metrics are not included in release one of WQI for clients.

**How do Willis clients benefit from the Willis Quality Index?**
- Willis clients have the opportunity to make better informed carrier choices, tailored to their specific placement needs, based not only on financial strength but also on superior performance.
- Willis clients have exclusive access to the Willis Quality Index through their trained Account Executive or Client Advocate®.
- A customised report can be produced for a Willis client showing relative performance of carriers for a particular business sector.
- Willis clients benefit from the combined opinions and experience of thousands of Willis Associates worldwide.
- The Willis Quality Index is a unique offering from Willis, with information covering the widest range of service performance measures in an easy to understand structure.
CONCLUSION

Overall, the contributors to this Marine Insurance Market Review concluded that we are still predominantly experiencing a ‘buyer’s market’. However, underwriters of certain products have begun to say “enough is enough”.

It remains to be seen whether this trend will spread but as brokers, we know only too well that there is always a gap between underwriters’ targets and their actual achieved results. Yet, we also know that once capital providers find themselves losing money it is only a matter of time before they force a change in underwriting policy.

It seems that within the Marine Cargo and Liability markets there are still opportunities for both improved terms and broader product offerings. Conversely, the price of P&I insurance is expected to rise yet again. The Hull market is giving mixed signals and lies somewhere between these two extremes.

No doubt the future holds both challenges and opportunities. As always at Willis Marine, we will ensure that our clients receive the benefits of the global insurance market, the most professional advice, and “cutting edge” policy terms and conditions.
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