

Marine Market Monitor

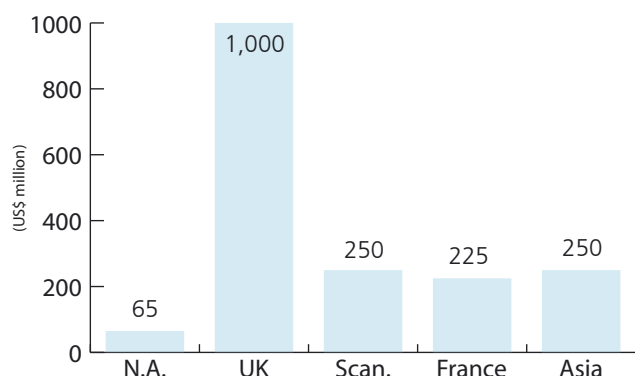
Blue water hull insurance

Hull (blue water) – Renewal experience over the last six months

Cost changes based on loss ratios

Marketplace	Excellent	Good	Poor
N. America	0 to -10%	0 to -5%	5 to +10%
UK	0 to -10%	0 to -5%	5 to +10%
Scandinavia	0 to +5%	2.5 to 7.5%	15 to 25%
France	0 to -10%	0 to -5%	5 to +10%
Asia	0 to -10%	0 to -5%	5 to +10%

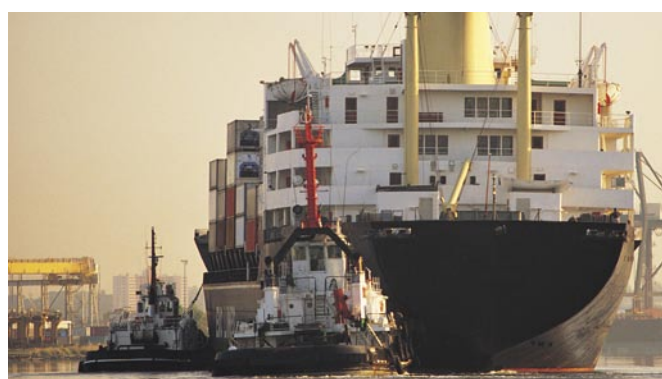
Theoretical capacity* (USD)



* Theoretical capacity refers to total maximum capacity assuming no restriction

Contents

Blue water hull insurance.....	1
Brown water hull insurance	3
Marine liabilities.....	3
Protection and Indemnity.....	4
Marine cargo.....	5



The marine hull insurance market has been the exception to other marine lines of business by consistently producing an underwriting loss for the prior ten year period – with underwriters averaging a 30 percent expense ratio, no underwriting year has been profitable since 1996. This premise was recently reinforced when a number of underwriters reported their financial year results, showing a contraction of premium income and deterioration in loss ratio. Amazingly, these poor results have not deterred newcomers to the marine insurance market, in effect compounding the over-capacity situation and increasing underwriter competition on the risks perceived to be of higher quality. These two factors continue to provide downward pressure on rates and are the main reason that the marine hull insurance market remains soft.

We estimate that the overall theoretical capacity (on the basis that all underwriters write their maximum line) per vessel is estimated to be in excess of USD1.5bn. Therefore it can be assumed that over 90 percent of the world’s hull business can be placed using less than 10 percent of the available market. The actual global marine hull written premium is estimated to be in excess of USD5.2bn. This amount is less than the 1998 premium income despite the considerable increase in vessel values and gross tonnage in the intervening period.

Underwriting deficits cannot carry on forever of course, and we are seeing the first signs that we are approaching the bottom of the cycle; the Norwegian market is seeking increases (and obtaining them with some degree of success). As underwriting results continue to deteriorate pressure will gradually build within the other international markets to first stabilise then increase the premium levels.

The most worrying concerns for hull insurers are the soaring cost of ship repairs in all sectors, and the increasing frequency of losses (see claims section). The recent increases in the price of steel have impacted the costs of repairing vessels and there is a general lack of availability of quality repair facilities worldwide. This is primarily due to the buoyant shipbuilding market and yards focusing on construction contracts rather than repair contracts. This situation affects the more specialised vessels such as Liquid Natural Gas (LNG) carriers.

Region to region, the markets are somewhat out of phase in the rating cycle. As an example, the marine hull insurance market in Asia continues to grow. With the expansion of Lloyd's Asia there is an increased appetite for liability risk. Singapore shows signs of becoming a "proper" global wholesale market in addition to being a domestic market. There are now over 15 hull or builder risks insurers in Singapore willing to lead or follow. Contrary to Singapore, both the China and Japan hull insurance markets show signs of hardening. Rates in the Japanese market are hardening as a result of recent losses. Rates in China have not yet hardened, but could do so because of the collapse of the Shanghai stock market and the hardening by some 20 percent of the RMB (Renminbi) against the U.S. dollar as at June 2008.

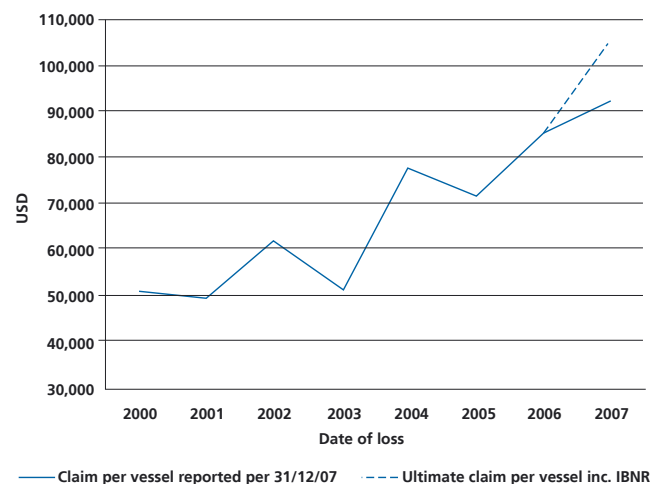
Overall, the current outlook for marine hull insurance indicates that for ship owners with a comparatively claims free history, there is a definite continuing softening in premium/rating levels with incumbent underwriters. For those ship owners with an indifferent record negotiating rate reductions with existing underwriters, while not impossible to achieve, are somewhat more difficult to accomplish. In real terms, for owners with less profitable business, a change of market is likely to bring a greater prospect of more competitive premiums especially when linked to future profitability or loyalty bonuses.

Claims trends

According to market statistics, average claims costs have risen by 86 percent over the past five years, with groundings and collisions being the largest area of increase. The latest available statistics from the International Union of Marine insurers (IUMI) can be summarised as follows:

- Total numbers of Total and Partial losses as reported by IUMI have risen by 270 percent over the last 10 years.
- Total and Partial losses have shown a 25 percent increase in 2007 over 2006
- Total losses:
 - Over the longer term total losses have reduced
 - 2006 and 2007 were bad years
 - Weather is still the largest cause of total losses, however groundings and collisions leading to total losses have increased over the past five years
- Partial losses:
 - While machinery damage is still the largest single cause of partial losses, groundings and collisions have increased over the past five years, with an overall upward trend.

The chart below sourced from Central Union of Marine Underwriters (CEFOR), illustrates the increased cost of claims per vessel experienced by the Norwegian market over the last several years. This trend can be considered indicative of Marine claims trends globally.



Underwriters are seeing an increase in claims resulting from human error, and are becoming justifiably concerned over the human factor influence on claims. Arguably, crews in many areas have the benefit of an as good or better 'textbook' education than applicable in the past. However the lack of experienced masters and crews, crew fatigue arising from gruelling sailing schedules, as well as other less tangible human factors such as frictional issues arising among multinational / multicultural crews are widely viewed as contributing in the increase in loss experience across most shipping industry segments.

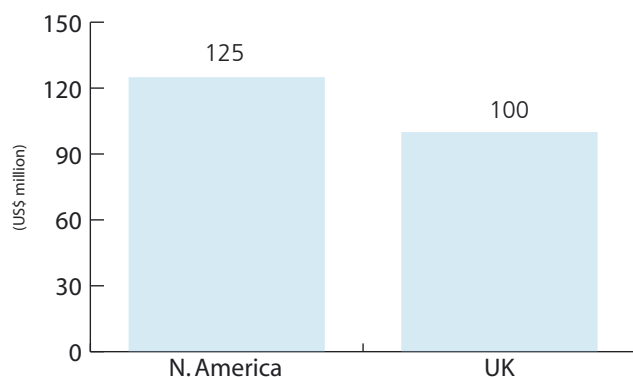
As such, the overall underwriting trend of increasing losses continues to be an issue for marine hull underwriters. Particularly at a time when the costs of materials and shipyard labour have increased, yet hull deductibles have remained largely unchanged.

Brown water hull insurance

Hull (brown water) – Renewal experience over the last six months

Marketplace	Cost changes based on loss ratios		
	Excellent	Good	Poor
N. America	-5 to -20%	0 to -10%	TBA
UK	0 to -10%	0 to -5%	TBA

Theoretical capacity* (USD)



* Theoretical capacity refers to total maximum capacity assuming no restriction

Owing to significantly lower values, most "brown water" hull insurance is placed within the operators' domestic markets. Only the London market, and to a lesser extent the U.S. market, will entertain non-domestic brown water fleets.

A key concern for underwriters in the brown water hull insurance market is the availability of experienced crews, spare parts, and repair facilities. This concern has become more pronounced as equipment; tugs in particular, become more specialised and complicated.

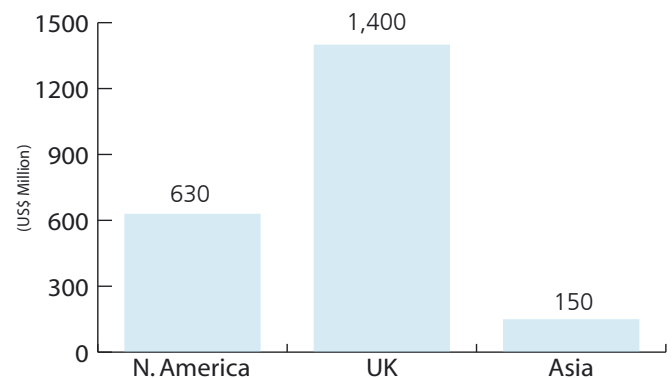
We continued to see an increase in U.S market capacity over the first half of 2008, contributing to the downward pressure on rates. Fleets with attractive loss records, and significant premium volume may be able to obtain double digit cost reductions, especially if the slip leadership changes.

Marine liabilities

Marine liabilities – Renewal experience over the last six months

Marketplace	Rates based on loss ratios		
	Excellent	Good	Poor
N. America	-10%	0 to -5%	TBA
UK	-10%	0 to -5%	TBA
Asia	-10%	0 to -5%	TBA

Theoretical capacity* (USD)



* Theoretical capacity refers to total maximum capacity assuming no restriction

In our last report we noted the continuing general renewal trend of 'flat' to 10 percent reductions. Overall market capacity has continued to increase, particularly in the U.S., and Asia, and in the absence of either a series of significant losses impacting large segments of the market, or a dramatic change in the availability of reinsurance, there is no reason to anticipate a change to the marine liabilities insurance market response in 2008.

Protection and Indemnity (P&I)

The February 2008 International Group Agreement (IGA) P&I renewal was one of the toughest for some years. The average increase sought was 15 percent, which in some cases included a mandatory element. This is on the back of average increases of nearly 11 percent annually since 2000.

In keeping with the rest of the insurance world, the P&I market has not been immune to concerns about the shortage of quality crew, a factor that is thought to contribute to the overall inflation in claims (particularly navigational claims). This continuing trend in high levels of Pool claims (excess of USD7m) posed a challenge to Clubs in terms of forecasting, a challenge that was further compounded by the fact that a few Clubs also observed an increase in retained claims. For the first time we saw elements of the general increase specifically allocated to Pool expenses, and offered on a non-negotiable basis. Pool claims in 2007 are reportedly a little off the USD600m level seen in 2006, but only by USD40m or USD50m.

Other factors that may be responsible for keeping claims levels around the 2007 threshold include the increased limits to international protocols, higher labour and commodity prices, and the notable increase in trade and the size of vessels. Additionally, spiraling wage bills have also kept crew claims high, with some owners having to adjust wages two or three times in the year.

In terms of profitability, investment returns varied between 4.5 percent at the low end and 8.8 percent at the upper end, neither sufficient to offset the underwriting losses sustained by most Clubs. The exception to this is Gard who achieved a return of USD124m, and North of England whose USD40m was in excess of a reasonable underwriting loss of USD10m.

Overall Clubs claim to have achieved their target increases. If so, a 15 percent rise in premiums will help to bring some stability. However the performance of the major Clubs for the year ended 20 February 2008, suggests that for some this is just the beginning and that similar rises will be needed next year if they are to maintain financial stability.

Club	Surplus (USD million)	Free reserve (USD million)	Underwriting result	Investment return (percent)	General increase (percent)
American Club	1.2	34	2.4	5.4	20
Britannia	-34	268	-74	5.4	23.5
Gard	69	561	-55	8.8	10
North of England	30	220	-10	7.1	17.5
Skuld	12	204	3.5	8.0	7.5
Standard	9	226	-20	8.5	15
Steamship	28	186	0	4.5	15
UK	-34	229	-96	6.5	10*
West of England	-31	174	-45	5.4	15

* plus a further mandatory 12 percent "Pool Surcharge" applied to premiums net of excess of loss reinsurance

Our projections suggest that if claims continue to rise at the 10 percent rate that we are seeing, International Group premiums will need 15 percent rises for the next three years just to keep pace.

Marine cargo

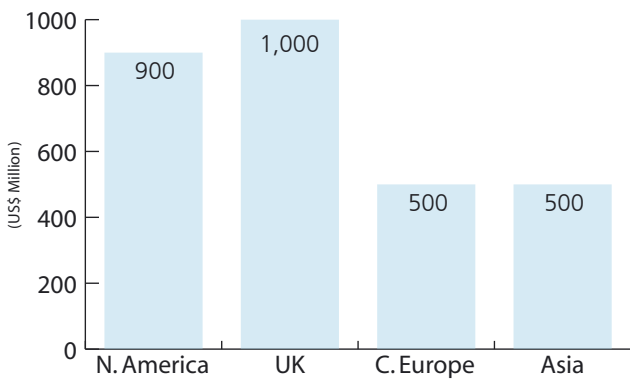
Marine cargo - renewal experience over last six months

Marketplace	Estimated rate increase or decrease based on loss ratio		
	Excellent	Good	Poor
N. America	-15 to -20%	-5 to -15%	5 to -5%
UK	-10 to -15%	-5 to -10%	Flat to 10%
Continental Europe	-15 to -30%	-10 to -15%	0 to -10%
Asia	-15 to -25%	-10 to -15%	-5 to 5%

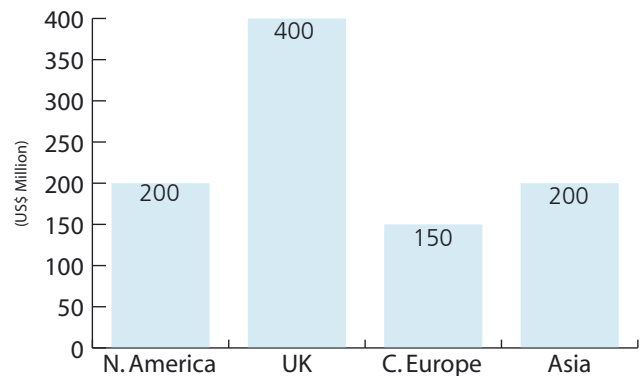
Marine cargo (Stock-throughputs) - renewal experience over last six months

Marketplace	Estimated rate increase or decrease based on loss ratio		
	Excellent	Good	Poor
N. America	-5 to -20%	-5 to -10%	5% to Flat
UK	-7.5 to -15%	-7.5 to Flat	Flat to 10%
Continental Europe	-10%	-5%	10%
Asia	-10 to -25%	-10 to -15%	0%

Theoretical capacity* (USD)



Theoretical capacity* (USD)



*Theoretical capacity refers to the total maximum market capacity available assuming all markets align on the same placement and each market provides their full treaty limits

Market overview

On average, cargo owners continue to benefit from falling rates within the global cargo insurance market. The absence of any significant claims activity over the first half of 2008, and the prior two year period, indicates that there will be continuation of the soft cycle.

The North America marine cargo marketplace continues to be aggressive in seeking market share at the expense of profitability. We anticipate this trend to continue for the upcoming six months for the following reasons:

- The capacity in the marketplace is more than sufficient when measured against the demand;
- New insurers continue to enter the marketplace offering between USD20m and USD25m of capacity;
- The marine cargo market has experienced two consecutive years of minimal catastrophic losses;
- The capacity in the reinsurance marketplace remains more than adequate for the limits purchased by the direct insurers.

It is important to note however that the trend noted above may be slowing. Over the last two years insurers have provided significant reductions of between 40 percent and 60 percent and are now beginning to quote more moderate decreases or even renewals “as expiring”. Poor loss ratio accounts are beginning to experience small increases for the first time in several years.

By contrast, the London cargo insurance market did not enter into the rating spiral seen in the past two years and continues to underwrite their portfolio on a more even keel in enhancing their long term partnership approach. Unlike the other markets, the London cargo insurance market does not typically respond with adverse pricing reaction in the event of a significant loss and this position remains a key attraction for many large Marsh cargo clients. Despite this traditional position, the London cargo insurance market has responded well to the increased local market pressures with renewals in the -7.5 percent to -15 percent range, (assuming a good loss ratio). We certainly see the trend continuing for the next six months. Notwithstanding the above, there are some isolated instances on larger accounts with increasing exposures where we have achieved a 20 percent rating reduction.

On the other hand, the cargo insurance market in Continental Europe has resembled the North America situation, particularly with regard to abundant market capacity and competitive underwriting, as new players strive to secure their market share.

Another similarity between the North America and Continental Europe cargo insurance markets is the differentiation between general cargo cover and the more complex accounts. For instance, in Continental Europe, most of the newcomers are trying to provide differentiation by extending the product range to include Delay in startup (DSU), Consequential loss, trade disruption, etc. The focus on longer term policies of 18 to 24 months will continue to dominate the cargo insurance market in Continental Europe. In response to the uncertainty in financial markets and current levels of pricing, we expect to see selective hardening for certain risks and a more stable market by year end.

The marine cargo insurance market in Asia remains fiercely competitive on pricing with clients mainly focusing on price, as opposed to coverage conditions (i.e. acceptance of fairly bland “All Risks” policies compared with broader manuscript forms). Local direct insurers with support from internationally based

reinsurers are going head to head with Asia based international insurers and adding pressure to the downward spiral on rates.

Given the capacity available, most business is being contained within the Asian market place – a trend that is expected to continue throughout 2008 and beyond. The only exception to this trend is the energy/ petrochemical sector, where limits as high as USD300m per shipment are required. In this instance, domestic markets are unable to respond and international capacity is sought. However, rates in this segment have come under intense pressure and there are signs that international markets have reached levels that they simply will not go lower on.

Infrastructure projects in Asia remain a buoyant class area for both cargo and DSU, however, with the current global credit crunch there is speculation of some slow down in the third and fourth quarters of 2008.

Stock-throughputs

Marine cargo insurers in the North America market are now willing to offer a stock-throughput product with increased limits. By adding the inventory exposure and making the account more complex, these insurers find that they are competing in a smaller marketplace where they can truly differentiate themselves beyond price as a means of attracting new business.

However, as more marine cargo insurers offer the stock throughput product, there is a growing focus on the catastrophic perils of earthquake, windstorm and flood. The inventory limits for the catastrophic perils provided in a stock-throughput programme are now typically aggregated, following the approach utilised in the property market for years. There are exceptions of course, depending on the spread of risk. This focus on the catastrophic exposures has prompted increased requests for more detailed underwriting information at a much earlier stage in the renewal process. In order to manage the increased demand for exposure information, Marsh has utilised a value stratification model to identify inventory risks in catastrophic and non-catastrophic prone areas and presenting same to interested insurers.

The London market has differentiated itself by its willingness to write significant limits on Stock-throughput catastrophic inventory exposures with capacity at an all time high of USD400m. The London market’s willingness to provide large capacity for



difficult risks has resulted in some significant placements and an increase in blended programmes placed into the North America, London and mainland Europe. Stock-throughputs for a retail store chain remains a highly popular product and we are seeing more insurers in the London market offering this product line. We are able to secure up to USD30m of “per store” retail capacity alone. Rates are continuing to fall but with close aggregate monitoring.

Unlike their peers in North America and London, the cargo insurance market within Continental Europe has demonstrated a lack of appetite for stock-throughput policies, largely due to negative underwriting results.

From an Asia perspective, it is worth noting that the devastating earthquake in China’s Sichuan region has had little to no effect on cargo rates. Since Stock-throughputs are not widely utilized within China, the cargo insurance line has been insulated from any revision in underwriting philosophy in response to these types of catastrophic perils.

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