

MARKETPLACE REALITIES 2013



A GROUP OF ONE

Willis

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Marketplace Realities is updated semi-annually.

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As the soft market approached the decade mark over the past few months, I heard plenty of chatter about whether it might indeed *never* turn. While there are noticeable turns in some areas, the chatter in places like Monte Carlo, at the annual Reinsurance Rendez-Vous, and Colorado Springs, at the recent Council of Insurance Agents & Brokers (CIAB), hasn't *really* ceased.

Years of predicting that a devastating loss-year – like, say, 2011 – would turn the market proved untrue. What is happening, instead, is that rates are drifting upward largely thanks to an interest rate environment that is making it hard for insurers to produce investment income with their collected premiums.

Still, there is other evidence showing that our industry has turned a different kind of page. The industry, after decades of waiting for a rising tide to lift all boats, may actually be getting smarter about how we price risk.

So what's on the next page?

In the absence of our traditional tidal shifts in pricing, we are seeing a marketplace where smaller, localized waves are the dominant force. Macro gives way to micro. *Industries* as useful groupings are giving way to *sub*-industries. Diving even deeper below the surface of the tide, regional divisions are forming inside those sub-industries. Where we once might have offered broad conclusions about pricing for life sciences risks, for example, now we may be more likely to talk about therapeutics risks. And then, cutting the data even more finely, we might talk about therapeutics risks in California, a geography that brings with it earthquake exposures and unique Workers' Comp laws and rates.

In the consumer world, the atomized data culled from places like Facebook has reduced the importance of the broad demographic groups that in the past guided so many marketing campaigns. Targeting advertising to discreet zip codes is possible for online entertainment offerings like Pandora. The choices we make create, in effect, a demographic group of one: ourselves. Our individual preferences, the factors that drive our decisions, are available in ways they have never been before.

A similar sharpening of focus will inevitably come to the business-to-business world, although gathering the data may not be so easily automated. Just like we tell Pandora that we like Frank Sinatra, so too will businesses need to supply their own preferences to get the best products and services – and insurance coverage – to suit their needs. And at that point, their vendors, suppliers and partners will need to know what to do with it. Through that process, each risk will become a group of one.

In many ways, we have already arrived at that point. Clients, brokers and markets are all developing refined tools for measuring risk, understanding the marketplace, and assessing the options and methods of handling that risk in – or out of – that marketplace. One such a tool is WillPLACE, our groundbreaking placement tool based on algorithms analyzing data from thousands of brokers and tens of thousands of transactions. We run that data against the desires of insurance buyers and have a detailed set of specific marketplace options. Another tool is the

client risk diagnostic we have built for specific industries and, even more usefully, sub-industries. The diagnostic combines our experience with the client's point of view to create a unique picture of their risk situation that points to a set of specific actions to help mitigate that risk.

This evolution in our business also means that, for brokers and insurance buyers, the nature of our opportunities may be changing. *Enjoy the soft markets, brace for the hard* – that has always been the operating principle. But where are the opportunities now? We believe, in fact, they are everywhere.

We have risks to mitigate, risk transfer alternatives to consider, marketplaces to shop and overall strategies to devise. There are still big savings to be had, even in a market that is firming after years of soft rates. We just have to work a little harder and look a little deeper to find them.

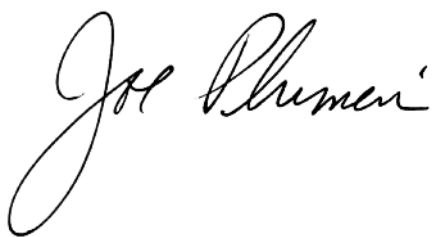
The key to success in a micro world is specialization, customization and individualization. And underpinning it all is the need for discipline.

So maybe the devil in the details is really an angel in disguise. Maybe the growing complexity of risk management will push us further in the direction we are going already. Maybe the service that's required of us, as brokers, will be that much more crucial. Instead of a rising tide lifting all boats, maybe the uplifting effect will be the industry's rising intelligence about the world around us. If that's the trend to watch, we're excited to see it coming.

A market-turning shock is always possible. Some unimaginable string of catastrophes could take away the record surpluses held by carriers today. That's possible, but that's not what's happening now, and that's not what we're planning for.

One aspect of our business has not changed, however. Buyers are under the same pressure to protect themselves, their capital and assets by spending as little of that capital as they can. We're pretty sure that will never change. And neither will the need for a broker that can be a trusted partner at every turn the marketplace may take.

In a world of devilish details, your broker should be your guardian angel, the protector of your group of one. That is our goal, and we strive every day to meet it.

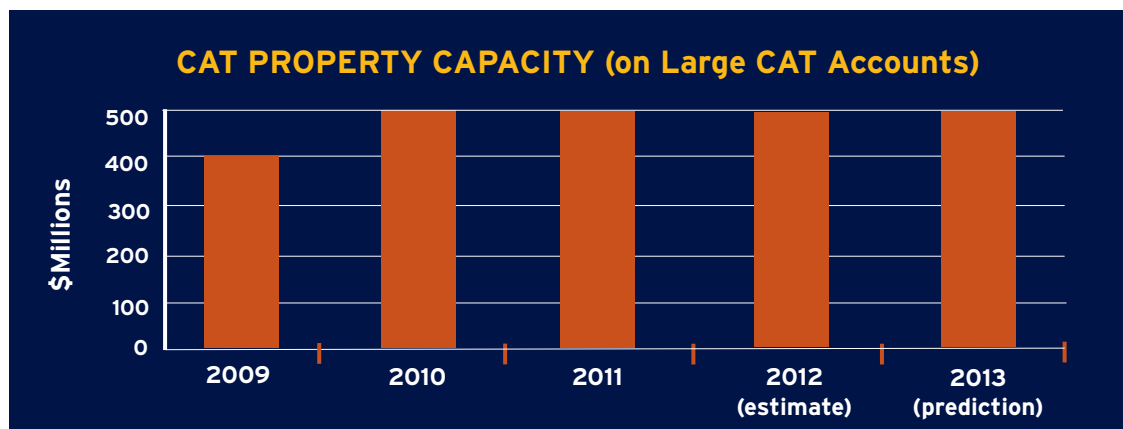


Joe Plumeri
Chairman & CEO
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- 2012 can be best described as a year of recovery for the Property market.
- Global Property losses totaled \$30B for the first six months of 2012 and, even with major losses between now and the end of 2012, loss costs will likely fall far short of 2011's \$116B total.
- **Most Property insurers are posting combined loss ratios in the low 90s for 2012, versus ratios in excess of 100 for 2011.**
 - Despite the spate of massive catastrophe losses around the world in 2011, the Treaty Reinsurance market saw moderate increases (5-10%) outside of the areas hit by major events (New Zealand, Japan and Thailand), where increases typically ranged from 25-40%.
 - At the annual reinsurance industry gathering in Monte Carlo in September, senior reinsurance executives confirmed that, absent a major event, they expect a flat to softening market in 2013.
 - CAT (hurricane, earthquake and flood) capacity is relatively unchanged from 2012 and, in fact, has been stable since 2010.
 - Some insurers re-engineered their portfolios during 2011 and 2012 in order to shed the amount of CAT capacity on their overall book of business. At the same time, other insurers were in the midst of re-engineering their books of business to become more relevant in the large national account Property arena. This reinforces the previous point that there is ample capacity in the market.
 - **In 2012, policyholder surplus reached a record \$570B, up from \$550B in 2011, thanks to a relatively light year so far for natural catastrophe events.**
 - The economy, in particular the anemic interest rate environment, continues to be the biggest impediment to growth for insurers. With little investment income, insurers are under increased pressure to turn an underwriting profit. In 2012, most should be able to achieve that goal.
 - **The formula for 2013 is simple: abundant capacity + low underwriting losses + a weak economy = a flat market. We expect the CAT market to be flat and the non-CAT market to once again offer rate decreases in the range of 5-10%.**

PRICE PREDICTIONS

Non-CAT	-5% to -10%
CAT	Flat



- **Average rate increases are running in the 3-7.5% range** for primary and lead umbrella placements, with excess layers ranging more broadly. Workers' Compensation rate increases are running a bit higher than for other Liability lines.
 - Accounts can expect significantly higher increases in several cases:
 - Poor historical loss experience
 - Hazard classes with significant severity risk
 - Expiring programs placed with overly competitive markets that are non-renewing or re-underwriting their book
 - Expiring programs with multi-year rate commitments
 - **Despite rate increases, underwriters continue to be more aggressive when quoting new business.**
 - Multi-year proposals are becoming very difficult to obtain.
 - Large accounts are better able to manage rate pressures by assuming higher retentions.
 - Regarding exposure changes: payrolls and sales are showing moderate increases while vehicle counts, number of locations and units sold are generally flat.
 - **As a result of the firming of rates and stricter underwriting, marketing activity is increasing**, with approximately 90% of renewals involving some degree of competitive remarketing and carrier account retention rates in the 80% range – lower than they have been in the recent past.
 - We continue to see upward pressure on attachment points for umbrella and on retentions for primary programs.
 - Construction risks, pharmaceutical manufacturers, medical device companies, mining, utilities and energy companies continue to present challenges to underwriters because of the potential severity of their Casualty exposures. Many face above average rate increases, higher retentions or attachments, and restrictions in coverage.
 - Future upward rate pressure may result from exogenous factors affecting investments, interest rates, taxes, inflation and exposure growth. Global and U.S. economic conditions may be impacted by upcoming presidential and congressional elections, the European debt crisis, actions of the Federal Reserve and geopolitical issues in the Middle East and elsewhere.

PRICE PREDICTION

+3% to +7.5%

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- **Underwriters are more conservative when it comes to manuscripted additional insured wordings.**
- **Some carriers are now asking for additional premiums for coverage enhancements, such as Most Favorable Venue (MFV), which were often given at no additional charge in the past.**
- Capacity is still abundant in the U.S., London, Bermuda and elsewhere, but at least one carrier is cutting back on maximum limits they currently offer due to the perception of inadequate pricing for the exposure at higher excess attachments.
 - Carriers are looking carefully at wildfires, EMF, fracking, nanotechnology and other emerging risks. They are also trying to anticipate the potential consequences related to climate change. With the exception of wildfire connected to utility operations, however, we have yet to see significant underwriting restrictions related to these exposures.

PRICE PREDICTIONS

Umbrella	Flat to +7.5%
Excess	+2% to +15%

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- **Worker's Comp is experiencing average rate increases of 5-10%, the steepest increases among the Casualty lines.** The highest average rate hikes are in NY, CA and FL.
 - The market for monoline Workers' Comp and Excess Workers' Comp insurance has become more restrictive in availability, capacity and pricing.
 - The National Council on Compensation Insurance (NCCI), which sets the standards for calculating experience modifiers used to determine ultimate Workers' Comp costs, this year revised their standards significantly for the first time in decades. **This could change the "mods" for many insurance buyers.**
 - Rising rates could well be compounded by rising payroll in a recovering economy and by changes in the experience mods.
 - **Workers' Comp rates continue to be driven by medical costs that rise faster than inflation** – and often rise faster than medical costs outside of the Workers' Comp realm.

PRICE PREDICTIONS

+2.5% to +7.5%, up to +20% in California
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- Large auto fleets will continue to see upward pressure on rates.
- A key issue is umbrella attachment points and the use of buffer layers before the umbrella market will attach.
- Attachment points and buffer layers are impacted by the choice of primary markets. If the primary carrier can only issue \$2M-\$3M in limits, buyers will probably need to purchase a buffer layer. If the primary insurer can issue a \$10M limit, or even a \$5M limit, buyers will probably not need a buffer layer.
- **Umbrella underwriters are requiring higher attachment points for large fleets that include higher hazard vehicles.** Medium to heavy long-haul trucking operations are among the most directly impacted.
- **Pricing is also being impacted by underwriters' heavier reliance on reinsurance than we have seen in the recent past.**

PRICE PREDICTIONS

+2% to +5%

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- Following the U.S. Supreme Court’s decision upholding the Patient Protection and Affordable Care Act (PPACA), employers are focused on elements of the health care reform law that will go into effect in the next few years. **The decision renewed a sense of urgency to assess the impact of reform, particularly in regard to the employer pay-or-play mandate, private insurance exchanges and the excise tax imposed on high-cost coverage.**
 - Many employers fear they will have insufficient time to prepare for coming mandates as government agencies have been slow to provide guidance with crucial detail on implementation.
 - Variables such as delivery system reform are creating additional uncertainty.
 - The cost of insurance continues to rise, as insurers pass down the costs of compliance. Health care reform has raised costs for employers by as much as 5% so far.
 - **Cost increase estimates for the coming year vary from 5% to over 10%.** Providers are asking carriers for improved payment terms, placing further pressure on costs.
 - Employers continue to take aggressive steps to stem the rising costs of health care:
 - Shifting costs to employees
 - Self-insurance options
 - Consumer-directed plans of various types including high-deductible health plans
 - Health Savings Accounts (HSAs)
 - **Cost containment is being driven in part by the Cadillac plan excise tax due to take effect in 2018.** A 40% excise tax on the value of benefits will apply to plans that exceed certain thresholds.
 - The correlation between improving employee health and reducing health care costs is sustaining interest in wellness programs. Employers are making greater investments in existing programs and moving toward outcome-based programs.
 - Employer efforts to offer competitive total reward programs remain thwarted by economic pressures.
 - Many health care providers are starting to offer their own health programs either alone or in partnership with insurance carriers. Accountable Care Organizations, which are focused on the delivery side of health care reform, will provide employers with more choices in providing health care benefits to employees. Understanding ACOs and how employers can benefit from them will be a complex process.
 - Uncertainty over the future continues, given November’s presidential election, but health care reform has stopped few employers from providing benefits to their employees.

PRICE PREDICTIONS



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- The market for stand-alone Cyber policies remains competitive, with **rates flat to down 3% for renewals. With increased losses, a few markets are looking for slight increases over expiring premiums.**
 - **First-time buyers will find a competitive environment**, though the range between insurers may narrow if losses mount.
 - **1041 data breach incidents were reported in 2011, second only to 1048 in 2008**, according to the Open Security Foundation. **The number so far in 2012 is 966.**
 - More stringent privacy laws in the U.S., Europe and other countries have multinational corporations addressing the risk enterprise-wide.
 - Several markets have revised their policies, bringing in more robust data breach response services and other enhancements.
 - A few carriers are introducing Cyber policies in overseas markets.
 - More markets are putting up excess limits, building capacity for large placements, while the competition is driving down the excess pricing.
 - All markets will provide social media liability protection under the Internet Media or Multimedia Insuring Agreement under a Cyber policy.
 - Insureds that buy Errors & Omissions (E&O) policies are often able to add Cyber risk by endorsement. Exceptions include financial institutions and health care organizations.
 - A new SEC guideline recommends that financial reports address exposure to cyber attacks, the potential disruption of computer networks, and how public companies will respond financially to the potential loss. The recommendation has generated more interest in cyber insurance from publicly held companies.
 - Both houses of Congress have filed amendments to the Homeland Security Act seeking certain cyber security measures from corporations that make up the financial and utility infrastructure (banks, power grids, etc.). The concern is about the potential for a cyber attack aimed at strategically chosen businesses to cripple the economic system.

PRICE PREDICTIONS

Renewals	Flat to -3%
First-Time Buyers	Competitive

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DIRECTORS & OFFICERS (D&O)

MARKETPLACE REALITIES 2013

- **The price-firming momentum for primary D&O placements is expected to continue into 2013.** Flat renewals and decreases have been few and far between, with any significant change in exposure (market cap increase or decrease) driving the primary markets to look for rate increases.
 - Certain markets are holding the line and are even willing to lose accounts and end long-term relationships.
 - **On the excess side, we expect competition to drive single-digit reductions where minimum premiums have not already been reached. Others will face modest increases.**
 - **Primary markets are expected to continue pushing for increased deductibles.** This is especially true for any client with M&A exposure, particularly as a target. We also expect markets to continue favoring split retention options.
 - Capacity remains constant, with no new entrants in the marketplace for commercial (non-financial) risks. Capacity for financial services firms remains stable, as carriers respond to the unexpected financial demise of two major options and commodity traders. As the impact of the LIBOR situation on D&O coverage is still uncertain, coverage outcomes continue to be closely monitored.
 - **Private companies and nonprofits are seeing rate increases as well, especially in the health care sector.** An increase in competitive health care capacity has yet to reverse this upward pressure. Homeowner/condominium associations are another difficult class of business with some markets dramatically increasing premiums or exiting the business entirely.
 - The most significant product changes are in the area of investigations. Limited coverage is available for individual directors and officers, but rarely for corporate entities.
 - Limited FCPA coverage is available for entities, but pricing is still high.
 - Another major trend is the expansion of global programs to incorporate local placements (where non-admitted coverage is not permitted).
 - Lead A-Side D&O carriers seek to differentiate their product offerings, but Bermuda continues to be the only market offering more than facilitation costs related to clawback claims under the Dodd-Frank Act.

PRICE PREDICTIONS

Overall	Flat to +10%
Large Public Company	Flat to +10% on primary, flat to +5% on excess
Other Public Companies	Flat to +10% on primary, flat to +5% on excess
Private Companies	Flat to +15%
Nonprofit Entities	Flat to +5%, health care +10%

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EMPLOYMENT PRACTICES LIABILITY (EPL)

MARKETPLACE REALITIES 2013

- **The price stabilizing we are seeing in the D&O marketplace is expected to migrate to EPL placements in 2013.**
 - **The lingering effects of the financial crisis continue to produce class and collective actions relating to the workplace, with more expected in 2013.**
 - The government continues to ramp up its enforcement efforts through the EEOC and the DOL, leading to more government-initiated litigation over workplace issues.
 - Significant EPL claims are being brought outside the U.S. and this is expected to continue into 2013. While the frequency is low, the severity is beginning to attract adverse attention from carriers.
 - **Capacity overall remains abundant with no new entrants into the marketplace.**
 - Carriers in the U.S., Bermuda and London are likely to offer competitive terms on larger risks while London continues to be a prime competitor for middle market accounts. Bermuda continues to offer competitive pricing with broad coverage, including punitive damages for larger companies with 5,000+ employees.
 - An ongoing trend is policy wording addressing new social media exposures.
 - EPL carriers still have little appetite for wage-and-hour claim coverage, with limited coverage available only to smaller organizations. Some carriers are considering offering this coverage in the future.
 - Strategic buyers will look for opportunities to leverage their D&O purchase with potential EPL markets while private and nonprofit firms usually combine the purchase.

PRICE PREDICTIONS

Overall	Flat to +10%
Large Global Companies	Flat to +10% on primary, +5% on excess layers
Mid-Size to Large Domestic Firms	Flat to +10% on primary, +5% on excess layers
Private and Nonprofit Entities	Flat to +10%
Smaller Employers (less than 200 employees)	+5% to +15%

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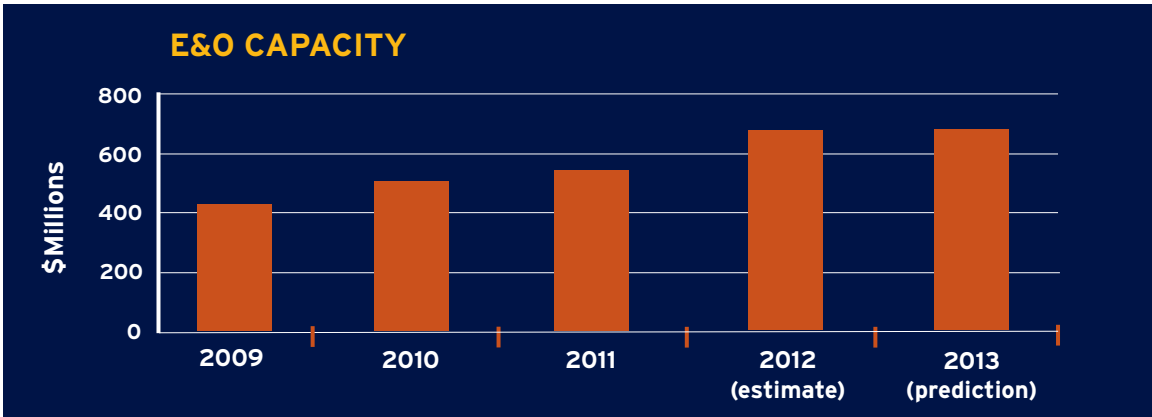
ERRORS & OMISSIONS (E&O)

MARKETPLACE REALITIES 2013

- The E&O market is hardening. For the final quarter of 2012, we **anticipate growing pressure for increases in the 5% range. In 2013, we expect 5% rate increases to be the norm.**
 - **We may see greater rate hikes later in 2013 if supply doesn't blunt the direction insurers are trying to establish.**
 - Other characteristics of a hardening market are also appearing and will become widespread as we move into 2013. Many underwriters are taking a more rigorous approach to underwriting. Policy wording expansion is more difficult to achieve and some amendments that have been generally available are now off the table.
 - Accounts with poor loss experience are facing significant price and deductible increases.
 - **On select accounts with good loss experience or a significantly improved risk control regimen, competition is often robust, with some insureds attaining decreases in the 5% range.**
 - **Competition will remain generally strong for the middle market through the remainder of 2012 and well into 2013.**
 - Abundant capacity continues to influence the market and is a stimulant to competition, though the effect is diminishing. New entrants continue to enter the market and some insurers are expanding their underwriting teams. The newcomers, however, are taking a cautious approach.
 - Authorized global E&O limits are approximately \$700M. Typical insureds should be able to buy from \$350M to \$400M. Recently, insurers have begun closely managing their capacity and often reducing the size of their capacity commitments.
 - Policy forms for mature market segments will not expand meaningfully in terms of core coverage, although insurers will continue to add or enhance options for Network Security and/or Privacy Liability coverage. For several market segments – real estate, for example – large claims will make larger rate increases likely.

PRICE PREDICTIONS

Good Loss Experience	+5% or more
Poor Loss Experience	+10 to +25%



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- **Since August, Fidelity underwriters have been pushing for rate increases, the result of anemic profits for the larger Fidelity markets.**
 - Long-anticipated rate increases began to take shape in late June when the Surety Association of America filed for a rate increase of 25% on behalf of its members, who include the overwhelming majority of leading Fidelity markets in the U.S. This filing followed an earlier 12.5% rate increase filed by ISO in early May. These increases do not mean that rates will now increase by 25% and 12.5% respectively, but they are strong indicators of a firming market.
 - Five of the top 10 markets reflected combined loss ratios of 95% to 194%, calculated by utilizing Surety Association loss ratios coupled with a standard expense factor of 30% (for commissions, salaries, rent, etc.). These five markets write over 67% of the total premium volume for the top 10 markets.
 - Primary capacity for the Fortune 500 and for large regional financial and money center banks remains limited to a handful of lead markets. However, capacity for Fortune 1000 and midsized commercial accounts, as well as smaller financial institutions, remains plentiful.
 - **Breadth of coverage afforded by underwriters remains intact and no indications of contraction are on the horizon.** Deductibles are holding firm and contract enhancements are being renewed.

PRICE PREDICTIONS

Overall	Flat to +10%
Comprehensive Crime: <ul style="list-style-type: none"> ■ Middle Market and Fortune 1000 ■ Fortune 500 	Flat to +5% Flat to +10%
Financial Institution Bonds: <ul style="list-style-type: none"> ■ Small to Mid-Sized ■ Regional to Large Institutions 	Flat to +10% Flat to +10%

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- **The price firming momentum we are seeing in D&O placements is expected to migrate to Fiduciary placements in 2013. Any increase in either Plan assets or employee count is now met with an immediate response from markets that rate increases are needed.** We expect that this noise will get louder in the coming months as the carriers continue to argue that these lines are underpriced. However, some markets are still willing to keep very low, or even zero, retentions.
 - Capacity remains constant, with no new entrants into the marketplace.
 - ERISA tagalong litigation (including FLSA tagalong activity) continues, and suits involving cash balance plans are still making their way through the courts.
 - Class certification in ERISA cases, especially in potential class actions involving 401(k) plans, has been strongly impacted by the recent *Dukes v. Wal-Mart* employment decision from the U.S. Supreme Court.
 - Market response (if any) to the IBM decision regarding settlor liability remains to be seen.
 - **Uncertainty about the national health care agenda and potential changes in the definition of “fiduciary” in the health care context are significant concerns not yet reflected in the marketplace.**
 - The migration of recent D&O coverage enhancements into Fiduciary policies is expected to continue throughout 2013. This can include affirmation wording relating to (presumptive) indemnification and advancement of defense costs as well as expanded coverage for investigations.

PRICE PREDICTIONS

Overall	Flat to +15%
Companies with large concentrations of their stock in their employee benefit plans	Flat to +15% on primary, flat on excess layers
Companies without company stock in their plans	Flat to +5% , flat on excess layers
ESOP-owned firms	+5% to +10%
Private and Nonprofit entities	+5% to +15%

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- **The Health Care Professional Liability (HPL) market will remain soft through the second half of 2012, with rate reductions up to low single digits.**
 - Certain long-term care risks may see slight increases due to shifts in the legal environment that have led to large losses.
 - **Loss frequency remains at historically low levels (with perhaps a slight uptick).** Severity has moderated and is actuarially predictable. Jumbo verdicts in 2011 and the first half of 2012 have not moved market pricing.
 - **Health Care Reform (PPACA), upheld by the U.S. Supreme Court, will shape malpractice risk and underwriter response, as many health care organizations prepare for the 2012 Accountable Care Organization (ACO) implementation** and/or move to clinical integration by acquiring physician practices and contractual relationships with other providers.
 - Many buyers may need to adjust terms and conditions to address cyber-related issues, executive risks, inter-related provider contractual liability and a new world of pay-for-performance and financial risk.
 - Consolidation of insurers in the HPL industry is continuing, particularly among the physician insurers.
 - “Integrated occurrences” (i.e., related acts or batch coverage) remain an issue for many insurers.
 - Despite a few recent court decisions overturning damage caps (e.g., the ruling in Missouri in August), we see no clear trend towards overturning malpractice reform legislation. Some state courts have recently upheld reform laws or enacted various enhancements to existing reform laws.
 - Rapidly expanding use of electronic medical records may present significant liability exposure while potentially reducing claims by encouraging better communication.
 - The movement of physicians away from private practice to the hospital employment model continues unabated.
 - Merger and acquisition activity by hospitals and hospital systems remains very high.

PRICE PREDICTIONS

Overall	Flat to -5%
Long-term care providers	Flat to +12.5%

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- **Downward rating trends continue, despite airline exposure growth. Rates are falling in the single digits. Where exposures are contracting, rates are not rising to compensate and premium levels are falling.**
 - **Unprecedented airline loss performance and abundant capacity are likely to accelerate the premium reductions.**
 - Market appetite for airline risks varies significantly, resulting in dramatically different renewal results.
 - Economies of scale will continue to improve results for the largest programs.
 - The Aerospace sector continues to see softening market conditions.
 - Corporate Aviation continues to see competition driving down premium volumes and bringing improvements in coverage.
 - Excess capacity is available across all sectors but is not being fully utilized. New entrants added relatively small amounts of capacity to this already competitive sector.
 - **Industry and program consolidation in all sectors continues to erode premium levels.**
 - **Airline losses combined over the last two years are well below the sector's five-year average.**
 - No losses involving large numbers of fatalities have occurred for several years.

PRICE PREDICTIONS

Airline	
■ Premium	-5% to -15%
■ Rates	Flat to -25%
■ Exposures	-10% to +20%
Aerospace	Flat to -5%
Corporate Aviation	-5% to -15%

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- **Rates for Property and Casualty continue to trend upward, but not to the extent that we would call this a hard market.** Incumbent carriers continue to push for rate increases. Guaranteed cost programs (policies without retentions) and excess Liability continue to experience the highest rate increases.
 - **Property - Many clients are experiencing increases of up to 10%.** Flat renewals are considered a good result. Claim history and CAT continue to be key drivers.
 - General Liability – Construction defect exposures and various state litigation trends are creating volatility. At the same time a number of carriers are underwriting this line.
 - **Workers' Compensation - Rate increases are averaging 10%, and more in some states.**
 - Excess/Umbrella Liability – Most renewals are subject to increases. Rates are up 7-10% on average and we expect that to continue into 2013. Limits of \$500M are available, with most of the larger contractors carrying \$25M-100M. Some carriers are retracting capacity in certain states or for certain construction risks. Carriers are also continuing to push for higher attachment points, particularly for Auto Liability and in many states for General Liability.
 - **Auto Liability - Renewals are stable.** Most 1/1 renewals are expected to be flat or +5%. Carriers often adjust Auto rates to offset rate movement in other lines of coverage.
 - Builders Risk – In general, the Builders Risk market remains very competitive and capacity is still very strong. Claim history and CAT exposures will significantly impact rates along with deductible levels and sublimits. Hurricane Isaac's initial Property damage estimates are around \$2B so we expect some reductions in CAT capacity for the Florida/Gulf Coast region, especially for smaller construction projects.
 - **Project Insurance (Wrap Ups) - Carrier interest in owner- or contractor-controlled insurance programs (CIPs) remains high and underwriters are enthusiastically pursuing these opportunities.** Market leaders are indicating a strong preference for contractor CIPs, citing better historic performance, but owners are still attracting plenty of interest. State limitations on indemnity agreements and challenges securing and confirming appropriate additional insured protection are pushing owners and contractors towards project solutions like CIPs, as well as project-specific Environmental and Professional Liability cove.
 - **After a long hiatus, residential construction projects have quietly resumed and sponsors and contractors alike are looking at CIPs for coverage certainty.** As insurance rates firm we anticipate that the market will look for opportunities to require greater risk sharing through higher rates. New York continues to present a unique challenge for owners as CIP costs can exceed conventional insurance. CIP activity over the past six months has been high, with carriers reporting much higher submission counts so potential CIP sponsors will need to get their projects submitted in a timely manner to avoid quote delays.

PRICE PREDICTIONS

General Liability	+3% to +10%
Excess Liability	+5% to +12%
Workers' Compensation	+3% to +10% (state-by-state increases could be higher)
Builders Risk	Flat to +10%, higher in high catastrophe areas
Project Insurance (Wrap-Ups)	Primary and excess rates remain flat with significant variation depending on job size, type of work and location

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DOWNSTREAM

- **In April, rating levels hit their lowest point in over 20 years, but some genuine hardening is now apparent in the North American Downstream market.**
- The international market remains essentially flat, although hardening can be detected in some quarters.
 - Market conditions remain relatively stable, as capacity has increased by 14% in 2012.
 - However, the run of losses in 2011 continues to impact this sector.
 - Of particular concern to many insurers following the losses of 2011 has been Contingent Business Interruption (CBI), with particular focus on supply chain, named suppliers and sub-limits.
 - Markets are differentiating even further between those risks and risk partnerships that they truly value and those that have been impacted by recent losses.
 - Increased values continue to disguise low rating levels.

PRICE PREDICTIONS

Generally modest rises

UPSTREAM

- **Overall capacity levels inch toward the \$5B mark.**
- **Those insurers that have continued to write Windstorm have reaped the benefits of another loss-free year.**
- The ultimate impact of 2012 hurricane season is still unknown, but so far so good, and overall exposures are down as fewer assets are insured.
- Buyers looking for increased OEE limits will find them – for a price.
- Marine liabilities remain an area of concern following the Macondo losses.
- Insurers are focusing on accurate underwriting information for FPSO risks, looking closely at:
 - The age of the FPSO, and the sophistication of its design
 - The nature of the dynamic positioning system (DPS)
 - Details of the mooring system
 - Details of the alarm system
 - Details of the unit’s electrical system

PRICE PREDICTIONS

Generally modest rises

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- **Competitive terms and pricing continue with respect to the base coverage forms for Contractors Pollution Liability (CPL) and site-specific Pollution Legal Liability (PLL) insurance. However, prices are up slightly for select risks and product lines, particularly Underground Storage Tanks (UST) and Combined Pollution/General Liability products.**
 - **Breadth of product offerings, capacity and underwriting appetite differ dramatically among the 30 carriers focused on environmental exposures.** In some cases, new forms are being developed or coverages are being added to existing pollution policies. In other areas, e.g., fracking exposures, coverage terms are being limited, and the market may be reticent to offer terms.
 - Many insurers have expanded coverage in their base Contractors Pollution Liability and site-specific Pollution Legal Liability forms so that extensive manuscripting is less common than a few years ago.
 - Certain product lines continue to move toward commoditization (e.g., Contractors Pollution Liability), while others are being “re-underwritten” by some carriers. Some products, such as Cleanup Cost Cap, have become extremely difficult to procure. And some risks are quite difficult to transfer at all, such as underground storage tanks more than 15-20 years old.
 - **With capacity plentiful, many insureds are implementing layered program structures.** Ten years ago, a handful of environmental insurers had single-policy capacities of \$50M to \$100M. Today, very few have more than \$25M.
 - Long-term policies are less available for operational exposures. One- to three-year terms are preferred. Ten-year terms are still available for project-specific applications and for historical protection, which is important for transactional placements. In some cases, Contractors Pollution Liability project terms plus completed operations coverage may still be available for as many as 17 years.
 - Increased writings and the development of longer-term policies placed in prior years continue to drive an increase in claim activity among the various product lines. The first 10+ year PLL policies terms were written about 15 years ago; claims and loss development are topics of discussion among long-standing markets.

PRICE PREDICTIONS

Contractors Pollution Liability	-5% to +10%
Pollution Legal Liability (including combined GL/PLL)	-10% to +10%
Environmental Professional Liability (including CPL)	-5% to +15%
Financial Assurance Instruments (USTs, Closure, Performance Bonds)	Flat to +10%
Cleanup Cost Cap	+10% to +20% (if available)

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- **Rates in the U.S. Special Contingency Risks (Kidnap & Ransom) market remain stable, and premiums will continue to be higher for companies with significant exposures in Latin America, Africa and the Middle East.**
 - Mexico, Venezuela, Nigeria, Pakistan, Afghanistan, Philippines, Iraq and Somalia continue to be the areas of primary concern, as do several more recent hotspots for kidnapping, including Mali, Mauritania, Niger, Sudan, Malaysia and Kenya.
 - **The risk of political evacuations caused by political upheaval remains high in places such as the Middle East, and carriers remain cautious in their approach to Emergency Political Repatriation and Relocation coverage.** Limits are commonly reduced and certain North African and Middle Eastern countries are frequently excluded.
 - Although some reports indicate that international efforts to reduce piracy off the coast of West Africa are working, Somali piracy remains a problem and the underwriting of exposures in impacted waters is cautious.
 - Buyers with exposures in the U.S. and low-risk overseas locations can expect flat renewals.

PRICE PREDICTIONS

Flat to +10%

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- **The long-term impact of the loss of the cruise liner Costa Concordia in early 2012 remains uncertain. The consensus so far is that nothing has fundamentally changed, as this and other notable losses have so far had little or no impact on hull premium rates or the availability of insurance cover.**
 - Piracy continues to blight the industry, with no lasting resolution in sight. As the number of successful hijacks diminishes, the ransom settlement figures and the duration of seizures are proportionately increasing. The desperation and unpredictability of the pirates and their financiers appear to be rising as well.
 - **The Cargo market remains soft, with reductions in both premiums and deductibles resulting in increased limits at little extra cost.**
 - New capacity in the Lloyd's market from start-up syndicates has created a more competitive marketplace.
 - Ratings remain fairly stable in the marine Liability market following a short-lived reaction from some underwriters after the Costa Concordia loss. Because of the ready availability of capacity in the sector, underwriters have been unable to sustain rate increases they have sought. **The market is now awaiting a game-changing trigger: another high profile loss, an increase in the cost of reinsurance or just an unwillingness to tolerate the erosion of profit levels.**

PRICE PREDICTIONS

Modest hikes in Hull, soft conditions elsewhere

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- Political risks are rising due to:
 - Economic tensions in Europe and China
 - Political tension between Iran and Israel
 - Rioting in Indonesia
 - Escalating violence in Syria
 - Maritime disputes involving China, Japan, South Korea, Vietnam, Taiwan and the Philippines
 - Anti-Japanese riots in cities across China because of a dispute over islands, leading to Toyota and Honda closing down factories in China
 - A return of anti-American violence in the Middle East
- **Despite the tensions, asset destruction due to political violence has been sparse.**
- In 2012, we anticipate several trends:
 - **Flat to slight downward pressure on premium rates**
 - Increased underwriter due diligence and increased focus on structure and security
 - Syndication for policies above \$50M in limit of liability
 - **The premium base for 2012 is expected to be around \$1.4 billion, with losses at less than 100% of that amount.**
 - Many insurers are waiting to see how presidential elections in Venezuela in October will impact the foreign investment and trade environment.
 - Forced abandonment cover is in the spotlight as political violence has pushed governments and corporations to evacuate nationals and employees.
 - North and South American construction and engineering companies bidding on projects in Africa, Latin America, Asia and the Middle East are looking to cover their contractors' plant and equipment against expropriation, deprivation, forced abandonment and political violence.
 - U.S. companies continue to protect potential losses arising from host governments (e.g., China) imposing foreign exchange remittance restrictions that prevent payment of dividends or repayment of loans involving foreign subsidiaries.
 - The Eurozone debt crisis continues to limit the outflow of capital while increasing the cost of funds for global investments. There has been a noticeable shift towards Asian, American and even Latin American super-regional financial institutions to cover the gap left by retreating European FIs.

PRICE PREDICTIONS

Flat to slightly decreasing

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- The industry continues to face increasing competition from new entrants.
- **In the face of declining revenues, sureties are more aggressively pursuing new business.** Sureties are targeting large contract accounts by offering lower rates and more attractive underwriting terms and conditions.
 - Loss frequency has continued to increase in 2012, primarily for smaller to mid-sized general contractors and specialty subcontractors. This helped raise the direct loss ratio for the industry from 13% at the end of 2011 to 24% for the second quarter 2012 (SFAA Results). **Despite the increased loss activity, the industry overall remains profitable.**
 - **Capacity continues to be readily available for contract and commercial bonds.**
 - Reinsurance capacity remains adequate to meet market demand and is available for both existing and new markets.

PRICE PREDICTIONS

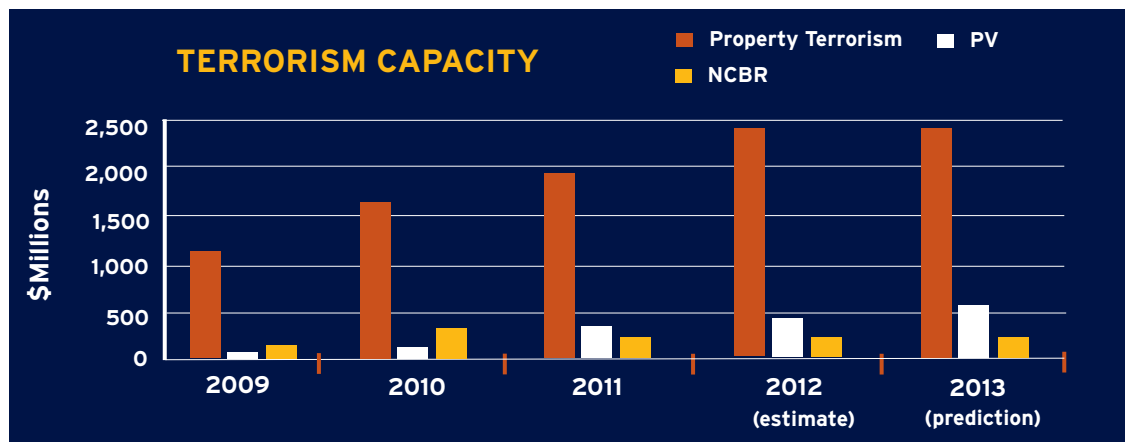
Moderate fluctuations within an overall softening market

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- Uncertainty looms as the U.S. Congress begins to debate the 2014 renewal of the Terrorism Risk Insurance Protection Reauthorization Act. **The Terrorism insurance market can be expected to harden in 2013 as insurers face doubt about continued federal support.**
 - **Buyers continue to seek coverage for Political Violence risks as an extension of traditional Terrorism coverage**, especially in light of rising tensions in the Middle East, North Africa and other global flashpoints.
 - New entrants into the stand-alone Terrorism insurance market have offset capacity reductions by established carriers. Terrorism capacity remains at an estimated maximum of \$2.5B per risk, though that figure is far lower in major metropolitan areas – particularly New York, Chicago and San Francisco.
 - New aggregate modeling protocols across the market could further reduce aggregate availability in certain Central Business Districts.
 - Customized deterministic terrorism models have also facilitated more accurate estimates of potential Property and Casualty losses stemming from a range of attack scenarios for individual risks.
 - Interest in Nuclear, Biological, Chemical and Radiological (NBCR) Terrorism coverage continues to grow. The maximum capacity for NBCR terrorism is estimated at \$200 million per risk.
 - **Captives remain an efficient risk transfer tool when capacity is otherwise unavailable for Terrorism perils**, including NBCR and Cyber Terrorism.

PRICE PREDICTIONS



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- Unstable economic and political conditions persist worldwide, especially in Southern Europe, yet **Trade Credit insurance rates and capacity remain stable**. The current market still offers significant opportunities for corporations wishing to transfer the risk of non-payment of receivables.
 - Market conditions have firmed a bit in the previous 12 months but remain far from historic 2008 highs. **Overall we expect the marketplace to remain favorable for insureds in 2013.**
 - Capacity for particularly risky individual buyer credits, however, especially in the retail sector, is becoming scarce.
 - **The potential for European default contagion continues to loom. Such a shock would likely create a swift and sharp increase in premium rates and an equally sharp contraction in available capacity.**
 - Reinsurance capacity remains plentiful for Trade Credit markets.
 - While current claim activity is down in terms of frequency, severity is up slightly compared to recent years. **We expect claim activity to pick up in Asia due to margin erosion in many sectors and in Western Europe due to the current recession.** Domestically, we expect a flat trend in claims in both frequency and severity.

PRICE PREDICTIONS

Flat to -10%

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