

BIQ

October 2007

BERMUDA INSURANCE QUARTERLY

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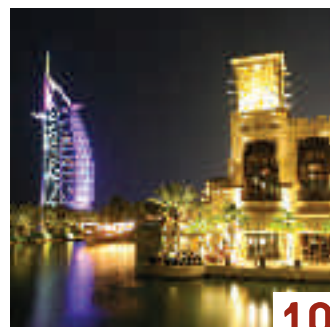
Q2 **12**

A WOMAN
TO BE
WATCHED!

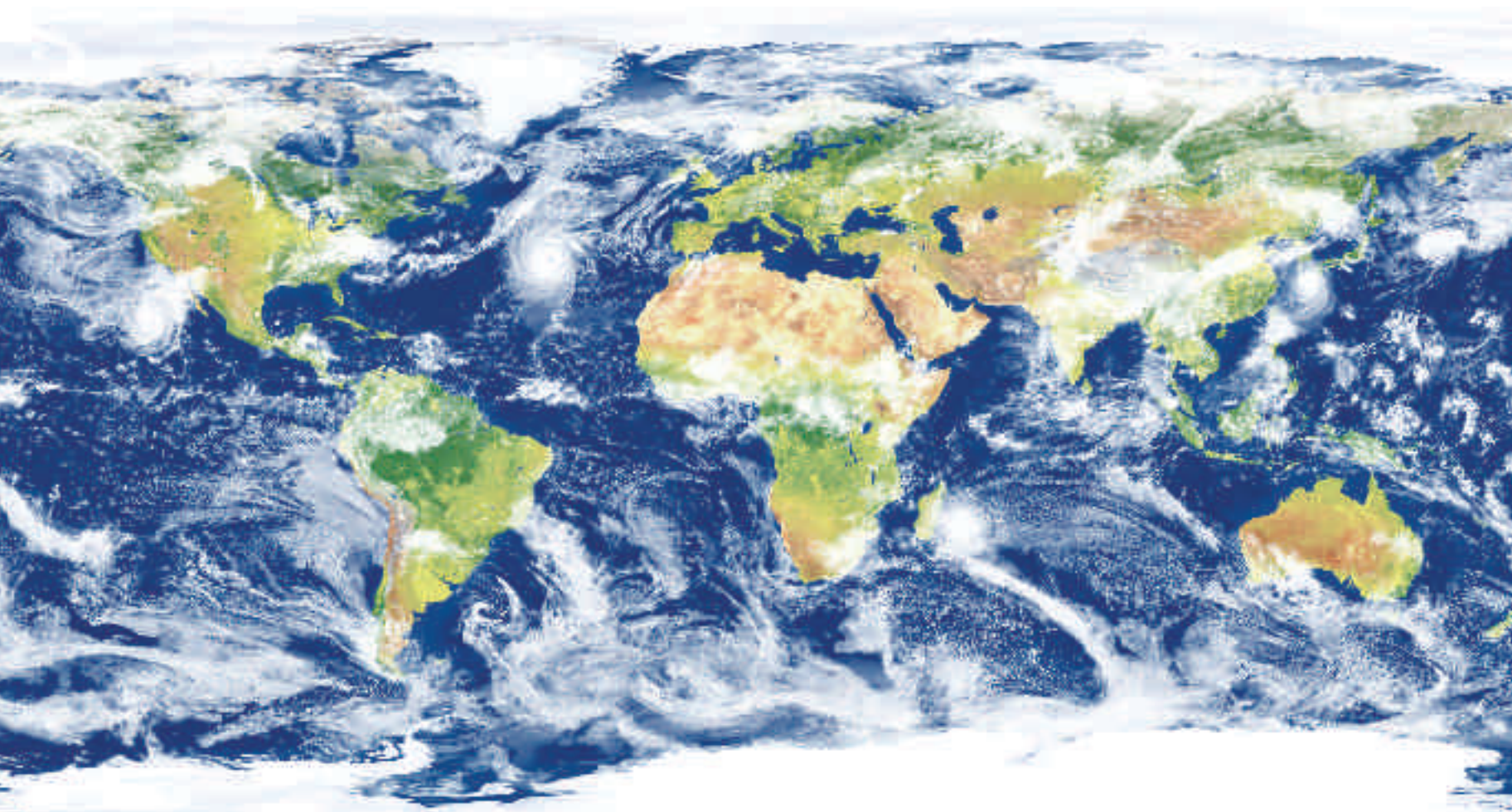


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BERMUDA
BOWS TO
DUBAI...



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STUDYING THE BIGGER PICTURE...

Even though the US hurricane situation remained quiet at press time, flooding losses from Europe and Australia impacted ratios. Meanwhile, Ren Re is funding a device that could help cut property losses by up to 10%. See articles on pages 12 & 15

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THE QUOTES OF THE QUARTER

“The non-life market is continuing its slow decline as cedants retain a greater portion of their business and competition at the reinsurance level intensifies. [However], pricing declines are being broadly offset by continued favourable loss trends, and PartnerRe is benefiting from cedants’ movement to higher quality reinsurers, which is consistent with this stage of the reinsurance pricing cycle.”

— **PartnerRe President & CEO Patrick Thiele**



“Hiscox Bermuda continues to build a worldwide book of catastrophe business and to reinsure selected parts of the rest of the group. Its external written premium income increased to £121.2 million (2006: £65.2 million) with a combined ratio of 99.1% (2006: 93.7%) caused by the losses from Windstorm Kyrill and the UK’s June floods set against modest first half-year earned income.

Again, if competition continues, Bermuda may, like Global Markets, reduce its income next year.”

— **Robert Hiscox, Chairman, Hiscox**



“The UK is one of our largest exposure zones and consequently we were impacted by the floods at the end of this quarter. This, together with flood losses in Australia, produced a disappointing result viewed on a quarterly basis. However, this is in the nature of the volatile business we underwrite and we continue to be pleased with the franchise we are building for the long term.”

— **Flagstone CEO David Brown** on a rough Q2 that saw net earnings down 53%



“This is our sixth consecutive quarter with operating income in excess of \$100 million, and annualised operating income and net income return on average equity in excess of 20%. Enhancing strong underwriting performance ... we continue to reap the benefits of historically strong operating cash flows and significant investment income momentum.”

— **Allied World President & CEO Scott Camilani**



One very highly rated market

STANDARD & POOR’S ENDORSES LOCAL COMPANIES WHILE BEST CONFIRMS OUR WORLD-CLASS CREDENTIALS

Bermuda’s leading insurers have been given a major vote of confidence by ratings agency Standard & Poor’s. In a new FAQ about the financial strength of locally based enterprises, S&P said that our 17 A-rated companies have a strong ability to pay claims and that overall the sector’s financial position is “very healthy”.

S&P credit analyst Thomas Upton noted that “following a year in which there were no material losses attributable to tropical storms in the Atlantic, we’ve made a couple of ratings changes on Bermuda reinsurers in early 2007”. The report details those changes as well as responding to “parties who follow the industry and have repeatedly raised several questions.”

Tokio Millennium Re and Top Layer Re received AA ratings while Everest Re, XL Capital, Hannover Re Bermuda, and PartnerRe were awarded AA- ratings and ACE, XL Capital Ltd

and Renaissance were rated A+.

S&P said it did not expect any of the top-rated firms to default in the event of similar disasters to 2005, which included Hurricanes Katrina, Rita and Wilma. The agency noted that only one company — Quanta — had gone into run-off and that other companies which suffered huge losses had successfully accessed new capital.

It added that, despite upgrades to catastrophe models over the past two years to reflect more frequent

and more intense storms, the industry had developed its own modelling and underwriting capabilities.

S&P said the sector had used traditional forms of reinsurance to transfer risk to the capital markets as well as developing more diverse portfolios that were less concentrated on catastrophe risk. But it also noted that companies with a high tolerance for risk — those willing to accept the volatility that goes with a highly concentrated

book of business — should be compensated with long-term average returns above the norm.

S&P added that it expects a well-conceived strategy to be flexible enough to accommodate a broad range of market conditions. “Within that strategy, a variety of tactics may be tried to deal with any contingencies that arise and a good management team will adapt to those short-term situations without abandoning its basic strategy.”

Doing pretty well in the premier league

This year’s A M Best list of the world’s top reinsurers provided further evidence of Bermuda’s growing importance. In all, 15 companies either headquartered in Bermuda or with a presence on the island, featured in the top 35, according to the ratings agency. The rankings are based on consolidated gross premiums written in 2006.

Hannover Re (fourth), **Everest Re Group** (seventh) and **PartnerRe Group** (tenth) made the top 10 while **XL Capital** finished out of the top 10 for the first time in five

years, but only just. It was rated eleventh.

Scottish Re, Renaissance Re, ACE, Endurance Specialty Insurance, Arch Reinsurance, White Mountains Re, Axis Capital Holdings, Platinum Underwriters Group, Aspen Insurance, Montpelier and **Allied World** also featured in the list.

Everest Re recorded its best ever position, climbing three places from 2006 with a gross premium total of \$4 billion. **PartnerRe** cracked the top ten after posting gross premiums of \$3.7 billion.

Undisputed champ

Bermuda is still way ahead of the competition when it comes to the reinsurance market, according to a Reinsurance Association of America report. Premiums ceded to the island's affiliated reinsurers grew from \$8.8 billion in 2002 to \$18.5 billion in 2006. Switzerland came second with \$8 billion last year while Germany and the Cayman Islands saw declines of \$4 billion and \$500 million respectively over the five-year period.

JLT buys Park

BERMUDA'S BIGGEST BROKER IS BORN, REPORTS CHRIS GIBBONS



Jardine Lloyd Thompson has acquired Park (Bermuda) in an \$11.8 million deal that will form Bermuda's largest broking firm. Park has been combined with JLT's existing Bermuda broking operation and will trade as JLT Park. The combined business will have about 40 staff, and JLT Park says it expects to place in excess of

\$400 million of premium in the Bermuda market each year.

Park, one of the leading independent insurance brokers in Bermuda, has been in operation since 1989. Its issued share capital is being acquired by JLT Risk Solutions (Bermuda) from the Park Group, a portfolio company of SunTx Capital Partners, for a

maximum cash consideration of \$11.8 million, of which \$8.85 million is an initial payment with the rest based on future performance.

Paul Scope, Chairman & CEO of the Park Group and Mark Simons, Managing Director of Park (Bermuda), will join the board and executive management team of JLT Park. John English, the current Chairman & CEO of JLT Risk Solutions (Bermuda), will continue in this role for the newly combined operation, while Mr Scope will become President.

Mr English said the new entity would be "dedicated to servicing the needs of independent regional and national brokers who seek access to the Bermudian market. The merged operation will have unparalleled strength and depth in Property & Casualty and Financial & Professional lines."

Mr Scope told *The Royal Gazette*: "The two companies had been in competition for a number of years but it was always a very respectful competition. They have been our biggest competitor since we set up in 1989."

The deal marks another chapter in Mr Scope's remarkable career since arriving in Bermuda in 1983 from the UK. After working for Harnett & Richardson and Freisenbruch-Meyer Management Services offering local insurance to banks, hotels and homeowners, he seized the opportunity presented by the establishment of ACE and XL and formed his own brokerage, Park International.

Park International was bought by MRM in 1992 before merging with H&H five years later. The firm became Park (Bermuda) as part of the Park Group after MRM was taken over by creditors, and was bought out by SunTX Capital Partners in 2003.

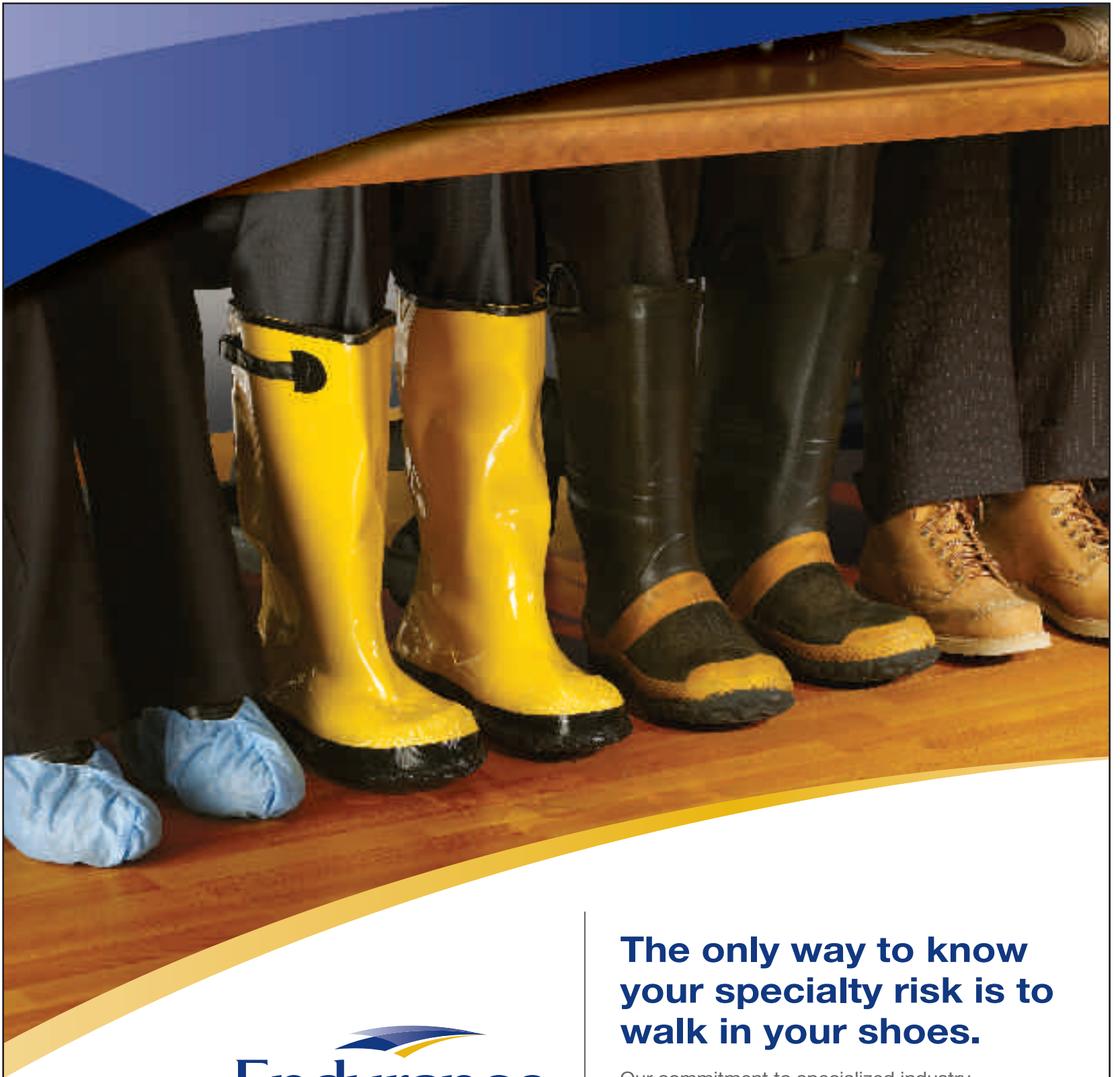
'They have been our biggest competitor'

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Ja-Ann Pully
[pictured with daughter Ri-Ann]
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Dean losses deemed 'manageable'

LUCKY BREAK FOR POPULATION AREAS AND REINSURERS

Bermuda reinsurers breathed a sigh of relief after they avoided a potentially disastrous first major Atlantic storm of the year. Insured losses from Hurricane Dean, which swept across the Caribbean and Mexico's Yucatan peninsula in late August, are expected to be manageable for the insurance industry, according to Fitch Ratings. Despite being the first Category 5 Atlantic storm since Andrew in 1992, Dean's 160-mph winds missed heavily populated areas like Cancun and Cozumel.

Fitch said preliminary estimates ranged from \$750 million to \$2 billion and noted: "It could have been much worse but, fortunately, Dean made landfall in a relatively rural portion of Mexico, missing most population and tourist centres." Fitch also indicated that it expected a "substantial portion of the insured loss to be borne by global reinsurers who typically have significant financial strength".

Risk modelling firm RMS estimated losses at between \$750 million and \$1.5 billion with up to \$300 million of insured losses expected in Mexico while the most costly damage occurred earlier in Jamaica.

Hurricane Dean won't trigger an insurance pool set up earlier this year by Caribbean countries and the World Bank that provides emergency cash to islands in case of natural disaster. Dean, which killed at least 20 people and did extensive damage to bananas and other crops, failed to surpass wind speed and other thresholds to prompt payments from the Caribbean Catastrophe Risk Insurance Facility, said fund supervisor Simon Young of Washington-based Caribbean Risk Managers. "Had the storm been 30 miles to the north that would have triggered immediate payment in Jamaica," he added.

The fund, which the World Bank says is one of a kind, lets countries pool their risk to reduce individual premiums by 40%.

Nations pay annual premiums from \$200,000 to \$2 million and are eligible for disaster payouts of \$10 million to \$50 million.

Mr Young said the 15-nation Caribbean Community and Bermuda purchased deductibles that were fixed to pay out for a 20-year hurricane or earthquake. "By our estimation, Dean was a one-in-10 year event," he added.



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US moves MUSIC to Montpelier's ears



Anthony Taylor: "significant vote of confidence"

AMERICAN OPERATIONS GAIN MOMENTUM

Bermuda-based Montpelier Re has announced two further developments in establishing a presence in the US.

Montpelier Underwriting Inc (MUI), the company's wholly owned US managing general agent, has been granted coverholder approval by Lloyd's to introduce business to Montpelier Syndicate 5151. Montpelier said Hartford,

Connecticut-based MUI will be the centrepiece of its growing US insurance and reinsurance underwriting platform. The first binder granted to MUI by Syndicate 5151 is for property brokerage facultative reinsurance business. This division of MUI will be headed by former Wellington Underwriting executive Paul Keefe as Senior Vice President.

Meanwhile, Montpelier US has entered into a stock purchase agreement for the acquisition of General Agents Insurance Company of America, Inc. for around \$4.75 million. It is a licensed admitted insurer in Oklahoma and is authorised as an excess and surplus lines insurer in 37 states.

Upon closing, Montpelier US will rename the company Montpelier US Insurance Company (MUSIC). MUSIC will write primarily excess and surplus line insurance in the continental US, and its underwriting operations will be based in Scottsdale, Arizona.

Anthony Taylor, Chairman & CEO of Montpelier Re, said: "MUI's attainment of approved coverholder status successfully completes Montpelier's entrance into the Lloyd's market and represents a significant vote of confidence by Lloyd's in the quality of [MUI's] management team. The acquisition of General Agents Insurance Company, meanwhile, will allow us to write specialist areas of E&S business traditionally written by US insurance entities rather than through Bermuda or London insurers. The combination of these activities represents another portion of Montpelier's strategic expansion. Our growing US trading platform will allow Montpelier to diversify its portfolio while remaining within its core competency of underwriting primarily short-tail business."

Max splashes out

Max Specialty Insurance Co, the excess and surplus lines division of Bermuda-based Max Capital Group, has launched a new unit focused purely on US marine risks. Michael Miller, former SVP & CUO of Fireman's Fund Insurance Co's specialty business unit, and a former Chairman of the Inland Marine Underwriters Association, will be the CUO, based in New York City.



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Cat trade milestone

BERMUDA'S ASCENDANT TAKES FIRST STEP ON NYMEX

The beginning of what is expected to be a growing trend — catastrophe risk trades on the New York Mercantile Exchange (NYMEX) — took place in August. GFI Group brokered the swap between Swiss Re and Bermudian reinsurer Ascendant. The trade was an option on a nationwide catastrophe risk futures contract.

Catastrophe derivatives enable tailored trading and hedging of combinations of risks. GFI said the inaugural trade was based on the Re-Ex Index, which is calculated by Gallagher Re, a reinsurance intermediary and advisory firm.

Albert Selius, head of the insurance-linked securities trading desk at Swiss Re Capital Markets, said: “We are always looking to trade cat risk in the best format. We wel-

come the NYMEX initiative as it provides an alternative platform for natural catastrophe trading in addition to the traditional industry loss warranties market.”

Rick Pagnani, President & CEO of Ascendant, said: “We are happy to have participated in the inaugural trade but, more importantly, we are excited at the prospects for this market. These cat derivative contracts add a new dimension to risk management and give (re)insurers and capital market participants alike a new way to enhance risk-adjusted returns.”

Ian Clague, GFI's Head of Commodity Broking for the Americas, noted: “We are seeing financial institutions starting to trade and manage reinsurance, and derivatives are making this more standardised and accessible.”



“In order to remain competitive in today's marketplace, Bentham, I'm afraid we're going to have to replace you with a sleazeball.”

Billion dollar questions

What effect will emerging markets such as China and Dubai have on Bermuda and the global reinsurance industry, and how much more business can the already saturated Bermuda market sustain? Those will be among the topics at this year's Hawksmere International Reinsurance Congress, due to be held at the Fairmont Hamilton Princess on October 3 to 5. For more details, email lisa.potterton@hawksmere.co.uk.

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PartnerRe steps up for Irish rejig

EUROPEAN AND CANADIAN OPERATIONS TO BE CONSOLIDATED IN DUBLIN

Bermuda-based reinsurer PartnerRe is to centralise its European and Canadian businesses in Ireland. The company announced that from January 1, 2008, Partner Reinsurance Europe, a wholly owned subsidiary of PartnerRe, to be based in Dublin, will be the principal reinsurance carrier for PartnerRe's business underwritten in France, Ireland, Switzerland and Canada.

Under the new European Union Reinsurance Directive, Partner Reinsurance Europe will be able to operate in all EU member states

under a single regulatory framework. Ireland was the first of the EU's 27 members to incorporate the directive into its national law.

PartnerRe said its clients would continue to benefit from the company's financial strength, underwriting capabilities and business unit structure following the move.

Partner Reinsurance Europe, which will be capitalised in excess of \$1 billion, has received provisional ratings in line with those of the rest of PartnerRe's operating subsidiaries: A+ from A M Best and AA- from Standard & Poor's.

Ariel wins Atrium

Bermuda-based Ariel Holdings is set to snap up Lloyd's of London specialist insurer Atrium Underwriting in a \$396.7 million deal. Ariel, founded in 2005 and headed by former ACE executive Don Kramer (below), provides property, marine, energy and aviation reinsurance as well as selected specialty lines of insurance.

Atrium provides war and terrorism insurance for the aircraft and shipping sectors. In 2006, it earned pretax profits of £44.7 million, up 347% from the previous year, on reported gross written premiums of £152 million.

Mr Kramer said: "Atrium [has] a high quality underwriting and management team and a long track record of achieving strong performance under challenging market conditions. Atrium's diversified mix of property and casualty business and access to the Lloyd's market make it a highly complementary addition to Ariel. We look forward to welcoming the employees of Atrium and to working with them to continue the momentum Atrium has built with its customers and partners across the Lloyd's market."



ACE active in Bahrain

The ACE Group has received the go-ahead from the Central Bank of Bahrain to underwrite commercial property and casualty insurance and reinsurance in the Gulf state. ACE has an established representative office in Manama, Bahrain's capital. Its property and casualty business will operate from the same location. The new business will write both domestic Bahraini business and facultative reinsurance throughout the Middle East and North Africa region.



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Merger launches Argo

'OUR COLLECTIVE GOAL FROM DAY ONE IS TO DELIVER ENHANCED SHAREHOLDER VALUE'

Texas-based Argonaut Group and Bermuda-headquartered PXRE Group have completed their merger. The new company is called Argo Group International Holdings and is the new Bermuda holding company for subsidiaries Argonaut, Peleus Reinsurance and the former PXRE. The company's new stock ticker symbol is AGII and it will underwrite specialty insurance and reinsurance products in the property and casualty market.

Argo Group President and CEO Mark Watson stated: "Our collective goal from day one at the new Argo Group is to deliver enhanced shareholder value. We intend to accomplish that by building upon the successes realised by Argonaut Group and PXRE Group and utilising our combined strength to deploy capital in selected areas to produce maximum return and continued growth."

There are 13 directors of Argo Group, nine of whom are former Argonaut directors. San Antonio businessman Gary Woods has been elected Chairman. Former PXRE President & CEO Jeff Radke will serve as a consultant to Argo Group, which has preliminary unaudited assets of \$5 billion, liabilities of \$3.7 billion and shareholders' equity of \$1.3 billion.

Flagstone makes two Cayman Island deals

Bermuda-based Flagstone Reinsurance Holdings has taken a majority position in Island Heritage Holdings, a Cayman-domiciled company specialising in insurance and insurance services in the Caribbean, which is part owned by Bermuda firms Butterfield Bank and ACE Insurance.

Flagstone said Butterfield and ACE would remain major shareholders of Island Heritage, with further participation by the local management of the companies. Flagstone Chairman Mark Byrne will become Island Heritage's Chairman.

Flagstone has also entered into an excess-of-loss retrocessional agreement with Monte Gele, a new Cayman-based single purpose vehicle. Monte Gele financed the transaction through the issuance of catastrophe bonds, according to Flagstone Re.



"Do you think now that we're doing fewer illegal things we can scale back the legal department?"



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INSURANCE/REINSURANCE



ACE into energy, construction

GROWING INTERNATIONAL REQUIREMENTS SPARK NEW ENTERPRISES

ACE Overseas General has formed two new international industry practice groups to serve growing needs in regional commercial construction and energy production.

VP David Walters, based in London, will lead ACE International Construction, reporting to Paul McNamee, SVP & Head of International Property.

The new group will offer a broad range of insurance lines for private and public sector construction risks and will have on-the-ground regional operations in the UK, Continental Europe, Asia Pacific, the Middle East and Latin America.

Meanwhile, ACE Energy & Technical Risks will offer upstream and downstream oil and

gas as well as power generation property insurance lines in the UK, Continental Europe, Asia Pacific, the Middle East and Latin America. It will be co-led by Roger Giddings, EVP & Head of ACE Global Energy, and Mr McNamee. Eric Boquist, SVP, Head of Underwriting Operations, ACE Global Energy, will serve as CUO of the new group.

Introducing SWBC RE

San Antonio-based Southwest Business Corporation has formed a Bermuda reinsurance company, SWBC RE. SWBC said the move followed tremendous growth over the past three years and the need to enhance its products and services.

Chairman Charlie Amato said: "We have offices in 27 states across the country and now in Bermuda. SWBC chose Bermuda because it's the most reputable location."

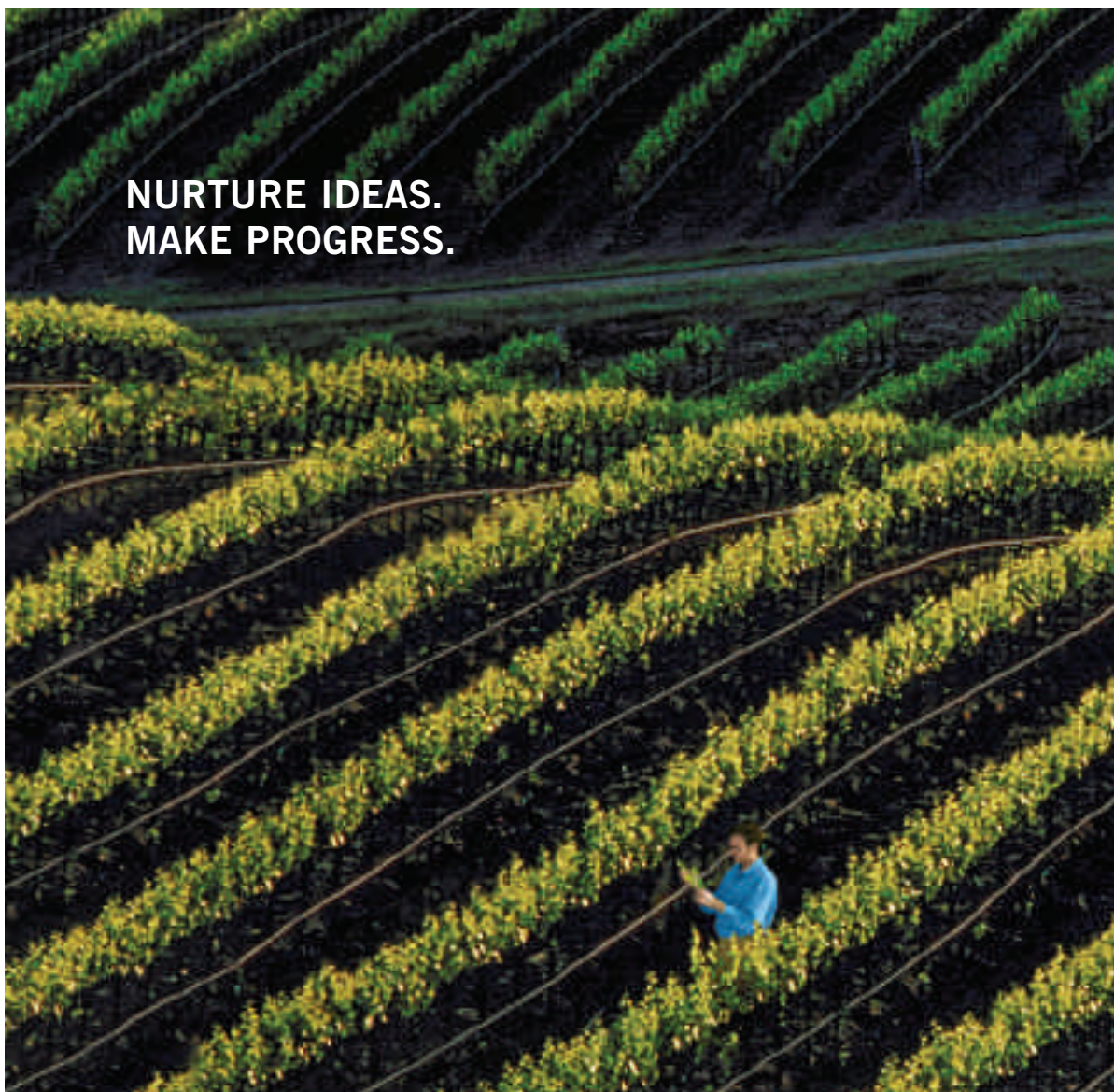
SWBC RE will be reinsuring business from a variety of insurance partners and companies. The first products to be reinsured are contractual liability contracts associated with the sale of debt protection by financial institution clients.

Explaining the inexplicable

The Reinsurance Association of America is bringing a version of its popular seminar, *Demystifying Reinsurance*, to Bermuda for the first time. *Bermuda ReBasics*, which is being organised in conjunction with the Bermuda Insurance Institute, will be staged at the Fairmont Hamilton Princess Hotel on January 16 and 17, 2008.

The seminar aims to provide "a thorough understanding of the structure and purpose of reinsurance and an introduction to life reinsurance. Attendees will be guided through all steps of understanding the reinsurance transaction and its impact on an insurance company's bottom line, with an emphasis on the concerns and perspective of Bermuda insurers and reinsurers." For more information, email hocutt@reinsurance.org.

Quanta's \$54.5m buy Bermuda-based Quanta Capital Holdings has announced the purchase of all the outstanding floating rate capital securities of Quanta Capital Statutory Trust I and II for approximately \$54.5 million as part of its run-off plan. Quanta originally issued and sold \$60 million of these securities in private placements. "They constituted the only long-term indebtedness for borrowed money on the company's balance sheet," said a spokesman.



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'Managing' terrorism

THE PRIVATE INTELLIGENCE AGENCY THAT PRIDES ITSELF ON PICKING GOOD RISKS

Accurately forecasting future terrorist attacks might seem a risky business — but for global companies such as Bermuda's reinsurers, operating without paying attention to terrorism is even riskier. An increasing number of them are using the services of organisations like Exclusive Analysis, a London-based "strategic intelligence company" that forecasts political and violent risk around the world.



Mike Bookman

CEO Simon Sole, an intelligence analyst and veteran Al Qaeda watcher, founded Exclusive Analysis five years ago after consulting to the insurance industry pre-9/11. He says: "Today, successful global companies must operate and compete internationally against a backdrop of terrorism. [We] enable clients to make profitable long-term investment and risk management decisions."

Mike Bookman, who leads the company's financial services and investment intelligence team, told us Bermuda is an increasingly important market for Exclusive Analysis. "We have a large footprint in the insurance industry and work with eight of the top 10 Lloyd's syndicates," he explained on a recent visit to the island. "We have a number of clients in Bermuda, mostly reinsurance. Most of the terrorism business

that comes here we will have taken a look at."

Mr Bookman said Exclusive Analysis prides itself and being objective and independent. "We have developed a proprietary methodology for serving the industry that can save insurers from bad claims and build their book of business. We don't broke any business and we're not out to dissuade people from underwriting



"Would you please elaborate on 'then something bad happened'?"

risk but our intelligence helps companies promote business in new areas and new lines. In a recent audit, we 'encouraged or strongly encouraged' underwriting 70% of the risks on which we were asked to give advice. Among those 70%, we have yet to see a claim. It's a pretty good track record."

Meanwhile, the company has recently launched a new risk assessment tool, TerrorRisk, in conjunction with Pitney Bowes MapInfo. TerrorRisk combines MapInfo's geographical detail with Exclusive Analysis's intelligence and historical data. TerrorRisk rates more than 3,700 global points of interest across 40 target types.

'In a recent audit, we "encouraged or strongly encouraged" underwriting 70% of the risks on which we were asked to give advice. Among those 70%, we have yet to see a claim'

Too much regulation is the biggest risk facing insurers around the world but it is much less of a concern here, according to a survey of senior executives' "insurance banana skins" compiled by the Centre for the Study of Financial Innovation in association with PricewaterhouseCoopers. Bermuda re/insurers polled in the survey cite "managing the underwriting cycle" as their number one concern.

At a time of softening across the global re/insurance markets, Bermuda companies are tightly focused on all aspects of capital management. As well as managing the cycle, items at the top of their agenda are capital and reinsurance availability, risk management and the pricing of new risks.

Outside Bermuda, senior executives place cycle management in

INSURANCE BANANA SKINS

BERMUDA'S CONCERNS DIVERGE FROM OTHER KEY PLAYERS', SURVEY REVEALS

fifth place after climate change, management quality, natural catastrophes and too much regulation. The findings suggest that Bermuda companies, many of which specialise in cat business, are more

comfortable than their global competitors with their risk management and modelling capabilities.

It also appears that Bermuda companies are not suffering the same level of shortage of intel-

tual capital — management quality does not feature as a perceived threat to their business, compared with the overall survey where the issue is placed at number three.

PwC Insurance Partner Colm Homan commented that Bermuda executives' top 10 banana skins reflect Bermuda companies' concentration on specialist business and on maintaining their relationships with capital providers. "That's why Bermuda companies are focused on underwriting performance through the cycle and on protecting their capital while delivering attractive returns to shareholders," he says.

BERMUDA BANANA SKINS 2007

- Managing the cycle
- Capital availability
- Availability of reinsurance
- Risk management techniques
- Pricing new risks
- Security of reinsurance
- New types of competitors
- Natural catastrophes
- Climate change
- Pollution

GLOBAL BANANA SKINS 2007

- Too much regulation
- Natural catastrophes
- Management quality
- Climate change
- Managing the cycle
- Distribution channels
- Long tail liabilities
- Actuarial assumptions
- Longevity assumptions
- New types of competitors

OPERATING RATIOS

QUARTERLY LOSS RATIOS

	Q2 2007	Q2 2006	Q2 2005
ACE	61.4%	61.6%	64.4%
Arch	56.6%	58.0%	60.0%
Aspen	60.5%	52.2%	49.6%
Allied World	58.1%	58.9%	67.5%
Axis	51.7%	54.8%	51.7%
Endurance	49.6%	66.3%	52.3%
Everest Re	62.0%	60.9%	63.2%
IPC	88.2%	13.3%	28.1%
Max Re	69.8%	72.5%	71.9%
Montpelier	38.8%	43.2%	35.9%
PartnerRe	54.9%	61.4%	60.7%
Platinum	55.6%	55.6%	55.8%
Renaissance Re	38.7%	48.1%	32.1%
White Mtn	61.6%	80.1%	60.4%
XL Capital	56.9%	62.0%	72.0%

QUARTERLY EXPENSE RATIOS

	Q2 2007	Q2 2006	Q2 2005
ACE	26.2%	26.6%	25.8%
Arch	27.5%	28.3%	29.3%
Aspen	27.9%	29.4%	27.0%
Allied World	21.9%	19.3%	18.8%
Axis	23.7%	23.5%	22.8%
Endurance	29.4%	30.8%	29.6%
Everest Re	27.2%	26.8%	28.1%
IPC	17.4%	17.7%	16.3%
Max Re	25.8%	17.2%	14.9%
Montpelier	31.2%	29.7%	28.7%
PartnerRe	30.8%	28.9%	28.7%
Platinum	25.2%	27.9%	28.4%
Renaissance Re	24.0%	24.1%	20.4%
White Mtn	41.9%	34.9%	39.7%
XL Capital	29.4%	28.0%	25.9%

QUARTERLY COMBINED RATIOS

	Q2 2007	Q2 2006	Q2 2005
ACE	87.6%	88.2%	90.2%
Arch	84.1%	86.3%	89.3%
Aspen	88.4%	81.6%	76.6%
Allied World	80.0%	78.2%	86.3%
Axis	75.4%	78.3%	74.5%
Endurance	79.0%	97.1%	81.9%
Everest Re	89.2%	87.7%	91.3%
IPC	105.6%	31.0%	44.4%
Max Re	95.6%	89.7%	86.8%
Montpelier	70.0%	72.9%	64.6%
PartnerRe	85.7%	90.3%	89.4%
Platinum	80.8%	83.5%	84.2%
Renaissance Re	62.7%	72.2%	52.5%
White Mtn	103.5%	115.0%	100.1%
XL Capital	86.3%	90.0%	97.9%

FINANCIAL STRENGTH RATINGS

A M BEST RATING

June 30, 2007 June 30, 2006

S&P RATING

June 30, 2007 June 30, 2006

	June 30, 2007	June 30, 2006	June 30, 2007	June 30, 2006
ACE	A+	A+	A+	A+
Arch	A	A-	A	A-
Aspen	A-	A-	A	A
Allied World	A	A	A-	NR
Axis	A	A	A	A
Endurance	A-	A-	A	A-
Everest Re	A+	A+	AA-	AA-
IPC	A	A	A-	A
Max Re	A-	A-	NR	NR
Montpelier	A-	A-	A-	A-
PartnerRe	A+	A+	AA-	AA-
Platinum	A	A	NR	NR
Renaissance Re	A	A	A+	A+
White Mtn	A-	A-	A-	A-
XL Capital	A+	A+	A+	A+

NR — Not rated by S&P

Q2 ANALYSIS / PRICewaterhouseCOOPERS

News and notes

General

● The Q2 results do not reflect recent market activity relating to US sub-prime mortgages. This is expected to affect Q3 for some companies, both in valuation of investments and potential exposure to loss in professional D&O coverage. Stock price movements across the peer group in July and August have resulted from this uncertainty.

Renewals

● June renewals were encouraging with the impact of Florida's Hurricane Cat Fund offset to an extent by demand for private reinsurance.

● Trends continue to be affected by conversion of QS cover into excess of loss/straightforward catastrophe cover as well as higher retentions and increased reinsurance purchases.

Earnings

● Despite the lack of premium growth, most companies continued to exceed earnings estimates due to better than expected current year

combined ratios as well as prior year reserve releases. Full-year guidance has been revised upwards for many companies.

● Flooding in the UK and Australia impacted loss ratios although, as noted above, these were generally offset by prior year reserve releases and low non-catastrophe losses. Further flooding in the UK in July is expected to impact Q3 results similarly.

● Investment income contributed significantly to the results due to increases in rates and contributions from hedge fund income.

Capitalisation

● Price to book trends over the last three years indicate that diversified companies show a less volatile ratio than specialist players. Also, Bermuda companies have tended to show a lower ratio than US ones.

● Share buy-backs are continuing as the favourable earnings are leading to increased focus on capital management.

GROSS PREMIUMS WRITTEN \$M

	Q2 2007	Q2 2006	Q2 2005
ACE	4,637	4,583	4,213
Arch	1,102	1,136	941
Aspen	504	522	549
Allied World	531	518	442
Axis	959	995	767
Endurance	507	451	403
Everest Re	935	910	1,109
IPC	109	120	87
Max Re	242	284	245
Montpelier	188	296	276
PartnerRe	908	818	767
Platinum	294	330	429
Renaissance Re	846	743	443
White Mtn	1,046	1,094	1,097
XL Capital	2,231	2,296	3,966

NET PREMIUMS EARNED \$M

	Q2 2007	Q2 2006	Q2 2005
ACE	3,008	2,906	2,921
Arch	751	797	740
Aspen	451	429	395
Allied World	303	306	332
Axis	694	679	624
Endurance	418	407	438
Everest Re	999	893	1,093
IPC	99	101	87
Max Re	138	199	192
Montpelier	129	151	227
PartnerRe	889	859	880
Platinum	296	337	431
Renaissance Re	358	431	339
White Mtn	961	954	943
XL Capital	1,930	1,985	3,713

QUARTERLY EARNINGS DATA

	Net income attributable to common shareholders (\$m)			Fully diluted earnings per share (\$)		
	Q2 2007	Q2 2006	Q2 2005	Q2 2007	Q2 2006	Q2 2005
ACE	649	573	467	1.93	1.72	1.58
Arch	199	138	126	2.65	1.81	1.69
Aspen	115	102	84	1.19	1.01	1.16
Allied World	123	102	72	1.96	2.02	1.41
Axis	252	223	173	1.51	1.37	1.13
Endurance	131	60	110	1.85	0.85	1.67
Everest Re	283	220	194	4.45	3.38	3.40
IPC	24	104	64	0.37	1.50	1.32
Max Re	94	20	23	1.45	0.31	0.47
Montpelier	51	58	109	0.53	0.62	1.62
PartnerRe	96	69	151	1.66	1.20	2.72
Platinum	88	79	68	1.34	1.24	1.39
Renaissance Re	183	130	172	2.53	1.81	2.39
White Mtn	103	116	147	9.49	10.72	13.64
XL Capital	545	377	136	3.00	2.10	0.97

CUMULATIVE YTD EARNINGS DATA

	Net income (loss) attributable to common shareholders (\$m)			Fully diluted earnings (loss) per share (\$)		
	Q2 2007	Q2 2006	Q2 2005	Q2 2007	Q2 2006	Q2 2005
ACE	1,350	1,062	904	4.02	3.18	2.98
Arch	398	267	242	5.24	3.52	3.26
Aspen	237	164	154	2.46	1.61	2.13
Allied World	237	200	136	3.81	3.96	2.68
Axis	479	419	955	2.88	2.56	1.84
Endurance	229	163	206	3.22	2.29	3.11
Everest Re	580	389	361	9.05	5.96	6.33
IPC	97	163	108	1.48	2.36	2.23
Max Re	174	95	61	2.70	1.49	1.22
Montpelier	124	97	183	1.29	1.07	2.73
PartnerRe	257	254	254	4.42	4.40	4.56
Platinum	158	154	141	2.42	2.40	2.88
Renaissance Re	374	309	216	5.16	4.31	3.00
White Mtn	195	212	323	18.03	19.61	29.94
XL Capital	1,094	836	579	6.06	4.64	4.14

MARKET CAPITALISATION

	Q2 2007		Q2 2006		Q2 2005	
	Common shares issued	Market value	Common shares issued	Market value	Common shares issued	Market value
ACE	329,009,343	62.52	325,371,481	50.59	288,073,439	44.85
Arch	71,273,285	72.54	73,937,973	59.46	35,262,005	45.05
Aspen	88,544,590	28.07	95,250,401	23.29	69,329,931	27.56
Allied World	60,405,307	51.25	50,162,842	N/A	50,162,842	N/A
Axis	147,924,000	40.65	149,809,873	28.61	140,668,032	28.30
Endurance	64,591,095	40.04	66,096,340	32.00	59,924,687	37.82
Everest Re	63,198,640	108.64	64,948,041	86.57	56,400,339	93.00
IPC	60,659,489	32.29	63,700,000	24.66	48,400,000	39.62
Max Re	60,127,859	28.30	59,425,278	21.84	46,099,712	22.90
Montpelier	103,067,067	18.54	107,875,959	17.29	63,327,564	34.58
PartnerRe	57,079,534	77.50	56,799,778	64.05	54,643,295	64.42
Platinum	60,077,313	34.75	59,546,050	27.98	43,406,788	31.82
Renaissance Re	72,266,000	61.99	71,849,000	48.46	71,113,584	49.24
White Mtn	10,842,538	606.02	10,780,053	487.00	10,774,373	630.90
XL Capital	181,884,099	84.29	180,394,236	61.30	140,389,078	74.42

SHAREHOLDERS' EQUITY (\$M)

	Q2 2007	Q2 2006	Q2 2005
ACE	15,184	12,466	10,499
Arch	3,704	3,016	2,503
Aspen	2,591	2,154	1,608
Allied World	2,418	1,565	1,757
Axis	4,694	3,819	3,167
Endurance	2,380	1,937	1,987
Everest Re	5,338	4,379	4,082
IPC	1,965	1,741	1,743
Max Re	1,473	1,212	1,025
Montpelier	1,541	1,256	1,463
PartnerRe	3,937	3,210	3,482
Platinum	1,991	1,639	1,273
Renaissance Re	3,460	2,539	2,823
White Mtn	4,575	3,864	4,092
XL Capital	11,522	8,547	8,372

BF&M backed by Best

REWARDED FOR GENERAL STRENGTH AND MOVES TO DIVERSIFY OUTSIDE BERMUDA

AM Best has affirmed the FSRs of A and assigned ICRs of a to Bermuda-based BF&M and its operating affiliates. The outlook for all ratings is stable. “The ratings recognise BF&M’s consistent operating performance, long-standing participation in life and non-life insurance in Bermuda, strong capitalisation and

experienced and focused management as well as its recent efforts to diversify its book of business outside of Bermuda,” said Best.

CRC (Bermuda) Reinsurance

Best has upgraded the FSR to A from A- and ICR to a from a- of CRC (Bermuda) Reinsurance. CRC is a direct wholly owned sub-

siary of Toronto-based Fairfax Financial Holdings. The outlook for both ratings is stable.

Renaissance Re Holdings

Standard & Poor’s has assigned its preliminary A- senior debt, BBB+ subordinated debt, BBB junior subordinated debt and BBB preferred stock ratings to Renaissance

Re Holdings’ recently filed S-3 \$750 million universal shelf registration. S&P said it “does not expect any potential issuances under the shelf to lead to a material change in the group’s financial leverage”, which remains within its expectations.

Arch Reinsurance

Best has affirmed the FSRs of A and the ICRs of a for Arch Reinsurance and its reinsured affiliates. Best also has affirmed the ICR of bbb- of Arch Capital Group (US). The outlook for all ratings is stable.

AXIS Specialty

Best has affirmed the FSRs of A and upgraded the ICRs to a+ from a for AXIS Specialty and its operating affiliates. The outlook for all ratings is stable.

Max Capital Group

Fitch has affirmed the A- issuer default rating of Max Capital Group and the insurer financial strength ratings of its insurance subsidiaries, Max Bermuda, Max Re Europe, Max Insurance Europe and Max Specialty Insurance Co, as well as the A- IDR and BBB+ senior debt rating of Max USA Holdings, a direct, wholly owned holding company subsidiary of Max Capital.



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The storm that saves...

REN RE'S WALL OF WIND COULD ASSIST IN CUTTING LOSSES BY 10%, SAYS WILLIAM RIKER

By Chris Gibbons

Bermuda catastrophe reinsurer Renaissance Re has been helping to create a storm in Florida — all in the name of hurricane research. The company has spent \$1 million in partnership with the State of Florida to create a “wall of wind” machine which is aimed at improving building design to better withstand hurricane-force storms.

Originally built as a two-fan machine in 2005, the system now consists of six powerful giant fans stacked 16 feet high in front of a full-scale model single-storey house on a field at Florida International University, home to the International Hurricane Research Centre (IHRC).

The machine is capable of delivering 140 mph winds — the equivalent of a Category 5 storm — and scientists hope it will help them discover which products and techniques work against hurricane winds, and whether hurricane building codes really protect homeowners. Previously, research had largely been confined to miniature models in wind tunnels. Eventually, the IHRC hopes to have a specially-housed 24-fan unit that will be able to batter two-storey model buildings.

US losses from hurricanes in 2004 and 2005 were more than \$150 billion with about \$82 billion covered by insurance. In a recent report on the wall of wind in the *Wall Street Journal*, Ren Re President William Riker claimed research could cut property losses by 10%.

The storms of 2004/5 have created havoc with insurance markets in states vulnerable to hurricanes, according to the *WSJ*. Insurers have been raising premiums and limiting the policies sold in coastal areas while state governments are pressuring insurers to give better deals to homeowners and businesses who take steps to reduce their risk to hurricane damage by reinforcing their properties with meas-



Ren Re's wall of wind in Florida: experiments will help decide what works and what doesn't in hurricane conditions. Inset: effects of the test wall's fans

ures such as storm shutters and impact-resistant glass.

However, whether these so-called improvements are truly effective is not fully known as the science of understanding how hurricanes damage buildings is relatively new. Hence the need for research like the wall of wind. As Mr Riker told the *WSJ*: “You’re never quite sure what failed first. Nobody stands outside in a hurricane and watches how a building falls apart.”

The machine is part of what the IHRC said will be “an innovative research capability in full-scale structural testing to determine inherent weaknesses of structures when subjected to categories 1 to 5 hurricane-force winds and rain, leading to new technologies, designs and products. This new wall of wind testing facility, the first of its kind, will revolutionise building construction and retrofitting practices.”

In the same way car crash tests changed automotive safety through the introduction of seat belts and air bags, the IHRC has high hopes for the wall of wind in affecting the housing industry.

It says full-scale destructive testing will change the public’s

perception of building safety and will lead to the development of a “culture of preparedness” — a change in public attitude that Florida Governor Jeb Bush has said must happen for the state’s economy to remain sustainable.

Arindam Chowdhury, Lead Wind Engineer at IHRC, wrote in a recent paper for risk modelling firm AIR: “The new facility can simulate holistic, full-scale effects of hurricane-force winds in an environment that is at once controllable, programmable and repeatable. Full-sized buildings — such as site-built or manufactured housing and small commercial structures — can be tested. Because

it eliminates scaling issues, the wall of wind can measure accurate wind loads in the presence of rain, and monitor performance levels and progressive damage of structures at various wind levels. In conjunction with a debris gun, it can simulate the effects of wind-borne missiles.

He added: “Test results will inform the development of new techniques to enhance the resilience of coastal buildings against windstorms. Research goals include the design of water-tight soffits, vortex suppression techniques to reduce roof damage, and mitigation strategies to prevent roof-top equipment failure.”



“It’s the old story. I was in the middle of a successful acting career when I was bitten by the accounting bug.”

Ventures pay off

LARRY RICHARDSON'S KEY ROLE LEADS TO PROMOTION AT RENAISSANCE RE

Bermuda's RENAISSANCE RE HOLDINGS has promoted **Larry Richardson** to Senior Vice President, Renaissance Re Ventures. He will continue to report to Jay Nichols, who is Executive Vice President, Renaissance Re Holdings and President, Renaissance Re Ventures. Mr Richardson joined Ren Re in 2001 as Vice President of the company's Ventures unit, which

creates and manages Renaissance Re's joint ventures and makes strategic investments. Ren Re CEO Neill Currie, said Mr Richardson had "played an integral role in enhancing Renaissance Re's position as a market leader for managing cat risk".

Meanwhile, Renaissance Re Holdings has named **Ralph Levy** as a Director. Mr Levy is a Senior Partner in King & Spalding, a law

firm headquartered in Atlanta. He is also on the Board of Attorneys' Liability Assurance Society (ALAS), a Bermuda-based mutual insurance company.

Bermuda-based MONTPELIER RE HOLDINGS has appointed **Timothy Aman** as Senior Vice President & Risk Management Officer.

More changes at troubled SCOTTISH RE GROUP: **Cliff**

Wagner, President & Chief Executive Officer, North America, and the group's former Chief Actuary, has resigned. **Paul Goldean** will serve as interim President & Chief Executive Officer, North America as well as continuing in his role as Chief Administrative Officer of Scottish Re Group.

Andrew Carrier will be joining the ARGO GROUP as President of new Bermuda reinsurer Peleus Re. For the past seven years, Mr Carrier has been the Active Underwriter for the Kiln Group's Catastrophe Syndicate 557 at Lloyd's, one of the market's most profitable and highly regarded syndicates. He was also Chairman of Lloyd's International Reinsurance Committee.

FLAGSTONE RE has picked **Donald Emleigh** as its General Counsel. Mr Emleigh has close to 30 years' experience in the re/insurance industry, most recently as White Mountains Reinsurance Group General Counsel.



Donald Emleigh

Dwight Evans has joined WHITE MOUNTAINS RE as Executive Vice President for Global Reinsurance. He was Chairman & CEO of Arch Worldwide Reinsurance Group from 2001 to 2005.

MAX SPECIALTY INSURANCE, which is in Richmond, Virginia, has announced that **Michael Miller** has joined as Chief Underwriting Officer of its newly formed Marine Division. Max Specialty is the US-based E&S platform of Bermuda's Max Capital Group.

ACE LIFE INSURANCE COMPANY, doing business as ACE TEMPEST LIFE RE USA, has named **Jim Gibbs** as Vice President & Chief Underwriting Officer and **Bruce Horton** as Vice President & Chief Marketing Officer.



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WHAT'S ON

October 3 to 5
Hawksmere International Reinsurance Congress
 Fairmont Hamilton Princess, Bermuda
www.reinsurancecongress.co.uk

October 28 to 31
Association of Insurance Compliance Professionals Annual Conference
 Portland, Oregon
www.aicp.net/annualconference/2007conference/index.cfm

November 7 to 9
International PLUS Conference
 Washington, DC
www.plusweb.org

December 1 to 4
NAIC 2007 Winter National Meeting
 Houston, Texas
www.naic.org

January 16 to 17
Bermuda Re Basics: Demystifying Reinsurance — A Basics of Property/Casualty Reinsurance Course, presented by Reinsurance Association of America and Bermuda Insurance Institute
 Fairmont Hamilton Princess, Bermuda
hocutt@reinsurance.org or
 202-783-8327

XL's woman to watch!

SHERRON WILLIAMS NAMED AMONG 50 OUTSTANDING INSURANCE WOMEN

Sherron Williams, the Chief Underwriting Officer, Professional Liability Operations at XL Insurance (Bermuda) has been chosen as one of 2007's "Women To Watch" by leading industry newspaper *Business Insurance*.

The 44-year-old Bermudian was among 50 women picked in the second annual review of senior executives at a variety of companies serving buyers of commercial insurance, reinsurance, risk management services and employee benefits.

Business Insurance wrote: "Sherron Williams oversees a team of 15 people managing the second largest portfolio of business within XL's Bermuda operations ... and regularly participates in industry events, sharing her industry knowledge and expertise with peers."

Ms Williams joined XL as a trainee underwriter in 1991 and recently chaired the 2007 Bermuda Professional Liability Underwriting Society symposium.

She told *BI* that the best professional advice had been given to her by a former manager: "He said to me, 'Don't forget the importance of empowering those who report to you.' Essentially, he was saying that oftentimes you find a manager who is threatened by [an employee] who is smarter than



Sherron Williams: firm views on nurturing talent and womanhood in the workplace

them, more creative than them, has a better working relationship with key contacts ... and as such feels that [he/she] shouldn't develop them further. Embrace those strengths and allow them to soar."

Ms Williams said the best part about her current role was that XL gave her a lot of autonomy: "We agree on goals, and then they leave me to execute." Her advice to

young women is to "work hard, be punctual, and be consistent". But she also urged them to embrace their femininity. She told *BI*: "Women bring unique talents to the workforce. Let us not forget that as we progress. But, please don't use the fact that you are women as an excuse for why you cannot excel. That I do not find acceptable."

The list of 50 top women was compiled from hundreds of nominations by readers as well as information supplied by senior staff of *Business Insurance*.

Editor Regis Coccia said: "We consider the 'Women to Watch' a starting point, not an endpoint, for discussing the importance of women in the industry. Even though more women are taking on high-profile jobs, senior management in the insurance business remains largely male. *BI* believes that diversity — whether through gender, race or ethnicity — is important for an industry that serves people and businesses in all walks of life."

'The best aspect of her current role is that XL gives her a lot of autonomy: "We agree on goals, and then they leave me to execute"'

RAM CFO quits

Rick Lutenski, CFO of RAM Holdings, has resigned. RAM President & CEO Vernon Endo said: "We are sorry to see Rick leave. During more than three years with RAM, he contributed significantly to its transformation to a publicly held com-

pany with an increasingly significant presence in the financial guaranty reinsurance market. We are especially pleased that he built a solid finance organisation, staffed with a talented team, which will be able to effectively

manage our financial operations until we recruit a new CFO."

RAM Holdings' subsidiary RAM Reinsurance provides financial guaranty reinsurance for US and international public finance and structured finance transactions.

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Dubai: at the epicentre of an explosion of demand for insurance products



‘We could not have chosen a more strategic venue than this...’

The Bermuda-based World Insurance Forum is to hold its 2008 event in Dubai. It will be the first time the biennial insurance and reinsurance industry event has been held outside

Bermuda. The WIF, owned and operated by industry group Bermuda Insurance Symposium, has been held in Bermuda since 1993.

It said the change was designed to “further

involve new and evolving global markets”.

The announcement added: “The WIF in Dubai in March 2008 will be a global summit at the entrance of the world’s fastest growing markets and is expected to draw industry leaders and key government authorities from multiple jurisdictions worldwide ... along with brokers, risk product buyers and investors, capital market players and senior country officials from the Middle and Far East regions.”

Michael Butt, Chairman of AXIS Capital Holdings and head of the WIF’s advisory board, stated: “Over the last 15 years, Bermuda has become a leading market for global insurance and reinsurance business. As the world continues to globalise, Dubai is seeking to become the leading centre for the Middle East and South Asian region. I am therefore delighted that we have this opportunity to open doors, build relationships, exchange views, develop mutual opportunities and move forward to help establish the standards of international best practice.”

The WIF’s Robin Spencer-Arscott added: “We could not have chosen a more strategic venue than Dubai as it successfully positions itself as a ‘crossroad city’ where east meets west and is beginning to emerge as a powerful regional and global financial centre.”

Omar Bin Sulaiman, Governor of the Dubai International Financial Centre, where the WIF will be held, said: “It is a very significant event for the insurance industry. Dubai and the Gulf in general are experiencing an increasing demand for insurance products, driven in part by the region’s massive investments in infrastructure spending, its introduction of compulsory health insurance and the rapid growth of Islamic or Takaful insurance offerings.”

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"This policy has not caused anyone any problems... No one who has come to the Ministry for extensions has been denied. There is no way this Government will tell a company that if they can't find a Bermudian, so-and-so has to go. That's not common sense."

— Immigration Minister **Derek Burgess** on criticism that the new work permit policy was forcing firms to outsource more jobs

"There's a lot of outsourcing on Bermuda. The cost per employee is relatively high, and so it's natural for companies to look at that."

— former ACE Chairman **Brian Dupereault**, quoted in *Reactions at the International Insurance Society's Annual Seminar in Berlin*

"I'm more than comfortable putting our traditional reinsurance products to clients in competition with the capital markets. I think the ability to design very customised products for individual clients, which is not yet possible with

insurance-linked securities, is an advantage."

— PartnerRe CEO **Patrick Thiele**, quoted in a *Reactions feature about the movement of capital markets in the catastrophe risk business*

"From a reinsurer's perspective we have not passed on any risk in the form of a cat bond because we don't buy retrocession. Our philosophy is that if we have put in the work to evaluate the risk thoroughly we prefer to hold it ourselves. We are more volatile because of that but we offer a disproportionately high return for that increased volatility."

— **Patrick Thiele**, explaining why PartnerRe invests in cat bonds rather than sponsoring them

"Surrealism was an ART movement that began in the late 1980s and is best-known for the visual artworks and writings of group members based in Bermuda. Their works featured the element of surprise, unexpected juxtapositions and, although clearly very weird now, seemed okay at

the time. No one was more affected by these surrealist artists than their patrons and buyers, especially after multi-million dollar losses began to roll in and the works were discovered to be deeply flawed."

— *Reactions pokes fun at modern ART (Alternative Risk Transfer)*

"I'm sure many insurance executives lie awake at night with cold sweats thinking about Katrina, still wondering whether they are prepared for the next 'big one'."

— **Robert Hartwig**, President & Chief Economist of the Insurance Information Institute

"US sub-prime is just the leading edge of a financial hurricane. For far too long, no one seemed to care if borrowers would be able to service their debts... In short, there was a global credit bubble."

— **Bernard Connolly**, Global Strategist for Banque AIG in the London *Daily Telegraph*



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The law firm was founded by Lynda Milligan-Whyte, J.P., the former U.B.P. Government Leader in the Bermuda Senate.

It's sub-prime time

AND THE INDUSTRY IS BRACING FOR ANOTHER ENRON, SAYS CHRIS GIBBONS

Could the sub-prime mortgage crisis turn into the next Enron? That's what some experts fear as tumbling US home prices and increased foreclosures put pressure on the world's financial markets — especially those institutions that offered, or invested in, high-risk, sub-prime mortgage-backed securities.

The crisis — already dubbed “sublime” by Bloomberg — could trigger substantial claims on Directors & Officers, Errors & Omissions and other professional liability policies and is making many insurers and reinsurers nervous.

Leading insurance broker Marsh & McLennan warned in a recent report that the crisis, “coupled with increased relaxation of underwriting standards, has led to the bankruptcy of several mortgage lenders, the collapse of hedge funds, increased regulatory scrutiny surrounding lending practices, and ratings downgrades of 2005 and 2006 vintage residential mortgage-backed securities bonds.

“In addition, the mortgage market problems have ignited concerns about the potentially large exposure insurance companies and pension funds may have to securities backed by sub-prime mortgages, including investments in collateralised debt obligations (CDOs) and collateralised loan obligations (CLOs) with sub-prime exposure.”

Marsh said potential litigation arising out of D&O and E&O liability could include:

- Lender lawsuits against banks — some lenders have been forced to file for bankruptcy when asked to buy back loans. It is likely that there will be claims of improper margin calls and flawed valuation of underlying collateral on the part of banks and other institutions that purchased or financed the loans.
- Shareholder suits against lenders, accountants, trustees and



underwriters — shareholders could make claims of misrepresentation and omission related to accounting for residuals, as well as claims of bad valuation and poor underwriting standards.

- Insurer lawsuits against lenders — large insurance claims on failed sub-prime collateral may lead to accusations of poor underwriting (misrepresentations and omissions) on the part of lenders.
- Investors' suits against trustees — possible claims of breach of fiduciary duty on the part of the trustees responsible for the distribution of cash flow.
- Trustee suits against lenders and underwriters on behalf of investors — potential claims are likely over fraudulent conveyance and breach of contract related to loan servicing.
- Individual investor lawsuits — if investors in mortgage-backed securities post poor returns as a result of failing sub-prime backed investments, individual investors may accuse the funds of not taking on suitable and prudent investments and failing to follow investment guidelines and standard risk management procedures. There also may be claims of misrepresentations, omissions, bad pricing and mark-ups.

Jill Sulkes, a Managing Director in Marsh's Financial Institutions Practice, said: “Insurance companies, hedge funds, banks and ratings agencies must continually assess the risks raised by the sub-prime crisis and examine their D&O and E&O exposures. Although the D&O and E&O insurance market has been largely stable, if there are a high number of costly claims under these insurance policies, this trend may reverse and costs may begin to rise.”

Bermuda-based Scottish Re is among those companies that could be exposed to claims arising from the crisis. Some analysts are concerned that the company has a large mortgage investment risk but the company moved to reassure investors and shareholders in mid-August, by providing additional disclosure on its sub-prime asset and mortgage-backed securities.

The company said it had more than \$500 million of available liquidity between itself and a subsidiary as of June 30, amid concerns about its sub-prime exposure.

Scottish Re said the \$500 mil-

lion was in excess of liquidity held by its insurance operating subsidiaries. It also said total invested assets within its three securitisation structures exceeded statutory reserves covered by these structures by about \$1.4 billion as of June 30.

In July, Scottish Re estimated that it had an unrealised loss of \$97 million from its sub-prime mortgage holdings. At the end of 2006, Scottish Re's two insurance operating entities had statutory surpluses of \$387.1 million, according to regulatory filings.

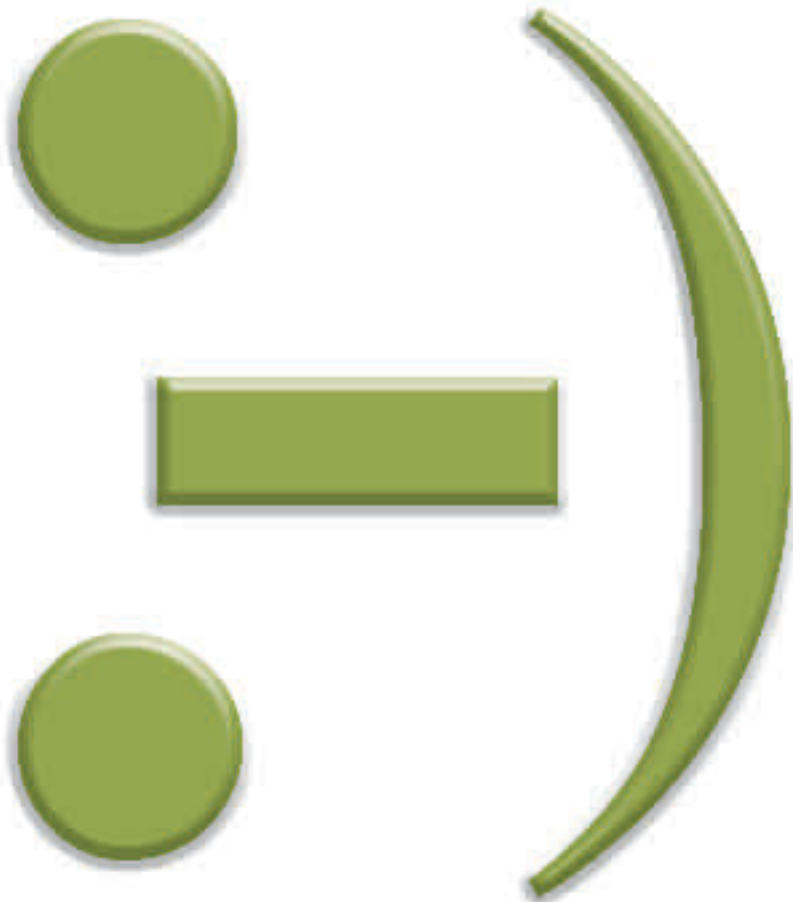
Chief Accounting Officer Duncan Hayward told analysts in a conference call following the August disclosures: “There has been heavy selling, particularly by hedge funds and other leveraged accounts hit with margin costs. Wall Street firms concerned with their own risk exposures have not wanted to buy bonds.

“As a result, the market has become increasingly illiquid and unbalanced with an absence of buyers, causing prices to be well below what we and our third-party investment managers regard as their true fundamental value.”

According to *Marketwatch*: “Sub-prime mortgages are offered to less creditworthy home buyers. Alt-A loans were originally designed for borrowers with cleaner credit records, but with other issues that often meant they provided fewer documents showing what they earned.

“Rising sub-prime mortgage delinquencies have made institutional investors wary of buying lots of other types of home loans in the secondary market. That, combined with a broader credit market squeeze, has hit the value of even some highly rated mortgage-backed securities.”

‘The market has become increasingly illiquid and unbalanced with an absence of buyers, causing prices to be well below ... their true fundamental value’



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