LLOYD'S

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MARKET

FOR BESPOKE INSURANCE SPECIALISTS

FLIGHTS OF FANCY

Are aviation rates really set for a sustainable rise?

FROM THE EDITOR

WELCOME TO THIS ISSUE OF *MARKET*

There is a global feel to this issue as we travel to Singapore and speak to Mr NG Nam Sin, of the Monetary Authority of Singapore on the benefits and attractions of trading in this vibrant city state.

Staying in Singapore, we speak to Mark Newman, CEO of Catlin Asia. He relates his experiences of conducting business in this market, which is a gateway not only to East Asia and the Pacific, but also India and the Middle East.

To Scandinavia next where Erik Borjesson, Lloyd's first Nordic Area Manager is working to help managing agents and syndicates build relationships in Denmark, Norway, Sweden, Finland and Iceland.

Helping us in our travels, the aviation market has had a particularly bumpy ride of late and we ask whether the prospect of more profitable business in 2009 is a mere flight of fancy.

We stop off in Brazil and Poland where Lloyd's have recently opened new offices and, helping to offset our carbon footprint, we learn how the Lloyd's Building is continuing its green policy.

Together with 360 Risk Insight, product stories and people news, we hope you enjoy this issue of Market.

Paula

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COVER PHOTO/Benedict Redrone/Gallerystock

LLOYD'S 360° RISK INSIGHT

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NEW PRODUCT

In response to new rules on pollution and tougher policing of existing rules and regulations, ACE has decided to write the company's environmental liability products through Lloyd's.

ACE Global Markets Syndicate will offer clients cover across varied industries in territories around the world, including the United States. Cover includes the clean up of the policyholder's own property and surrounding land and water, third-party liability including nuissance, damage to biodiversity, business interruption and pollution caused by contract works.

Wayne Harrington, Environment Risk Manager for UK & Ireland at Ace, said: "There is an increased recognition that the ongoing operations of a variety of businesses can actually create pollution issues and pollution risks for organisations as a result.

"New regulations will make companies more aware of the risks and they will have to assess their exposures in regard to them. Most probably some didn't think of themselves as a potential polluter before."

Growing concern about the world's ecology and the impact of industrial growth has seen environmental liability move up many major corporations' list of potential emerging risks. This year the UK became the latest European country, following the lead of Germany, Spain, France and Italy, to introduce the European Union's Environmental Liability Directive.

The directive introduces tough new penalties on firms that have caused environmental damage, with a particular emphasis on protecting biodiversity.

The rules impose a new obligation on organisations to prevent environmental damage and, where damage cannot be prevented, requires organisations to carry out much more comprehensive clean-up work than they may have done previously.

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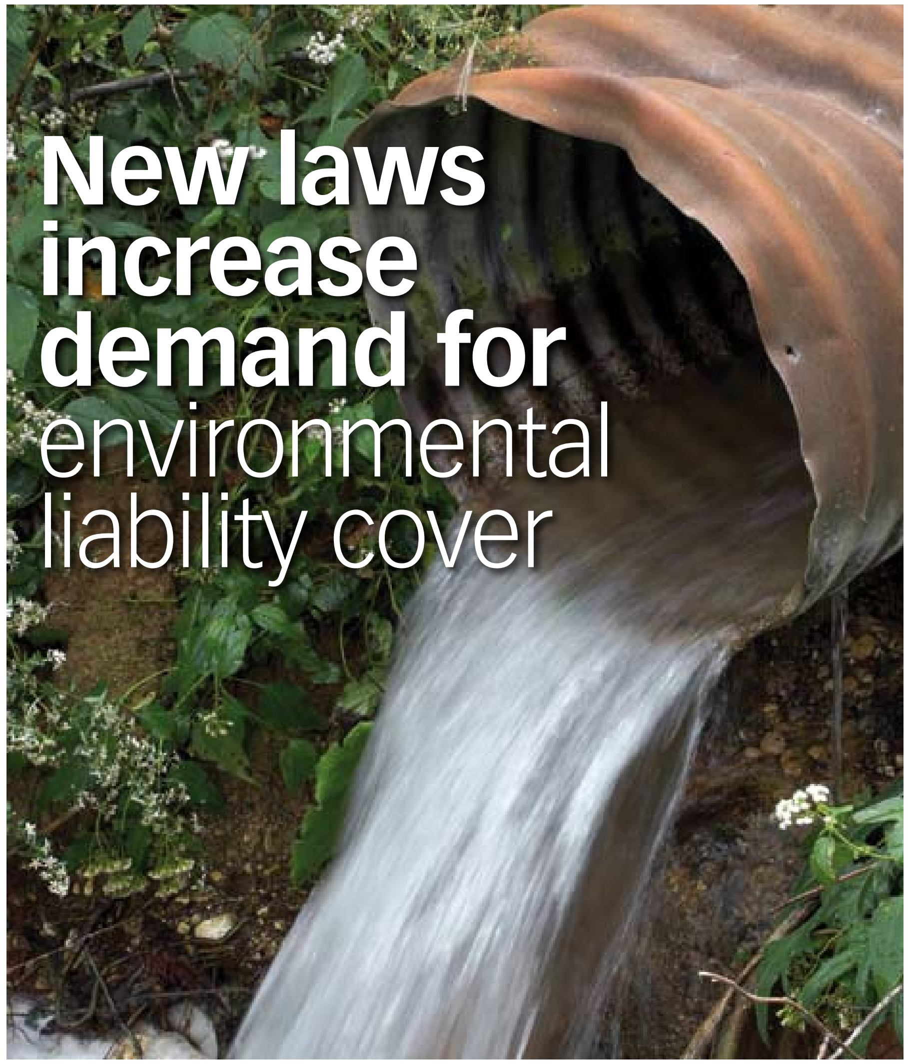
New laws increase demand for environmental liability cover



LLOYD'S POSTS SOLID PROFITS

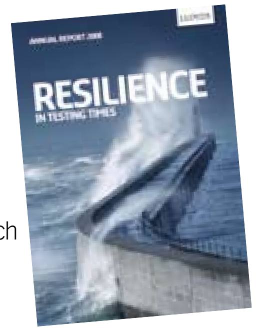
LLOYD'S NEWS

Lloyd's announced profits in March of £1.9bn for 2008, despite very difficult trading conditions.

A series of massive natural disasters, including hurricanes, earthquakes and wild fires, made 2008 the second most expensive year for the insurance industry to date, costing Lloyds alone £1.8bn.

"Given the financial crisis that has unravelled over the past year and the scale of catastrophes, our results represent a solid performance and are better than we might perhaps have expected in such a turbulent year," said Lloyd's CEO Richard Ward.

The results include an underwriting performance of £1,198m, an investment performance of £957m and currency movements of £853m. Lloyd's strong capital position and stable ratings have also made it attractive to worldwide markets, leading to approximately £18bn of business being written last year.



"However, we can't afford to be complacent," Ward said. "The coming year will be tough and so our focus remains very much on underwriting discipline, sound risk management and continuing to improve the efficiency of the market and the attractiveness of the Lloyd's franchise."

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COMMUNITY PROGRAMME
celebrates two decades

see page 19

Costa finds coffee to insurers' taste

UNUSUAL RISKS

With its origins stemming from an 18th-century coffee house, it is perhaps no surprise that Lloyd's has insured the tongue of Gennaro Pelliccia, Costa Coffee's Italian Master of Coffee, for £10m.

Gennaro Pelliccia personally tastes every single batch of raw coffee beans at the company's roastery in London before they are shipped to its stores. Costa estimates that Pelliccia is responsible for the taste of about 108 million cups of Costa Coffee consumed around the world each year.

Speaking about the insurance policy, Pelliccia said: "In my profession, my taste buds are crucial. My 18 years of experience enable me to distinguish between thousands of flavours. My taste buds also allow me to search out any defects, which helps guarantee Costa's unique Mocha Italia blend."

The average tongue has approximately 10,000 taste buds, which means Costa has in effect insured each of Pelliccia's taste buds for £1,000.

This is not the first time Lloyd's has insured a tongue. Wine tasters for supermarkets and wine merchants have also taken out policies.

The Costa policy was placed through Glencairn, a Lloyd's broker. A Lloyd's spokesperson said: "Lloyd's is the pre-eminent place in the world for the insurance of people, whether it is individual body parts or dealing with particular physical attributes that are necessary for people to pursue their occupations."

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RISK PRIORITIES AND PREPAREDNESS

360 RISK INSIGHT

Knowing that something is a very real risk for your business does not always mean that you are equipped to deal with it. This is one of the conclusions of a new comprehensive research report that Lloyd's and the Economist Intelligence Unit (EIU) will publish this summer.

The EIU has asked more than 400 global business leaders what their risk priorities are and how prepared they believe their company is to deal with them. Supported by 20 in-depth interviews with well-known CEOs and other public figures, the report will identify some fascinating trends about how business leaders approach five main categories of risk: natural hazard; security and crime; economic and market; environmental and health; and strategic and business risk.

The report will reveal that the current financial market turmoil and economic recession have begun to have a major impact on the appetite for risk-taking in the boardroom, and will highlight how the risks that CEOs are most worried about have begun to shift as a result of the downturn. It also discusses some important gaps between awareness of the risks and the level of action that boards take to manage them.

Which region is the most risk-aware and which industry is best placed to tackle the changing environment? Lloyd's and EIU will reveal the answers at the end of June.

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NEWS IN BRIEF

LLOYD'S APPOINTS NEW UNDERWRITING PERFORMANCE DIRECTOR

Tom Bolt (pictured below) has been appointed as Lloyd's new Underwriting Performance Director to succeed Rolfe Tolle, who retires at the end of 2009. Bolt has more than 25 years' experience of international insurance and reinsurance across the UK, US and Europe, most recently as Managing Director of Marlborough Managing Agency. As Underwriting Performance Director, Bolt and his team will be responsible for working with individual Lloyd's businesses to improve the commercial performance of the market. Bolt will be starting his new role in early autumn 2009.

Tom Bolt

NEW OFFICE IN WARSAW

Lloyd's has opened a representative office in Poland after securing a licence to write business there in 2008. The office will be run by Witold Janusz, who has been building relationships with the regulatory authorities and developing business in Poland since Lloyd's was granted its licence. Janusz said: "Establishing an office in Poland will help Lloyd's to further develop opportunities in the country and across Eastern Europe."

Lord Levene with the Governor of the State of Rio, Sergio Cabral

LLOYD'S OPENS OFFICE IN RIO

INTERNATIONAL

After becoming the first reinsurer to gain admitted status in Brazil in 2008, Lloyd's has officially opened its first office in Brazil.

Located in Rio de Janeiro, Lloyd's Brazil will allow syndicates and managing agents to offer reinsurance in the country, and already has two syndicates with a permanent local presence – Liberty and Marlborough – with a third, Catlin, already established in Sao Paulo.

The office was opened by the Chairman of Lloyd's, Lord Levene, and he was joined by Sergio Cabral, Governor of the State of Rio, Joaquim Levy, the Secrectary of Finance for the State of Rio and Maria Silvia Bastos, President and CEO of Icatu Hartford, as well as a number of attendees from the market.

Lord Levene said: "We very much look forward to a long future in Brazil, working with the Instituto de Resseguros do Brasil and other local reinsurers to share our expertise and capacity."

Since the Brazilian reinsurance market opened to foreign reinsurers at the beginning of 2008, Lloyd's has seen a 79% rise in premiums compared to business in 2007, up to £95m from £53m.

Brazil is Latin America's largest insurance market, and represents 44% of gross written premium. The Brazilian insurance regulatory body SUSEP expects continued premium growth in the country of 16.2% for 2009 and 11.4% for 2010. With a lack of catastrophes, a stable economy and vast mineral wealth, it is a very attractive market for (re)insurers.

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Run-off progress continues at Lloyd's

LLOYD'S NEWS

The number of years of account in run-off at Lloyd's fell from 54 in 2007 to 37 in 2008 – a drop of 32%. In aggregate, run-off years reported an overall profit of £104m, including investment income and syndicates backed by insolvent members, supported by the Central Fund, which reported a small overall surplus.

The decline in the number of open years is the result of concerted efforts at Lloyd's to reduce run-off. A key driver in this reduction is the impact of Reinsurance-to-Close (RITC) transactions, which contributed to the elimination of £2.3bn of run-off liabilities in 2007, enabling 18 syndicates to close. Meanwhile, other finality tools – including schemes of arrangement and commutations – and the absence of major new run-offs have contributed to the contraction of the market.

UK run-off is likely to continue shrinking, despite the potential impact of the financial crisis on new run-off business, said Paul Corver, Chairman of ARC, the UK market body for insurance and reinsurance legacy management. Speaking at the association's 2009 Congress, he said that recent scheme sanctions were likely to put to rest large portions of legacy business.

"Scheme closures reduce the total amount of liabilities in the market," explained Corver. He added that it would take time to see any impact from the financial crisis translating into new run-off.

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New policy helps forces soldier on

NEW PRODUCT

Cassidy Davis, the personal lines division of Jubilee Managing Agency at Lloyd's, has been appointed by Forces Financial to underwrite and provide claims handling services for a personal accident insurance product for UK armed-forces personnel. The product represents the first significant revision to standard policy offerings to service men and women in more than 20 years.

The policy supplements cover provided by the Armed Forces Compensation Scheme (AFCS) and focuses the main benefits on providing cover for injuries sustained off duty. Whereas the AFCS provides a sliding scale of payments for injuries and accidents incurred on duty, the same injuries experienced by personnel off duty are not covered.

In filling this gap in coverage, Forces Financial's Personal Accident Insurance includes four levels of cover, with 100% of the benefits payable as a consequence of permanent disablement or injury if the policyholder is injured off duty, and 20% if the policyholder is on duty.

Forces Financial, the financial products provider for serving and retired members of the UK Police, Armed Forces and MOD, designed the policy in response to a number of factors that had influenced the cost and effectiveness of traditional Personal Accident insurance.

Al Voice, Managing Director of Forces Financial, said: "Previous policy frameworks were designed when overseas conflicts were rare and did not reflect today's operational tempo. Meanwhile, premiums had become too expensive due to increased claims forcing many customers to forgo their protection. The current financial climate suggests that the time was right for a smarter product that recognised the cover provided by the improved AFCS as well as representing choice and increased value for money for the consumer."

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LORD LEVENE SPEAKS UP FOR THE CITY

GLOBAL SUMMIT

In media interviews, Lloyd's Chairman, Lord Peter Levene, spoke up on behalf of the City of London and its importance to the UK economy.

Following the G20 Summit and the regulation frameworks needed, Levene told Bloomberg TV that it was important for any new rules to be realistic and implemented on a country-by-country basis.

"If we get one super 'über' regulator, I don't think that's going to work at all," said Levene. "We have to look at where the problems are and there has to be a coordinated view about how to fix those problems, but on the basis that people can work with it. There's no point in bringing in rules and then the industry says: 'Well, we just can't operate'."

Levene added that a wait-and-see attitude was sensible and that it was important to recognise that not all financial regulation is defective.

In a separate article for the *Evening Standard*, Levene pointed out that, beyond the banking sector, other parts of London's financial services industry remained healthy. He wrote: "London's financial services industry, which stretches well beyond the Square Mile, out to Canary Wharf, the West End and elsewhere, has been a major and successful contributor to the economy of the UK for many years.

"London is still the world's leading financial centre, outstripping New York for competitiveness, and until recently financial services was contributing some £42bn to the UK's tax coffers in 2007-8 – more than the total schools budget."

In a rallying call for London's financial services industry, he said: "[The banking crisis] does not change the fact that the City in all its many other guises – insurance, asset management, legal and accountancy shipping and private banking – is still one of the UK's great assets and an essential part of our future.

"Instead of indiscriminately knocking the City, it is time to remind ourselves that the City is more than just bankers and much of it has continued to prosper and serve us well."

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Straits talking

Mark Newman, CEO of Catlin's Asia-Pacific operations, talks to *Market* about doing business in Singapore

PHOTO/CJ Sameer Wadha

What prompted Catlin to become the first syndicate to set up in Singapore in 1999?

At the time, we had a stamp capacity of approximately £200m but were only writing about £120m of premium income due to market conditions. We needed to be more proactive and to look for business opportunities ourselves.

Lloyd's was also changing. We had already undertaken a research project on possibilities in the Asia-Pacific area in 1998, so with a bit of encouragement from Lloyd's, we agreed to support their Singapore initiative. This resulted in Catlin leading the way in establishing a presence in Singapore.

What are the benefits?

The principal benefit is the limited capital required to establish an operation in Singapore, or anywhere else that Lloyd's has an operating platform. Elsewhere in Asia, and through the Lloyd's licences, we also have access to markets that may otherwise be closed to individual syndicates.

How has the Singapore and wider Asian market developed since you set up?

The number of syndicates participating – and therefore the market's capacity – has grown significantly and consistently. The international broker community has also invested considerably in building local broking and client-facing expertise. Singapore is now often seen by clients as an equally important market as London, not only for East Asian and Pacific business, but also for Indian and Middle Eastern clients.

How diverse a market is Asia-Pacific?

Catlin looks at Asia-Pacific as one management and underwriting region. However, within this huge geographical area, there are sophisticated and mature insurance and reinsurance markets, especially in Japan, Australia and South Korea. In contrast, China, India and several other South-East Asian countries have remarkably low per capita insurance spend, which will increase as the distribution of wealth evolves and the middle classes emerge.

How is the financial crisis affecting the Asian market?

Economic output is slowing in the region, but so far there has not been a correspondingly widespread reduction in buying patterns for insurance or reinsurance. Commodity prices and lower shipping volumes are affecting the marine sector, and some private equity-financed construction projects have been delayed. Conversely, regional governments have actively brought forward many infrastructure projects and increased public spending to maintain momentum in the construction industry.

The rate reductions that many classes had experienced for the past 24 months or so have now generally ceased. Pricing increases are being seen across the financial lines, energy and trade credit classes. The January treaty renewals did not deliver the rate increases or capacity reductions that many had anticipated, but we expect rate hardening during the 1 April and 1 July renewals, especially as more insurers release their 2008 financial results.

What advice would you give to a Lloyd's syndicate starting out in Singapore?

There are no shortcuts to doing it properly. A man and a dog in Singapore are just not going to cut it, and acting as a postbox for underwriters in London is equally ineffective. Therefore, a proper presence in Singapore is required. Stick to classes of business that you understand and learn to appreciate that the rules for good underwriting are the same in Singapore as in London. M

> MORE

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GATEWAY TO ASIA

Mr NG Nam Sin, Executive Director of the Development and External Group of the Monetary Authority of Singapore (MAS) discusses how the city state has become a major centre for the Asian and international insurance industry

AS A MAJOR (re)insurance centre in Asia, the industry in Singapore has benefited from impressive growth over the past years, driven by the emerging Asian economies. Total industry assets have increased five-fold over the past decade. Most major insurance and reinsurance firms now have a presence in Singapore.

The industry has matured in terms of the breadth and depth of products and services offered, with more insurers writing specialised risks such as aviation, energy, marine, political, terrorism, professional indemnity and trade credit risks. We have seen increased interest from new life insurers catering to high net worth and mass affluent segments.

In line with the development of the insurance industry, the number of insurance intermediaries has grown. Most of the top global brokers have established a presence here. As Asian clients become more sophisticated, these intermediaries have been expanding their range of products and services, especially in the areas of risk modelling and research.

As part of increasing the breadth and depth of risk management offerings in Singapore, we have seen good growth of the captive insurance sector over recent years. Today, Singapore is a leading captive domicile in the Asia-Pacific region.

As you might expect, due to the global economic slowdown, the current business climate is challenging. However, with every crisis, opportunities also present themselves. We have confidence in the long-term potential of the Asian economies as the fundamentals remain sound.

Moreover, insurance penetration rates in the region have traditionally been low compared to developed markets like the US and Europe. In 2007, Asia (excluding Japan) contributed only 10% of total premiums globally, despite being home to 60% of the world population. However, this region presents significant opportunities as premium has grown by an average of 20% over the past three years.

Alongside the growth and increasing sophistication of Asian economies, more demand for specialist insurance coverage in Asia is expected in areas such as aviation, energy, credit insurance, product liability, D&O, professional indemnity and terrorism. Such demand comes on the back of infrastructure development in Asia, the expected pick-up of intra-Asian trade and an increased focus on sound corporate governance practice.

FOREIGN APPEAL

Singapore remains an attractive business location for many reasons. It has a stable political and economic climate, with a pro-business environment, and a skilled and educated workforce.

Singapore's geographical location is also a major factor being so close to the fast-growing Asia Pacific markets as well as to the Middle East. Moreover, the Singapore insurance industry has built up a critical mass of both international and local (re)insurers and brokers. They contribute to a thriving marketplace, which is also supported by a comprehensive network of support service providers such as specialised lawyers, consultants and IT services.

> "The Singapore insurance industry has built up a critical mass of both international and local (re)insurers and brokers"

OVERCOMING THE CHALLENGES

The Asian insurance markets are in different stages of development and do not share similarities like the markets in the US and Europe. There is a need for firms to understand the regional differences, regulations, practices and cultures of each country. As an Asian base for global firms, Singapore's ability to bridge Western practices and Asian culture offers a unique proposition. In addition, Singapore has always thrived on its ability to provide a conducive operating environment for firms that have strategic interest in expanding in this region.

As we do this, we are committed to maintaining high prudential standards while we seek ways to accommodate business models and structures new to Singapore.

A case in point is how Singapore has created an appropriate regulatory framework for the Lloyd's market to evolve here. We amended the Insurance Act in 2002 and introduced the Lloyd's Asia Scheme to facilitate the creation of a replica of the Lloyd's subscription market in Singapore. Lloyd's Asia has seen impressive growth over the past few years, servicing not just Singapore but the whole region.

Access to talent will be another challenge. While the Asian insurance market has shown strong growth in recent years, more needs to be done to build up expertise and in-depth understanding of Asian risks for better risk assessment and pricing. Singapore is committed to building the talent pool for the financial sector.

At the same time, we are keen to attract talent from all over the world. Singapore's open immigration policy is an added advantage for those looking for an established Asian insurance centre to locate their specialised talents. We also place strong emphasis on continuous development of skills. For instance, we support industry training initiatives, such as the efforts led by the Institute of Banking and Finance to raise competencies across the financial sector through the Financial Industry Competency Framework. This includes working with insurance practitioners to introduce competency-based training and assessment for insurance professionals at different job levels.

Through nurturing talent and providing an effective operating environment for financial services, Singapore will continue to attract interest from both within the region and internationally. M

Esplanade Theatres on the Bay, on the waterfront of Singapore's bay, purpose-built as a concert hall and theatre for the performing arts

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AIR PRESSURE

Is the prospect of more profitable aviation business in 2009 a mere flight of fancy?

AVIATION INSURERS HAVE had a bumpy ride in recent times. The hopes of a smooth return to profitability are high, but uncertainty in the airline industry makes the sustainability of rate rises hard to predict.

Some commentators say airline business has turned a corner after years of decline. Others are more cautious. But all agree that for underwriters, brokers and their aviation clients, these are indeed testing times.

The past few years have been dominated by the aftershocks of the terrorist attacks on New York and Washington DC in 2001. The tragedy sent rates soaring. This attracted plenty of attention from insurers keen to get into the business, putting downward pressure on rates and resulting in a decline that turned into free fall.

Magnus Allan, aviation analyst for broker Aon, says lead hull rates fell by about 18% in 2006 and by another 11% in 2007. Clearly, that sort of drop would create difficulties for any business.

Allan is one of those who believes that the picture has now changed and that the market can be considered a hard one. Aon's figures tell of a 5% upswing in lead hull and liability premium in December 2008, the month with the largest number of aviation renewals. That translates into a 16% increase compared with 2007. Fellow broker Willis also saw a rise. Its figures record an increase of 4% in December and 8% in the fourth quarter of 2008, in what it describes as "truly the make or break time for the year". Reinsurance broker Benfield also spoke of "a significant change in the mindset of reinsurers" with "a reversal of six years of rate reductions". Furthermore, Stephen Catlin, Chief Executive of Lloyd's underwriter Catlin, went on the record as long ago as November 2008 saying that aviation insurance was expected to have "at least bottomed out".

> "Risk selection and cycle management are absolutely crucial to mitigate the challenging rate environment"

But others point out that the swing is from a point of extreme weakness and that today's rates are still too low to put the sector into profit. Guy Sellers, Underwriting Performance Executive at Lloyd's, says: "It's very challenging to make money even at today's rates. Risk selection and cycle management are absolutely crucial to mitigate the challenging rate environment."

Brokers' figures put global premium at significantly less than US$2bn. Sellers says some experts believe the figure needs to be "well north" of that – or as high as US$2.5bn – to make aviation an attractive proposition for underwriters. The picture is one of a market swinging back towards equilibrium but being so finely balanced that both sides are feeling the strain.

PROFITABLE BUSINESS?

As Magnus Allan says: "The airlines are facing falling demand just at the time that insurers are under pressure to recoup lost ground. The timing is terrible for the aviation industry, as both business and personal travellers appear inclined to stay at home.

"All of a sudden everyone is in uncharted territory while the insurance people are trying to harden their markets."

Sellers points out that last year's rates were still lower than they were before 9/11. He also says that smart underwriters need to price in the risk of a catastrophe – the sort that happens only rarely but that can cause major tragedy and financial loss.

He says: "Many commentators would say that the current premium is not nearly enough to cover expected attritional claims costs, catastrophe load provision, reinsurance and general expenses and also allow an adequate margin for profit."

David Slevin, Head of Aviation for Lloyd's underwriter Faraday, says: "The sympathy has to be with our clients, who are suffering heavily as a result of the global economic downturn, and who in turn face the prospect of higher insurance costs, coupled with an increased nervousness as to the creditworthiness of their insurers."

He expects that losses from the past two years of account will urge them to increase rates significantly. "These developments could instigate some major changes in limits and coverage provided."

Slevin predicts that many insurers will be left with significant losses from 2008, after costs are taken into account. "As 2009 progresses, we expect that capital providers will increasingly appreciate that airline insurance is capital-intensive and ►

PHOTO/Benedict Redrore/Gallerystock

► that losing money will affect their appetite for this line of business. This in turn may lead many underwriters to shift focus away from market share and towards a much more profit-motivated business plan. The effect of this could be for rates to increase further by the end of 2009."

COMPLICATED EFFECTS

Aviation is one of the most highly leveraged and capital-intensive classes written, which could make it particularly sensitive to the effects of the credit crunch. But these effects are unlikely to be straightforward.

Forecasters were expecting carnage in the airline sector even before the global economic downturn began to bite. The International Air Transport Association reported that cargo volumes fell by 22.6% year-on-year in December. Its Director General, Giovanni Bisignani, has said that 2009 could be one of the industry's toughest ever years.

Airlines are already pulling back their investment in aircraft. Figures from Willis show that average fleet values were climbing briskly at the beginning of 2008 – by more than 40% in January and more than 30% in February. But by December, the rate of increase was down to less than 3%.

On the one hand, the economic downturn is squeezing airlines that were already desperate to control their costs. On the other, falling demand for air travel could mean falling exposures for insurers. But changes like that are unlikely to feed into the insurance buying process until later in 2009, in readiness for the fourth quarter.

Another major factor – and another unknown – is the safety of air travel. The recent tragic air crashes in Buffalo, New York and Schipol Airport in the Netherlands have renewed concerns about flying, while the extraordinary sight of a stricken US Airways flight ditched in New York's Hudson River was made even more amazing by the fact that all 155 people on flight 1549 survived. It will go down as one of aviation's great escape stories and it illustrates the point that some very serious incidents have resulted in major hull claims but fortunately have not resulted in correspondingly tragic losses of life.

Although 2008 had the fewest fatalities for 13 years, aircraft will always be vulnerable to uncontrollable factors such as the birds believed to have flown into the engines of flight 1549.

Lloyd's has a significant share of the airline market, particularly for leading on risks, and writes business around the globe. Its experts, both underwriters and brokers, are at the centre of understanding the conflicting pressures on the multibillion-dollar airline industry. Participants on all sides of the aviation business seem likely to need every bit of ingenuity and creativity to hold their ground in this year's negotiations. Whichever way they go, it is not going to be easy. M

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Climate change and security: planning for the future

New report aims to help business leaders factor the effects of global warming into their planning

CLIMATE CHANGE COULD jeopardise the economic and national security of countries fanning tensions between states as they compete for natural resources, says a new report published by Lloyd's.

The effects of global warming will make fresh water an increasingly precious resource, put food production under greater pressure, create increased volatility in the supply of energy and trigger shifts in population movements as a result.

Businesses assessing the risks of climate change will need to encompass a range of possible outcomes and frequently revisit their plans, according to the Lloyd's 360 report published in co-operation with the International Institute for Strategic Studies (IISS).

As the effects of global warming become increasingly difficult to predict, the report – entitled *Climate change and security: risks and opportunities for business* – aims to help industry leaders focus on what they should be considering when factoring climate change and security into their planning.

Published in April, the report discusses how climate change is likely to transform many areas of everyday life, including how cities are designed, how transport systems function and how production and trading systems are organised.

With rainfall patterns widely predicted to become more erratic, water will become a scarce and expensive commodity in many countries and could be the cause of inter-state conflict in some parts of the world. The report says that, while every business is likely to be affected, those companies whose production processes are heavily dependent on water will face particular challenges.

Meanwhile, food producers will increasingly struggle to meet demand as arable land becomes scarcer, forcing global food markets to alter considerably. Food and catering sectors will also face supply challenges. However, some businesses linked to water-efficient and sustainable farming techniques may be well placed in this changing environment.

Businesses will reap rewards if they are flexible enough to maximise green energy opportunities, but energy markets as a whole are likely to become more volatile. Most businesses will need to assess their energy requirements and map these against likely scenarios for energy supply to ensure future security. The report emphasises, that as a result of climate change, energy efficiency will become an increasingly important financial and reputational driver for many companies.

The resulting scarcity of these resources is likely to have a considerable impact on population movements, the report proposes. There is a large risk of mass migration from the developing world, as the less advanced economies closer to the equator will suffer most from climate change. For businesses with operations in these regions there will be workforce implications, while social and political tensions could damage operations locally.

WITH RAINFALL PATTERNS WIDELY PREDICTED TO BE MORE ERRATIC, WATER WILL BECOME A SCARCE AND EXPENSIVE COMMODITY

All the above factors will compound governments' ability to manage the economy and society, and will make it increasingly important to harness the inventiveness and organisational capacities of the private sector. The report advocates that this will be necessary not only for developing specific solutions to mitigate and adapt to climate change, but also to alter consumer behaviour – without which all efforts to combat climate change will have a limited chance of succeeding.

LLOYD'S 360° RISK INSIGHT

CLIMATE CHANGE AND SECURITY: RISKS AND OPPORTUNITIES FOR BUSINESS
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VIKING SPIRIT

Lloyd's sees opportunities for adventure in Scandinavia

THE SEA HAS traditionally been seen as the life blood of both the Scandinavian economies and the Lloyd's insurance market. It's therefore no surprise that Lloyd's is committed to the Nordic market bringing its specialist expertise – particularly of the marine, oil and gas sectors – to the region.

But while Lloyd's looks to bolster its leading position in these specialist lines, it also aims to build new relationships with Scandinavia's commercial and industrial businesses, and foster the expertise to service them.

Erik Börjesson, Lloyd's first Nordic Area Manager, says that one of his main challenges is to "demystify Lloyd's" in the Scandinavian market. "Of course, Lloyd's is well known as a brand in the region, but the understanding of how the Lloyd's market works is less clear," he says. Charged with helping syndicates and managing agents build relationships in Denmark, Norway, Sweden, Finland and Iceland, Börjesson is upbeat about the opportunities in the region.

Years of consolidation within the Nordic market have led to it being dominated by a small number of large players. The largest insurance group – If P&C Insurance Group – is the clear leader, with a market share of about 20%, according to Standard & Poor's. "More consolidation is not possible because there's nothing left to buy," says Börjesson. He believes that more competition can only be a healthy development for the market.

Initial prospects for newcomers have so far been limited to niche and specialty lines of business. Lloyd's March 2007 report *Northern Lights* pointed to energy, aviation, property, marine and liability as the best fit for Lloyd's specialised products. Lloyd's has to date concentrated on these five sectors but, with a total premium volume of $600m in the Nordic market, Börjesson is keen to explore other areas.

"We want to do more of the treaty reinsurance business," Börjesson reveals. "I also see large possibilities in the Swedish, Norwegian and Danish multinationals, where we can increase Lloyd's part in their programmes." As well as multinationals, there is the possibility of increasing penetration in the market's burgeoning SME sector.

DEVELOPING BUSINESS

The market too, has recognised the opportunities in the region. Markel International is also looking to broaden its scope. Having taken on an existing team of marine experts in Sweden last year, it is now looking to develop non-marine products and increase its concentration on niche lines within the hull and cargo sector, as well as looking for geographic expansion.

"We're focusing on the Nordic/ Baltic market," reveals Ove Staaf, Managing Director of Markel International Sweden. "Our ambition is gradually to market ourselves towards the eastern countries." Newcomers can exploit the maturity of the market, explains Staaf. "The big players are few and dominate the market, but they also have quite high operating costs. They have become quite inflexible, as more established organisations sometimes are, providing an opportunity for a smaller and quick-footed competitor with lower operating costs."

Competition isn't the only challenge when entering the Nordic market. Having an insight into the market requires a sound business strategy. "Just to move into the market and do business at a premium volume can be one thing, but you have to be smart and target the most profitable business," says Börjesson. Tapping into local talent can provide an edge in such a tight-knit market.

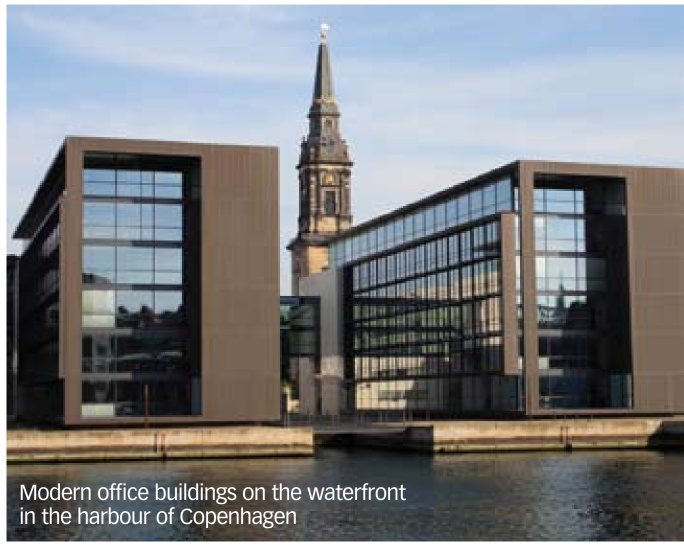
CLOSE CONTACT

Being spread over a much wider area than the London market, face-to-face meetings with brokers and clients are less frequent in the Nordic countries. But relationships are just as important. "You must understand how the market operates but you also need to have the contacts in the market because this is a people business," Staaf explains.

Brokers are relatively new to the market, having been allowed to operate in the region in the late 1980s and early 1990s. There was initial success but the introduction of the EU directive on insurance mediation has hindered recent progress. "Commissions are generally discouraged in the Nordic countries, so it's a fees-based business in general," explains Börjesson.

The claims experience in Scandinavia is one of the market's great attractions. It has little volatility and risks are well managed. "In general, the Nordic risks are very good risks," says Börjesson.

The exceptions are in energy and marine classes, which are more exposed to the vicissitudes of the global insurance market. "The last couple of years in particular were really bad years from a claims point of view in marine products," reveals Staaf, noting that the current economic climate has one silver lining – an improving trend in marine claims. "Ships are laid up now and being scrapped, so pressure on the limited pool of seafarers will not be the same."



Modern office buildings on the waterfront in the harbour of Copenhagen

> "The big players are few and dominate the market, but they also have quite high operating costs"

Claims are reducing but premiums are also dropping. "The value of assets we insure and the volume of trade is going down," says Staaf.

In a global economy, nowhere is immune from the continuing financial malaise. Capital has become more expensive, but to date, the insurance industry appears relatively well insulated from the worst of the crisis. Nordic market experts expect to see opportunities continue as prices harden.

Börjesson says: "Prices are not going downwards any more and we see a stabilisation of rates as the first step of the hardening market." M

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NAVIGATING recession

Participants in the market believe they are well placed to withstand recession, but caution is key

WHEN IT COMES to assessing how market participants view the way that Lloyd's is withstanding the recession, it's hard to argue with the evidence. A flurry of syndicates have entered the market in recent months. Since the start of 2009, Aspen, Beaufort, Beazley Furlong, Hiscox, Kiln and Sagicor have established new syndicates at Lloyd's – no small indication of confidence in the market.

Lloyd's has been perceived by some commentators as a relatively safe harbour amid the continuing financial storms. And while losses elsewhere in the insurance industry have been severe, the 2008 results coming out of Lime Street in recent weeks have been far more encouraging. Syndicates have, by and large, escaped exposure to some of the more esoteric financial products that have hit balance sheets elsewhere.

In March, despite an increase in net impact from Hurricanes Gustav and Ike to $41.3m, Omega posted profits of US$28.2m and revealed that exposure to Madoff- or Stanford-related claims was negligible. Hiscox posted a profit of £237.2m with a combined ratio of 84.4%, while Brit – despite shouldering an increase in Gustav and Ike claims to $112m – also posted a profit of £89.2m. And the list goes on. Profits may have declined, but they are still, even after such a tumultuous year, profits.

Commenting on Lloyd's overall results, Andrew Hubbard, Head of Insurance Services at accountancy firm Mazars, said: "Although Lloyd's overall investment returns are at their lowest level for the past five years, this is a creditable result in the current financial climate and vindicates the conservative investment policy consistently adopted by Lloyd's."

Understandably, some of the positive aspects for Lloyd's have arisen from outside the market. At Brit, for example, the strengthening US dollar provided a real boost to results, with net foreign exchange gains of £124m compared with £18.6m the previous year – a pattern replicated in numerous other results. And there can be little doubt that the dramatic strengthening of the dollar, which started last year, has proved to benefit EC3 players more generally, as it provides a much greater incentive for brokers to place business with Lloyd's.

Though it is likely that these exchange gains may reverse next year, while the exchange rates remain favourable, brokers and underwriters alike are smiling. Neil Coulson, a partner at CLB Littlejohn Frazer says: "Based on what I've seen from results coming out, businesses seem to have seen an increase in volume due to the increased value of the dollar and the euro. The whole scale of income has gone up by about a third, which has obviously had a positive effect on results."

"In terms of investments, many of the syndicates have been quite cautious," he adds, "not going for too risky ones and instead plumping for government bonds, which has generally been a wise move – though most have still had a very difficult investment performance."

Despite the talk of rate rises this year, the reality has been that they have been slow in coming in some classes. Yet the classes in which Lloyd's specialises – the big ticket property, marine and aviation risks on which it has built its reputation – rates have been steadily moving upwards and showed definite increases at 1/1 renewals. And for exceptionally volatile areas such as Gulf of Mexico windstorms or mining – both of which saw the loss ratio explode last year – there's little doubt that rates are absolutely surging.

The signs from the analysts are similarly upbeat. "As with other Lloyd's insurers, we have recast our forecasts on the basis that underwriting conditions are expected to improve modestly in 2010 and more in 2011, although from a worse than previously expected base in 2009," commented Keefe, Bruyette & Woods analyst Chris Hitchings on Amlin.

And it's clear that the market shares such optimism. Matthew Fosh, Chief Executive of Novae, is similarly upbeat in predicting a hardening of rates across several lines as a response to both capital erosion and a difficult recent claims environment. "We relish the opportunities that the next few years will bring."

REASONS TO BE CAUTIOUS

Although the interest shown in Lloyd's by a number of new syndicates demonstrates the (re)insurance market's faith in Lime Street going forward in 2009, there are still reasons to be cautious. After all, although certain lines are experiencing propitious conditions, these come at a price. For example, the Lloyd's Franchise Performance Directorate has suggested significant changes to Gulf of Mexico windstorm terms and conditions, such that buyers can expect retentions to be between 2.5% and 5% of total insured value (TIV) of the assets insured. Policy limits are generally restricted to between 12.5% and 25% of TIV, depending on the total value of the buyer's assets, its spread of risk and its individual risk profile. And for mining, a lack of capacity has meant that prospective leaders at Lloyd's are understood to be demanding similarly stringent conditions.

According to one senior broker: "There's little doubt that a lot of the Lloyd's following market simply isn't going to want to touch these large risks this year, and even the leaders have become a lot more cautious. So, business could go to other local markets who are prepared to take it on."

"We relish the opportunities that the next few years will bring"

On another level many commentators expect to see a rise in claims frequency across the industry as the recession starts to bite. But while the current economic conditions will continue to put businesses and insurance buyers under pressure, for the short to medium term, there will be opportunities for insurers at the same time. As Lloyd's Chairman Lord Levene has pointed out, insurance is largely a non-discretionary product and, while asset values will fall, many businesses will go to greater lengths to protect their assets and shareholders. M

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LEAN AND GREEN

How the Lloyd's building is reducing waste and saving energy

REDUCING LLOYD'S ENVIRONMENTAL impact isn't quite as simple as putting out a few recycling boxes or turning off light bulbs. Green champions and new technology are part of a scheme to reduce the Lloyd's building's energy consumption.

When the building was constructed in 1986, it was groundbreaking. "At that stage, the whole focus was on reducing usage of utilities and trying to get as cost-effective a building as possible," said John Mitchell, Head of Lloyd's Property Department. The famous structure, designed by Richard Rogers, has all its pipes, staircases and lifts on the outside of the building. This was mostly to maximise floor space and provide flexibility in its usage, but green elements were also built in.

Some of these systems are still considered innovative today. Air conditioning is distributed by external pipes to the various gallery levels and fed in via under-floor voids. Perimeter triple glazing helps remove heat gain and loss, easing the load on the air conditioning. There is also a heat-retaining slab on the outside of the building that absorbs heat during the day. Lighting is controlled through a centralised system and has automatic controls in meeting rooms, while the intelligent heating system was ahead of its time.

However, new technology means there are now ways of improving the building's green credentials. A Carbon Trust audit of energy use helped identify areas for improvement. Heating systems have been enhanced and waste reduction has become more important. "One example is putting variable speed motors onto the fans and pumps, which means you only use the amount of energy that the pump requires," Mitchell added.

Water usage is also being monitored. New taps have been fitted with built-in aerators to reduce the amount of water needed, while in the basement there is a new water bottling plant, using filtered tap water to replace bought-in bottled water.

Lloyd's has purchased green energy since 2008 – a combination of wind, water and solar energy. "Buying green energy shows businesses are committed to reducing their carbon footprint and will hopefully encourage others to follow suit," said Simon Harper, Commercial Manager at Lloyd's Property Services.

Recycling efforts were stepped up at the start of 2009. Catherine Opoku, who is in charge of recycling, says there has been a good response – partly driven by 'green champions' staff with a personal interest in the environment, who help get the message across.

Dealing with large volumes of paper, bottles and cans for recycling requires the right equipment. "A system in the lower basement of the building comprises an on-site compactor, a baling machine for cardboard and a glass crusher," said Opoku. "The fact that we've got equipment on site to deal with it makes a big difference."

Lloyd's has also introduced a 'wet recycling' waste stream, which turns food waste and compostable food packaging into compost for agricultural and garden use.

> Lloyd's has purchased green energy since 2008 – a combination of wind, water and solar energy

GREEN POLICY

- The primary objective of Lloyd's Environmental Action Plan is to reduce energy consumption
- Lloyd's also supports the ClimateWise principles, which focus on encouraging more climate-friendly behaviours among insurers, incorporating climate change into investment strategies and urging companies to analyse the risks of climate change

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LCC tour to Singapore and Malaysia

THE LLOYD'S CRICKET CLUB (LCC) tour to Singapore and Malaysia was hailed a success when the team returned to London in early Spring.

The team, which represents a diverse swathe of the Lloyd's market, was undefeated in the three games it played in Singapore. The LCC beat the Misfits XI at Ceylon Sports Club with half centuries from Kevin Barrett of Liberty Syndicates and James Woods of The Oval Group. The team enjoyed another victory in a tense game against the Singapore Cricket Club at SCC Padang. At Kallang Cricket Ground, the weather proved to be equally formidable as the team's opponents – the Singapore Cricket Association – and a heavy thunderstorm forced the teams to abandon play.

LCC XI at the Ceylon Sports Club

Over the Malaysian boarder in Kuala Lumpur, another thunderstorm hampered a well-poised match against the Royal Selangor Club, while the Malaysian Cricket Association President's XI, which comprised some members of the national team, defeated the LCC by 90 runs.

Mark Bromage of broker Nausch, Hogan & Murray and tour manager of the club said: "The standard of cricket was high while the conditions were pretty tough – the humid and oppressive heat was very much a challenge for us."

"It is worth pointing out," Bromage added, "that James Wood showed remarkable stamina, opening the batting and keeping wicket impeccably throughout. Akshay Reddy also did a great job as tour skipper – and Steve Cooper is particularly worthy of mention for his seemingly boundless energy, as one of the elder statesmen of the side! Everybody worked very hard in difficult conditions."

Between games, the team enjoyed several opportunities to meet with local insurance professionals, including a lunch sponsored by PWS East Asia and THB Asia Pacific Holdings, a barbecue hosted by Newline Asia, a cocktail reception hosted by CSL Global and a golf day sponsored by adjusters Braemer Steege.

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20 years of community support

LLOYD'S COMMUNITY PROGRAMME (LCP) celebrates its 20th anniversary in 2009, making it one of the longest-running community involvement schemes in the City of London. The programme provides volunteering opportunities for individuals and companies at Lloyd's to give their time and share skills in an effort to improve the opportunities of people living in the local community.

Launched in 1989 by HRH the Prince of Wales, LCP has worked to address some of the main socio-economic challenges of Hackney and Tower Hamlets in East London, an area that has some of the highest social deprivation statistics in Britain.

Over the past two decades, LCP has gone from strength to strength. In 2008, more than 900 volunteers from more than 60 companies in the Lloyd's market took part in a range of volunteer opportunities in East London. This year, LCP aims to reach a target of 1,000 volunteers.

There is a wide range of volunteering opportunities for Lloyd's people to get involved with, including: helping children with literacy and numeracy skills; sports coaching; developing skills to help young people get a job; sharing skills with community leaders or even lending a hand on a local city farm.

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To find out how to get involved, visit www.lloyds.com/community or email communityaffairs@lloyds.com

EVENTS

27 MAY 2009

Spanish Insurance Week 2009

Lloyd's will be hosting its own conference in Madrid, with a replica Lloyd's Underwriting Room for local insurance professionals to meet with Lloyd's managing agents and brokers.

31 MAY – 5 JUNE 2009

Lloyd's US Broker Programme

Lloyd's will present a one week programme designed to familiarise up-and-coming brokers from the US with the Lloyd's Market.

In tune

London Phoenix Orchestra (formerly the Insurance Orchestra) presents a festival of music on 2 July, 7.30pm at St John's, Smith Square, London SW1. Dvorák's vibrant Carnival Overture will be followed by the romanticism of Tchaikovsky's Violin Concerto, played by up-and-coming fiddler Fenella Humphreys. The programme is rounded off by Stravinsky's most colourful ballet, The Firebird. Truly a feast for all music lovers!

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> The IMF expects Brazil to be a strong performer this year

VIEWPOINT

RICHARD WARD
Lloyd's Chief Executive

VIEW from the WARD ROOM

The current financial crisis has shown how closely connected the world is today. However, it also shows that the world is changing. Emerging markets are becoming more powerful and are having a greater say in how the global economy runs.

It is what commentators are referring to as 'a new world order'. You don't have to look any further than the recent G20 meeting in London for evidence of that when we saw both Brazil and China at the table. So where are two of our newest offices in the world? Rio and Shanghai. Last month we celebrated the second birthday of Lloyd's China in fitting style, by opening Lloyd's Brazil on the same day. The IMF expects Brazil to be a strong performer this year, and for a country with very rare occurrences of natural catastrophes and the largest insurance market in Latin America, we are excited by our future there.

This increased globalisation is not new to our industry. Of all sectors, insurance and reinsurance is perhaps the most global. For that reason Lloyd's believes that we must avoid creeping protectionism that may come with the changes we are seeing.

Regulation is an important consideration, and what we need as the world changes is much greater co-operation and mutual recognition between supervisors across all areas of financial services, from both the developed and developing world. Only by working together can we build the effective and efficient infrastructure that the insurance and reinsurance markets need in this new world order.

Photo/Paul Stuart/Phil Adams