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PRIME STORY

Adaptation and Mitigation Measures - I

The previous two issues of “MEDIAN” have dealt in detail about the challenges posed by climate change and how the associated risks are endangering our lives and living. We can no longer remain oblivious to this stark reality that the very existence of living organisms on our planet earth will be at peril, if appropriate risk management, adaptation and mitigation measures are not taken at the earliest. Of course the metamorphosis taking place in our environment because of climate change may be slow, but they are very steady. It is certainly beyond our power to halt the impacts, but they can surely be attenuated and we have to try all possible ways and means to achieve the same.

We are aware that the world leaders under the authority of UN are trying to work out a consensus in shape of a climate treaty and its mandates to be followed by the developed and the developing nations of the world. Even prior to that, it would be worthwhile to create more and more of public awareness about climate change and its impacts. A decade ago, only a small group of scientists and a smaller group of policymakers were aware of the threats from climate change. In the ensuing decade, the concerns for environment and climate change have got mainstreamed. In all fairness of things, increased awareness would result in a number of individuals and organisations propagating it, working for it and making a difference. Ours is such a beautiful world and if each one of us become eco-friendly and we do even a little bit to help our fight against global warming, we can admirably nurture our mother earth. Creation of public awareness also means sharing knowledge of best practices both within and outside the country. This would ultimately lead to spearheading the search for solutions to climate change at the level of individuals and organisations. Practical measures which reduce vulnerability to the impact of climate change are described as “adaptation”. Armed with their highly educated, healthy and skilled workforces, industrialised countries are already committed to defensive projects like new-patterns of agriculture anticipating floods, coastal erosion etc. Adopting drought – resistant crop varieties, improving soil, forest and water conservation are very costly technological propositions with price tags of millions of dollars, which is not at all problematic for developed countries. But these are much more formidable tasks for the people residing in developing countries, where vast majority of the population can manage only to remain absorbed in making their both ends meet. Even for a rapidly growing economy of a country like India, Development versus Environment is a big dilemma. Capping carbon emissions could reduce growth. And growth or development is the only way out of poverty. Therefore, the challenge for us is to satisfy both the ends, which is to look beyond mutually exclusive solutions.
That means we have to discover win-win paths to development. It is possible only through more and more of awareness and education so that we are in an elevated position to welcome and embrace practical and energy efficient alternatives, which can ensure development without any disturbance to our eco-system. This is how we approach adaptation and development as two sides of the same coin. Our commitment to adaptation will ensure that the climate change issues get absorbed into local development plans and thus the existing community experience of coping with the threats of variable climate is buttressed.

Let us now ponder over a little about our habitats and habitations. A vast majority of us in India are largely concentrated in geographical locations known as villages situated in rural areas of the country. These are the centres of poverty. The population is primarily dependent on rain-fed agriculture for subsistence and livelihood. Poor families are still ill-equipped to respond to changing rainfall patterns and shorter growing season caused by warmer days and nights. Strategies to achieve the United Nation’s targets for global poverty reduction known as Millennium Development Goals (MDGs) are being jeopardized by climate change impacts. As per estimates of the World Bank, almost 40% of aid projects could be bereft of success because of unanticipated climate risks. Hundreds of millions of the world populace is already distressed from the impacts of changing climate. Thus their efforts to eradicate poverty from villages are frustrated. It is also very important at this stage to understand that global warming is rarely the sole cause of climate related humanitarian suffering. Invariably mis-management of local resources is a major factor. For example, overgrazing of pastures results in desertification. Similarly, deforestation exacerbates flooding. This is why mass awareness and education programmes can play a big role in motivating people in the rural areas to take up various adaptation measures to wage a valiant war against the ravages of climate change and also to put an end to mis-management of local resources. They could be trained to use bio-fuel and to generate power through green sources. They could be inspired and instructed to use rain water watershed harvesting system. The rural economy shall then be vibrant and everyone in villages will have access to clean energy and clean water. That means rural habitats would be eco-friendly and can finally aim at complete carbon neutrality. A success story of adaptation at village level is given below.

Wankute is a village in Samgamner Taluka of Maharashtra’s Ahmednagar district. The villagers began with the slogan of voluntary labour for village development and their efforts culminated in formation of Jai Malhar Rainwater Harvesting System in the village. Wankute has now emerged as an Oasis of Hope that can fend off the worst of droughts. The Jai Malhar Watershed Committee was one of the recipients of the JSW – The Times of India Earth Care Awards – 2010. The Watershed is now managed by a Committee elected by the village members, which ensures that irrigation needs of all the cultivable land of the villagers are met properly and not a drop of water goes waste.
Mckinsey – the global consultancy group has projected that the number of people living in Indian cities will grow from the present estimate of 340 million to 590 million by the year 2030. At present only about 30% of 1.1 billion Indian population reside in urban centres. The remaining 70% dwell in villages in the rural areas. In near future, many new cities will emerge in India. This is a great opportunity for us to create green and eco-friendly cities we would like to have in the present situation of changing climate. It is the time we consolidated our ideas about the profile of a city we should have. The optimum level of population should be our main concern because increasing concentration of population adds to pressure on resources and leads to severe resource crunch. With increasing wealth and hence increasing per capita energy consumption, the threat of climate change looms large. So modern cities have to address better living standards with reduced emissions so that they can progressively move towards carbon neutrality. Ideally a city should have a population of not more than five million. It should generate its own power through green sources in order that everyone has access to clean energy and clean water. People should use bio-fuel and insist on rain water harvesting. It should be full of parks and trees.

Worldwide transport causes 13% of emissions. Every litre of petrol or diesel burnt in vehicles contributes 2.7 kg of carbondioxide emissions equivalent. On an average, a car would emit about ten tonnes of carbondioxide per year. Bicycle could be a healthy option. Hybrid cars and other means of public transport, which use solar and bio-fuel energy need to be encouraged through public awareness drives. Buildings use 50% of global energy. Energy efficiency measures can reduce the use of energy atleast by half. Emerging trend of intelligent buildings and green buildings entail the use of eco-friendly designs, smart materials and modern technology. One of the quickest path to achieving carbon neutrality is to transform the way energy is generated and supplied. The present system of generation and supply accounts for more than 26% of emissions. This can be avoided via garbage – fuelled electric power – plants spread across the cities. Such a power – plant can generate 5800 MW of power. Similarly, wind and solar energy plants can also be used to supplement conventional power sources.

Our future cities will have to create mini-forest eco-zones, wherever possible. These forests can be planted with high growth varieties attracting a diversity of flora and fauna. With proper awareness and education programme, school children, youth and general public need to be mobilised to populate these eco-zones with trees. Every tree is capable of absorbing 20 kg of carbondioxide every year. These measures are bound to reduce emissions drastically.

This is how a combined, integrated and participative approach to adaptation can make the dream of carbon neutral villages and cities a reality. And as a result, the threats of changing climate can be tamed.

…. (to be continued) .. 6/
NON – LIFE

BRIGHTER FUTURE FOR CREDIT SECTOR

Psychological issues have dented confidence in the Credit Reinsurance market, but interest has returned, improving conditions for Insurers. But it is not a market with universal appeal. Just two years ago, Swiss Re signaled its intention to pull back from the Credit Reinsurance sector. However, conditions have changed. The future will not be like the past. Earlier, it was a limited market in terms of players on the Reinsurance side. Ceding Companies would place quite huge stakes with one of two players, putting quite a few eggs in not many baskets.

Psychology is a big element. The “Credit” name suggests that the line of business is closely linked to the financial markets and banking business, so people get nervous. The financial market crisis had an impact on perceptions. In the middle of an economic crisis, one never knows how deep or long it will be. The volatility of the economic environment is still quite big. It seems as thought things have stabilized.

ENERGY MARKET

An increase in the limits of coverage required for operators under the Offshore Pollution Liability Association (OPOL) is expected to drive more business into the Energy Insurance market. All offshore operators active in Exploration and Production (E&P) on the UK Continental shelf are party to OPOL, with some offshore areas in north-west Europe also subject to the regime. OPOL was set up in 1974, with the aim of making offshore companies accept Strict Liability for Pollution Damage and the cost of remedial measures. The operators have to show that they can meet their obligations to claims payments arising from OPOL by proving that they have sufficient insurance, self-insurance or whatever other means at their disposal. When the Agreement first came into effect, the Limit was set at USD 16 m, which later rose to USD 120 m. But the members of OPOL agreed recently to more than double the existing limit to USD 250 m.

The ”Deepwater Horizon” incident put aside what clients desired to purchase and there does appear to be a regulatory desire to raise limits. Clients can decide whether to buy insurance, but with Governments imposing greater limits, they will look to insurances as a form of risk transfer. It sounds encouraging for underwriters to consider the potential application OPOL
limits in relation to other potentially available coverages such as OEE (Operators’ Extra Expense) and TPL (Third-Party Liability). The amendments to OPOL come some four and a half months after the “Deepwater Horizon” platform caught fire and subsequently sank, causing the worst environmental disaster ever to befall the US.

**FOSSIL FUELS**

Although plans for the introduction of low-carbon technologies like nuclear, solar and wind are becoming more and more ambitious, the simple fact is that it will be many years before the world’s consumption of fossil fuels starts to tail off in any meaningful way. Millions more tonnes of carbon dioxide will go up the stack and play their part in inducing climate change before low-carbon technologies can sensibly take over.

Is there any way these emissions can be avoided? The answer could lie in Carbon Capture and Storage (CCS). CCS is the process by which carbon dioxide is separated from the other exhaust gases produced in the industrial combustion of fossil fuels and stored at suitable onshore or offshore underground locations. CCS has the potential to drastically reduce the amount of carbon dioxide emitted by fossil fuel-powered industry. If it is wholeheartedly embraced and adopted, we will be able to continue to use fossil fuels without any major downside until low carbon technologies arrive on the scene. Although many of the constituent parts of CCS have been tried and tested in other contexts, experience of all the parts working together as one is very limited. Demonstration Projects are being planned and financed in an effort to demonstrate that CCS as a whole can be made to work.

**INSURER OPPORTUNITIES**

It is becoming clear to Insurers that climate change is leading to a range of exciting opportunities. For example:

- The possibility of investment in completely new asset classes such as renewable energy;
- The possibility of making profits through carbon trading; and
- The possibility of insuring novel aspects of renewable energy projects and low carbon technologies.
Carbon Capture and Storage (CCS) represents for Insurers just one possible opportunity of many arising out of climate change. The potential scale of its use in the future is enormous. Although it is still some way off widespread use and the nature, timing and size of some of the potential liabilities of operators under the proposed licensing regime are not clear-cut or conventional, insurers should be monitoring the development of this technology with great interest.

**FOCUS ON AGGREGATE LOSSES**

Aggregate exposures will be at the forefront of energy underwriters’ minds in the wake of the “Deepwater Horizon” loss. Underwriters had a lucky escape with BP taking the self-insurance route, but that does not mean lessons can not be learnt. There needs to be a focus on Aggregate – what “Deepwater Horizon” should have identified is how much exposure you can have with different companies on one incident. The fact that BP did not buy insurance is really helpful. With BP the main operator on the Macondo Well, it is likely to bear the brunt of claims. But other companies, such as Anadarko, Mitsui, Cameron International and Haliburton could also find themselves in the firing line. Although BP does not insure itself in the commercial market, these other companies do and the same insurers appear on many of these slips.

In the general offshore energy market, rates have increased in all lines in the aftermath of the diameter. Although the “Deepwater Horizon” loss played a major part in rates increasing, there were also other factor plays as well.

“Deepwater Horizon” is the biggest, but there are a lot of other losses coming through. There is absolutely no doubt with the “Deepwater Horizon”, “Aban Pearl” and “West Atlas” losses, Insurers spent all the premium income and rates must go up accordingly. At the same time, Insurers are dealing with clients, who are considering buying bigger Limits for certain coverages. There are suggestions from various bodies that they will be imposing larger Limits, particularly with regards to Pollution.

While rates have already risen, it is likely that there will be further increase at the start of 2011. Rates have increased on the property side and the liability side, but what is not evident yet is the further increases, when it comes to the Reinsurance Renewal season at January 2011. But the level of rate increases imposed may still not be sufficient and the potential remains for a whole new take on writing offshore energy business.
FOCUS ON DISCIPLINE

A dramatic rethink is required among Energy Insurance underwriters to correct the “unacceptable” 125% five year loss ratio the sector has reported. Owing to a series of high profile losses during the past few years, the Energy Insurance market’s premium base is growing – something that is a definite plus point for the sector’s underwriters. But, this is being offset by a series of significant negative factors.

On the positive side, premium base is growing. Developing technology and the push into deep water is evidence of a healthy exploration and production sector. The price of oil is significantly higher than it was earlier in the decade. The belief now is the price of oil is at a permanently higher base level than it was back in the 1990s and earlier in this decade. This has contributed to the overall increase in the values of offshore assets.

This has been offset by a series of negative issues that have affected the market. In the past year, we have had three major mobile rig total losses – the “West Atlas”, “Deepwater Horizon” and “Aban Pearl”. Additionally, attritional losses have increased in virtually every line of business. The five year loss ratio from 2005 to 2009 is at 125% without the full effect of “Deepwater Horizon” – clearly an unacceptable result.

The market’s overall loss ratios are trending higher inspite of the increased premium base, a situation of a disturbing trend, given the fact that market is still running deep deficits from the wind events of recent years. This is one of the biggest problems for the energy market: it is still reeling from the substantial windstorm losses of 2005 & 2008 and now the sector has been hit by a series of major non-storm related catastrophes.

Consequently, underwriters must look at their books and take an even tougher stance on some portfolios, subjecting them to greater analysis. Heightened wind activity has been followed by heightened loss activity. All of this points to a market need of underwriting discipline in the form of higher rates and adequate deductibles.

INDIA’S DRIVE FOR SHIPS

India’s flag has never been more popular and is set to grow through increased trade as the economy expands. With Indian shipowners on an asset buying spree, total domestic tonnage flying the Indian flag has crossed the 10M gt mark for the first time. As of 1st September 2010, a total of 1,029 ships with 10.1 M gt are registered under the domestic register. Of this, 336 vessels are in overseas trade, while the remaining 693 ships of about 1 M gt are engaged in coastal trade.
Indian economy is growing rapidly and it needs more ships. India is now importing more crude oil and coal, and exporting more iron ore. Shipping companies are looking to acquire more ships under the Indian flag, seeing a further rise in the tonnage.

In 2004-05, the Government introduced a tonnage tax system in order to help shipowners compete and to promote expansion of the fleet. India has allowed 100% foreign direct investment in its shipping sector, although little actual foreign funding has come to the shipping market. Indian tonnage has steadily grown over the past five years from the 6.94M gt that was registered under the country’s flag as of 01st April 2004.

**LIABILITY CHARGE - “MSC CHITRA”**

The Indian Coast Guard asked the owners of fully cellular containership “MSC Chitra” to pay INR 25 m ($562,493), to cover operations carried out to contain oil spill damage caused by the vessel after it collided with bulk carrier “Khalijia 3”. The two vessels crashed off Mumbai harbour on August 7, 2010 causing a huge oil spill that resulted in ecological damage. The State Government sought INR 30 m from “MSC Chitra” for clean-up operations carried out off the coast, after it identified the vessel as a “polluter” following the collision. The Coast Guard was claiming for the rescue of crew members from the vessel immediately after the mishap, for monitoring the spread of the oil spill and for spraying thousands of litres of chemical dispersants on the sea to control the spread of oil. Other operations that were subsequently carried out, such as helping the Navy clear the navigational channel (several containers were floating in the water) also incurred costs. Earlier, the Mediterranean Shipping Company (MSC) purportedly reported at least 189 containers from the “MSC Chitra” were missing, eight of which contain toxic materials. Six of the remaining eight contain sodium hydroxide, one contains organic pesticides and another contains aluminium phosphate tablets.
INTERNATIONAL

PIRACY - A PROBLEM

Actuaries are struggling to price the cost of piracy to the maritime and insurance industries accurately owing to a lack of reliable data. Pirates off the coast of Somalia are enhancing their activity after the end of the region’s monsoon season, with vessels in the area once again at threat of being hijacked. A new Report, compiled by the Acturial Profession has revealed the true cost of piracy to the maritime industry and therefore the associated insurance industry is still too difficult to quantify with any real accuracy. The scarcity of statistics on maritime piracy around the world makes the true estimation of risk difficult to measure, the Report explains. Piracy attacks have been on the increase in the past 15 years but since 2006, the level of attacks has increased by an average of 125% and this is almost entirely due to the attacks of Somali pirates.

Using publicly available data, the Report suggests that each attack costs those who have fallen foul of the pirates something in the region of $9m. And with a success rate of around six per 1,000 transits, this produces kidnap and ransom rate of around $57,000 a vessel when traversing the Suez canal. However, this is based on judgement, not on strict modelling. Without accurate figures, uncertainty will remain – future costs may be significantly different.

Actuaries, who have an increasingly prominent role in the marine insurance market, face considerable challenges when pricing products as a result of the lack of data available to them. With statistics relating to piracy thin on the ground, they are struggling to price cover accurately. Firstly, despite the increase in piracy attacks, the numbers are still relatively small. Secondly, the information about the attacks issued by shipowners is often vague. The monsoon season tends to signal a downturn in pirate activity owing to poor weather conditions. This year’s season carried on until the second week of September 2010.

Figures from the international Maritime Bureau show that at least five vessels have been hijacked in the Gulf of Aden and the vast expanse of water off the east coast of Somalia since the end of the monsoon season. The latest vessel to have succumbed to an attack was Panama flagged general cargo vessel “MV Izumi.”
SEA RISE

Average global sea levels are rising at a faster rate than at any point during the past 7,000 years. However, there are uncertainties about the actual rate of rise and strong regional variations. The volume of the oceans is increasing at a rate that may become comparable to that achieved at the end of the last glaciation. This is likely to have geological impacts on coastlines and volcanic activity. Climate change and sea level are linked. Climate change affects sea level and the changing sea level transmits the effect of climate change throughout the earth’s coastal regions.

SOLVENCY II

Insurers need to be more selective when it comes to choosing which technological changes they instigate as part of their Solvency II implementation. In some cases, Insurers may be doing more than they need to, as fears of the cost of Solvency II will eat up many Insurers’ entire change budgets continue to proliferate. It is quite difficult to differentiate between what is a Solvency II project and what isn’t. There are lots of efficiencies, lots of data improvements and lots of systems upgrades planned. But which ones are required actually to meet Solvency II commitments.

Solvency II can be compared with the “Millennium Bug”, which led to many corporates across different sectors rushing to upgrade their systems to ensure that there were no computing problems, when the year 1999 changed over to 2000.

MICROINSURANCE

Insurers will need to harness new technology, if they are to generate potential revenue from the microinsurance market. There are four billion people living in developing countries and the potential insurance market that exists within these countries is vast.

For underwriters, the key is to keep the process of selling a Policy as simple as possible, thereby reaping as much benefit from the premium as possible.
SAFER CITIES

Cities across the world have been taking steps to make themselves better prepared for catastrophes amid calls from the United Nations (UN) for all stakeholders to play their part in coping with natural hazards. October 13 marked the annual UN International Day for Disaster Reduction and a series of events took place, as cities joined the 120 already signed up to the UN’s “Making Cities Resilient” campaign, which was launched last year.

In Egypt, three cities joined the campaign – Cairo, Alexandria and Sharm El-Shaikh – and meetings took place with Insurers in an attempt to improve the resilience of the cities. Lebanon hosted a celebration, as Beirut also joined the campaign, while other cities across the world joined in by hosting events to promote effective disaster risk reduction measures. Since the campaign was launched last year, a large number of efforts have already been made to boost resilience. In Mexico City, around 10,000 civil servants are being trained to better protect the city from earthquakes. Amman in Jordan is implementing a disaster risk-management master plan, while Colombo in Sri Lanka is expanding storm drainage system and a tree maintenance unit to reduce storm damage. Saint Louis in Senegal is taking new measures to prepare its city to cope with coastal erosion. And in El Salvador, a national conference was held on urban resilience. While it was impossible to stop cities growing, it was possible to plan them in a more sustainable way. This does not require huge amounts of new resources, but different ways of using existing resources. It requires better co-ordination between all actors and use of good practices that have been already tested.

By 2030, two billion people will live in slums and 60% of the world population will live in urban areas. Cities will continue to grow, as they represent economic growth, job opportunities, education, culture and modern life, but risks will continue to accumulate as well.

Figures produced by the Centre for Research in the Epidemiology of Disasters (CRED) show more than 236,000 people have been killed by disasters so far in 2010, with nearly 256 million affected by earthquakes, floods, tropical storms and landslides. CRED estimates indicate disasters this year cost countries $81 bn upto the beginning of September 2010, of which less than one – quarter is expected to have been insured.
The reinsurance pursuant to which the dispute had arisen, covered OMEX in respect of its liability arising out of or in connection with the activities of the original insured, during the period from July 1, 2001 to December 31, 2002.

It was written in “Slip Policy” form and incorporated various Standard London market Clauses. The reinsurance was also subject to a Claims Co-operation Clause, expressed to be a Condition precedent to reinsurers’ liability, which provided “interalia” that:

“The Reinsured shall, upon knowledge of any loss or losses which may give rise to a claim under this Policy, advise the Reinsurers thereof as soon as it is reasonably practicable and in any event within 30 days.”

However, the reinsurance was silent on the question of its Governing Law and the Jurisdiction under which any disputes under it were to be resolved.

The “Stonebridge” decision provides both a useful summary of the factors which may be taken into consideration by the English Court, when considering the Governing Law of a Reinsurance Contract, which is silent on the issue. It confirms that a reinsurance placed in the London market by London brokers is likely to be found to be subject to English Law absent any indication to the contrary and particularly if it contains Standard London market Terms.

Once a reinsurance is found to be subject to English Law, this case makes clear that the English Court is also likely to reach the view that it is the most appropriate forum to handle matters of English Reinsurance Law.
LIFE

RURAL PRODUCTS

The future growth of the insurance industry in India lies in designing products that address the needs and aspirations of the people living in rural areas, according to the Insurance Regulatory and Development Authority (IRDA).

This thought was floated at the recent launch of India’s first health plus life insurance combi product.

Those in the low income strata would benefit from a single product that could take care of all their exigencies.

GLOBAL PREMIUMS FALL

Global life insurance premiums fell 2 % to USD 2332 bn in 2009, the latest Sigma Report from Swiss Re has concluded. Premiums were hit hardest in the US and UK, with premiums dropping 15% and 12 % respectively. In the US, life premiums dropped from USD 578 bn in 2008 to USD 492 bn last year, while UK life premiums dropped from USD 286 bn in 2008 to USD 217 bn last year.

Growth was the strongest in South and East Asia at 10 %.
REINSURANCE

UNCERTAINTY AMONG REINSURERS

Bar a major cat before year-end, the reinsurance market will find it hard to maintain underwriting discipline for 1/1 renewals. Not for the first time, it is hard to know exactly where the reinsurance industry stands, such are the conflicting signals the sector is emitting. By some measures, the reinsurance sector is in rude health, having rebuilt its capital position in impressive fashion following the damage caused by the credit crisis. Yet, with the upturn in major loss activity this year, underwriting results are coming under pressure and the market shows no sign of reversing the soft trading conditions.

Global reinsurance capacity increased 10% during the first six months of the year to reach USD $ 442 bn, up from USD $ 402 bn at the end of 2009. Growth slowed in the second quarter of 2010 owing to the higher level of share buybacks and the impact of currency translations. It expects buybacks to be down in the third quarter because of uncertainty about the severity of the North Atlantic hurricane season before picking up again in the last quarter of the year. By contrast, primary insurance capital grew just 2% in the first half of 2010, reflecting further pressure on rates and tough investment conditions.
We value feedback.

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