



STEAMSHIP MUTUAL

Pre Renewal Report 2011



Life at sea...

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Overview

It is now clear that the consequences of the financial crisis of 2008 will be with us for some time. The debt overhang both sovereign and private will not be easily or quickly resolved, especially at a time of slow economic growth. The ramifications for shipping are extremely serious; banks are reluctant or unable to extend credit, trade is constrained and freight markets stressed by an oversupply of tonnage.

Shipping faces the most difficult conditions for 30 years. In such circumstances the Board is determined to ensure that the Club is steadfast in its support of the Membership.

That means the provision of the most efficient level of service possible and a stable financial base, objectives the Club continues to meet. However, the pressures of claims inflation and the replacement of older higher rated tonnage by newer lower rated tonnage ('churn') mean that a general increase in premium is necessary. The Board has set a general increase of 5% plus a small increase in deductibles.

In most years the Club expects and has in fact benefited from, a reduction in prior year estimates. This year there has been some deterioration in the prior year claims figures, the causes of which are set out in the Claims section of this report. The IBNR provision for prior years is set at a prudent level but from time to time it is possible that claims will develop in such a way as to require an additional provision to be made, though of course when this happens it is not welcome. Fortunately, the defensive investment strategy appears likely to deliver a respectable investment return and there is expected to be only a modest reduction in the year end free reserves. The Club's financial position remains strong.



Gary Rynsard Chief Executive Officer

Underwriting and Reinsurance

At 20th November 2011, tonnage had increased by 5.75 million, or 9.9%. As was the case last year, growth in entered tonnage has exceeded the Club's projections for the first nine months of the year. However, it seems unlikely that growth at this rate will be sustained in the present economic climate, and we expect lay ups and perhaps scrapping to increase in 2012.

Churn occurs throughout each policy year, and its effect is to reduce the average premium rate per ton, as the year develops. Nevertheless, it has reduced by about 20% when compared to the same point last year.

In setting a general increase, the Board was mindful of the effect of churn, as well as the potential for claims inflation. That there is such potential – although the downturn may also have the opposite effect – is evident from some prior year claims deterioration, as well as slightly higher claims so far this year when compared to last. Furthermore, claims in the Pool have also been slightly higher than in 2010, with nine notified as at 20th November, although none by the Club.

In the present economic climate, amid concern that the drivers of international trade over the last three or four years will be significantly impacted by the eurozone crisis and by falling demand in home markets, it is extremely difficult to predict how claims will ultimately develop this year, and even more difficult to make an informed projection for next year. The Board thus concluded that a cautious approach towards claims projections should be balanced by recognition that many Club Members are under considerable pressure as a result of these conditions.



Stephen Martin Chief Operating Officer and
Head of Underwriting

At their October 2011 meeting, the Directors decided that there should be a general increase of 5% across all classes of the Club's business, and that deductibles should be raised to a minimum of US\$ 5,000, and increased by US\$ 1,000 if presently below US\$ 25,000. The Directors also agreed to reduce release calls to 5% for the 2009 year, and to 15% for 2010, to maintain the release call at 20% for 2011, and to set it at 20% for the forthcoming 2012 year. As usual, any changes in the cost of the Club's excess of loss reinsurance will be passed on to Members.

Negotiations for the renewal of the International Group's Excess Loss contract have started. At the time of writing, the Group has experienced only one claim exceeding US\$ 60 million in the current year, whilst 2008, 2009 and 2010 are also likely to be good years for the Excess Loss underwriters. This has consolidated the improvements in record which have restored balance, following more difficult years in 2006 and 2007.

In spite of one of the worst years for major reinsurance market losses arising out of the New Zealand earthquakes, Japanese tsunami and Australian floods, the good record of the International Group Excess Loss contract should provide a positive background to the renewal.

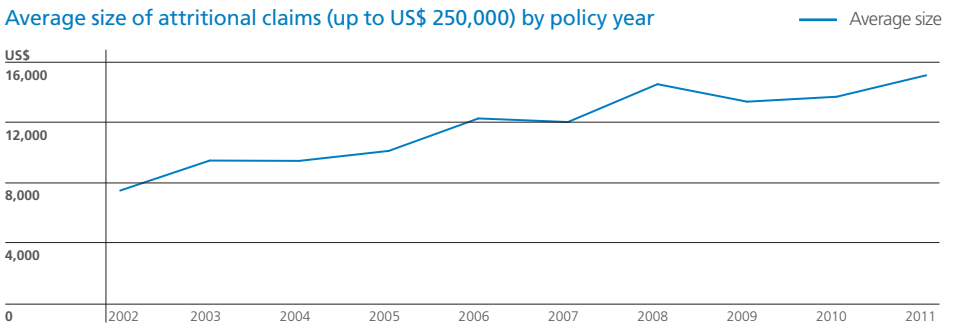


Rupert Harris Head of Reinsurance

Claims

Claims for the current policy year appear to be developing along similar lines to the preceding year with an overall increase in claim cost per ton of less than 1%.

The increase is slightly more marked at the level of attritional claims where the cost per GT for such claims has increased by 2.5%. Moreover, the average size of attritional claims has increased by over 10%. This follows the long term pattern of year-on-year increases, with 2009 being the notable exception, as can be seen from the following graph.



On the basis of claims notified in the first nine months of this year, attritional claims have increased both in number (by nearly 2%) and in overall value (by approximately 12%). The increase is reflected across a majority of claims categories but is most noticeable in respect of crew claims; typically the largest single claim category.

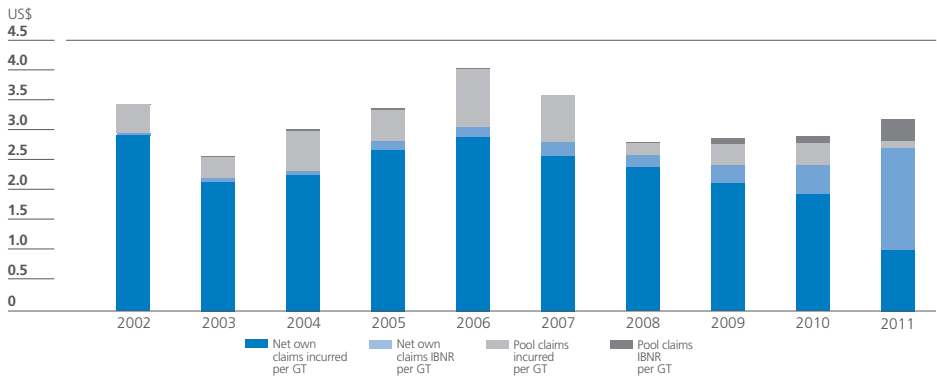


Colin Williams Head of Claims

This increase is mirrored in the larger claims, taken as a whole. However, whereas the increase last year was prevalent in the US\$ 250,000 – US\$ 1,000,000 layer, this year’s rise has occurred in the US\$ 1,000,000 – US\$ 1,800,000 band; being particularly noticeable in the Chartered and Fixed and Floating Objects claim categories. By contrast, claims in excess of US\$ 1,800,000 are lower than in previous years, and the Club has experienced no claims in excess of retention to date. However, such large claims occur quite randomly and cannot be taken as being indicative of claims trends.

A moderate increase in retained claims is projected, as shown in the following graph. Moreover, Pool claims projections continue a steady increase since their low point in the 2008 policy year.

Projected net owned claims and pool contributions per GT by policy year
 Excludes Chartered and Defence claims



Unusually, the projected net cost of claims arising from prior years, including 2010, has increased since February 2011. The majority of this deterioration occurred in the first quarter but analysis does not suggest any clear pattern or single reason for this experience. Moreover, an improvement in the projected net cost of prior year claims has been noted over the second and third quarters; suggesting that the first quarter deterioration was an isolated occurrence. It is anticipated that, overall, a prior year claims deterioration, rather than the more usual improvement, will be reported at the end of the year.

Claims

continued

So far this year, nine Pool claims have been notified, all resulting from collision or grounding incidents. None of these Pool claims involves the Club and only one of them – the Rena – is expected to exceed the upper Pool limit of US\$ 60 million.

The development of claims on the International Group Pool up to US\$ 60 million each claim is set out in the table below. On the basis of the notifications made up to the mid-year point, current year claims are similar to those experienced last year, but not as bad as the 2006 and 2007 years which remain the worst two years on record. However, the most critical months for the Pool are still ahead of us, so it is too early to predict the final outcome for 2011.

International Group's Pool experience

Annual claims development of incurred claims up to US\$ 52 million excess of US\$ 8 million

Data is as at 20th August for each year.

Policy year	2011	2010	2009	2008	2007	2006	2005	2004	2003	2002
2002	207.1	204.1	200.4	196.6	190.4	196.5	187.9	178.3	155.8	6.7
2003	186.7	172.0	179.9	171.3	182.6	189.7	180.9	174.3	53.6	
2004	257.4	256.6	256.2	254.9	262.9	242.6	228.9	33.6		
2005	216.0	216.6	226.4	204.2	196.2	155.5	0.1			
2006	425.3	421.9	441.0	428.1	418.0	66.2				
2007	385.1	389.4	376.3	329.5	77.7					
2008	111.0	114.0	126.4	19.5						
2009	218.0	209.3	48.7							
2010	272.1	62.7								
2011	60.3									

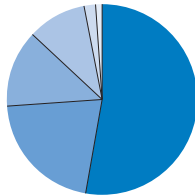
Investments

Global equities and government bond yields fell sharply in the third quarter amid rising risk aversion and concerns that the world economy could slip back into recession. Fears about sovereign debt and solvency in the eurozone, slowing economic growth in China and the US combined to produce the worst quarter for equities since 2008. Strong corporate earnings and hopes of a plan to resolve the eurozone issues led to a recovery in October but sentiment again turned sour in November as slow progress in the eurozone and uncertain political changes continued to put strains on sovereign debt and bank funding.

The combined Club and Trust investment portfolio recorded a gain of US\$ 25.2 million, a 3.1% return, for the first nine months of the year. The matching portfolio, which hedges the economic value of claims liabilities with lower risk government bonds, has contributed a substantial portion of this return.

Combined asset allocation at 20th November 2011

Government bonds	53%
Cash and deposits	21%
Corporate bonds	13%
Alternative investments	10%
Equities	2%
Property	1%



The target allocation for the remaining surplus portfolio includes an 11% allocation to Alternative investments, which complement the returns from corporate bonds, cash and equities. The Board has decided to use up to 6% of this allocation in funds which target growth in emerging market economies.

Low interest rates, central bank support measures and weak growth in western economies are expected to remain the backdrop for investment markets for the next year or two. Volatility is expected to remain high due to macroeconomic events and fragile investor sentiment. In view of this outlook the Board continues to maintain overall portfolio risk below its target range.



Steve Ward Head of Finance



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