AON BENFIELD

Insurance-Linked Securities

Third Quarter Update 2010

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Aon Benfield Securities again presents a quarterly review of the insurance-linked securities ("ILS") market, offering insight into market activity and the innovation which continues to characterize this alternative asset class.

The second quarter of 2010 was particularly active with the issuance of nine catastrophe bonds totaling $2.3 billion in notional value. During that period, sponsors rushed to secure risk transfer capacity prior to the opening of the 2010 Atlantic Hurricane season. Subsequently, the third quarter of 2010 gave rise to only two catastrophe bond transactions, both having wind as the covered peril.

Aon Benfield ILS Indices

The Aon Benfield ILS Indices are calculated by Thomson Reuters using month-end price data provided by Aon Benfield Securities. The ILS indices once again posted exceptional returns for the third quarter of 2010, benefiting from an overall increase in demand for catastrophe risk as well as a loss-free 2010 U.S. Hurricane season through September 30.

The Aon Benfield All Bond Index posted a 4.1 percent return for the three months ending September 30, 2010 compared to 6.0 percent for the same period in 2009. The Aon Benfield BB-rated Bond and Aon Benfield U.S. Hurricane Bond Indices produced similar results at 3.9 percent and 5.2 percent, respectively. Because U.S. Earthquake spreads did not compress as much as other sectors, returns were smaller but still substantial, with the Aon Benfield U.S. Earthquake Bond Index gaining 2.2 percent for the quarter.

Outlook

Factors that influence the Aon Benfield ILS Indices include reinsurance rates, investor inflows and the demand for catastrophe risk in the capital markets. Assuming that there are no significant catastrophe events, we expect further softening of spreads. This will cause prices of current catastrophe bonds on risk to continue to rise.

Aon Benfield Cat Bond Indices By Sector

Index Title	Index Value			Return for Annual Period Ended June 30	
Aon Benfield ILS Indices	**6/30/10**	**6/30/09**	**6/30/08**	**2010**	**2009**
All Bond	220.88	195.73	190.15	12.85%	2.94%
BB-rated Bond	211.90	187.60	184.15	12.95%	1.88%
U.S. Hurricane Bond	213.00	184.92	185.67	15.18%	-0.41%
U.S. Earthquake Bond	188.48	176.08	174.13	7.04%	1.12%
Benchmarks*					
3-5 Year U.S. Treasury Note	300.26	281.65	262.88	6.61%	7.14%
3-Year U.S. Corporate BB+	353.25	308.95	289.15	14.34%	6.85%
S&P 500	1030.70	919.32	1280.00	12.12%	-28.18%
ABS 3-5 Year, Fixed Rate	317.00	265.18	272.09	19.54%	-2.54%
CMBS Fixed Rate 3-5 Year	235.72	185.82	186.91	26.85%	-0.58%

Source: Aon Benfield Securities

Aon Benfield Securities publishes its indices each month on Bloomberg and through the Thomson Reuters online ILS community.

* The 3-5 Year U.S. Treasury Note Index is calculated by Bloomberg and simulates the performance of U.S. treasury notes with maturities ranging from three to five years.

The 3-Year U.S. Corporate BB+ Index is calculated by Bloomberg and simulates the performance of corporate bonds rated BB+ on a zero coupon basis. Zero coupon yields are derived by stripping the par coupon curve. The maturities of the BB+ rated bonds in this index are three years.

The S&P 500 is Standard & Poor's broad-based equity index representing the performance of a broad sample of 500 leading companies in leading industries. The S&P 500 Index represents price performance only, and does not include dividend reinvestments or advisory and trading costs.

The ABS 3-5 Year, Fixed Rate Index is calculated by Bank of America Merrill Lynch (BAML) and tracks the performance of U.S. dollar denominated investment grade fixed rate asset backed securities publicly issued in the U.S. domestic market with terms ranging from three to five years. Qualifying securities must have an investment grade rating, a fixed rate coupon, at least one year remaining term to final stated maturity, a fixed coupon schedule, and an original deal size for the collateral group of at least $250 million.

The CMBS Fixed Rate 3-5 Year Index is calculated by BAML and tracks the performance of U.S. dollar denominated investment grade fixed rate commercial mortgage backed securities publicly issued in the U.S. domestic market with terms ranging from three to five years. Qualifying securities must have an investment grade rating, at least one year remaining term to final maturity, a fixed coupon schedule, and an original deal size for the collateral group of at least $250 million.

The performance of an index will vary based on the characteristics of, and risks inherent in, each of the various securities which comprise the index. As such, the relative performance of an index is likely to vary, often substantially, over time. Investors cannot invest directly in indices.

Past performance is no guarantee of future results.

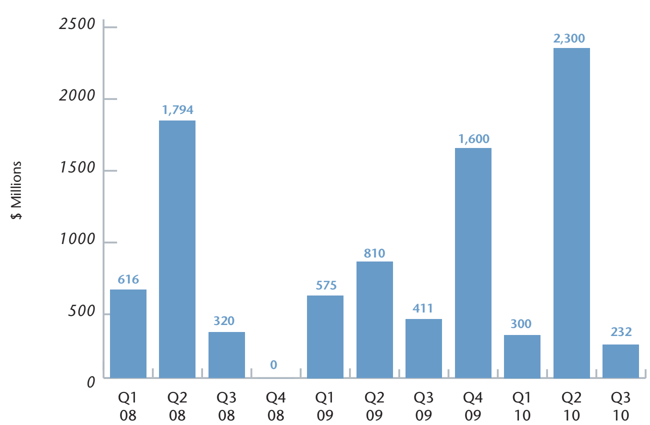
Catastrophe Bond Transaction Review

Traditionally, the third quarter of each calendar year is characterized by light issuance activity in ILS. The trend continued in the third quarter of 2010 as only Shore Re Ltd. and Green Valley Ltd. Series 2 provided an additional $232 million of catastrophe bond capacity to sponsors (note that Green Valley Ltd. Series 2 was issued as €100 million, or $136 million at the then applicable conversion rate).

The $96 million Shore Re Ltd. catastrophe bond provided investors with exposure to Massachusetts Hurricane risk on an indemnity basis, through the Massachusetts Property Insurance Underwriting Association ("MPIUA"). Following on the heels of earlier heavy issuance of bonds offering exposure to U.S. Hurricane, the MPIUA deal was marketed as two separate tranches. At that time, however, most investors had already approached or exceeded their U.S. Hurricane portfolio limits and, consequently, Shore Re Ltd. struggled to obtain its desired capacity. The Shore Re Ltd. Tranche A notes closed with $96 million, below its targeted issuance size of $100 million, and priced at the top end of the pricing range. Meanwhile, the Tranche B notes failed to close altogether.

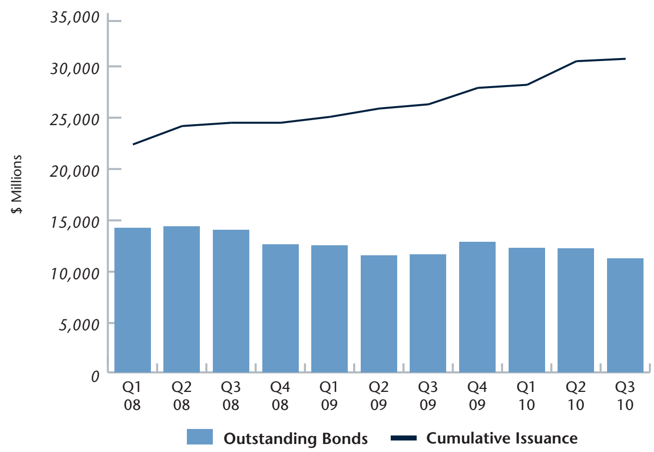
The lack of receptivity to U.S. Hurricane exposed bonds (as demonstrated by Shore Re Ltd.) signaled investors' evolving eagerness to diversify their portfolios by seeking non-peak peril catastrophe bonds. In September 2010, Groupama S.A. responded by providing investors with much needed geographic diversification through Green Valley Ltd. Series 2, a €100 million France Windstorm catastrophe bond with parametric trigger. With Swiss Re as the sponsor (and Groupama S.A. as the reinsured), the Green Valley Ltd. Series 2 deal was the first catastrophe bond issued in the calendar 2010 year that did not include U.S. peril risks. Due to strong investor demand, the transaction was heavily oversubscribed and ultimately priced below the pricing range used during marketing.

Catastrophe Bond Issuance By Quarter



Source: Aon Benfield Securities

Outstanding Catastrophe Bond Volume By Quarter



Source: Aon Benfield Securities

There has been $2.8 billion of new transaction issuance from January 1, 2010 through September 30, 2010. Outstanding catastrophe bond volume totaled $11.1 billion as of September 30.

Structural Observations

With respect to collateral management, the note proceeds from Shore Re Ltd. were invested in U.S. Treasury money market funds, continuing the conservative standard established by all prior-2010 catastrophe bond deals[1]. However, with the issuance of Green Valley Ltd. Series 2 came a new EURIBOR-based collateral management solution. The note proceeds from Green Valley Ltd. Series 2 were invested in medium term notes from the European Bank for Reconstruction and Development ("EBRD"), providing investors with a higher yield on directed investments over the returns found in U.S. Treasury money market funds. The reference rate for the notes was 3-month EURIBOR less 31 basis points, providing investors with funding diversification away from money market funds. As a France Windstorm transaction paying a low interest risk spread, investors were sensitive to overall returns. The EBRD collateral structure offered additional yield to help satisfy investors' return thresholds.

[1] The Vita Capital IV Ltd. Series II Class, an excess mortality bond rather than a catastrophe bond transaction, utilized IBRD (International Bank for Reconstruction and Development) notes for its collateral solution.

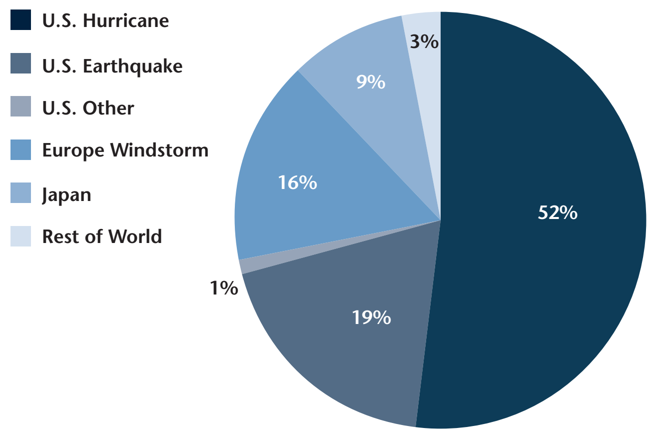
Secondary Market Trading Proves Variable During Third Quarter

As we reported in *Market Momentum* on June 30, 2010, recent ILS issuance had pushed investors' U.S. Hurricane exposure to previously unseen levels. As of September 30, 2010, 52 percent of the risk in the catastrophe bond market came from U.S. Hurricane (based on the contribution to expected loss), as compared to 27 percent in the period immediately after Hurricane Katrina. As a result of large supply, prices declined for U.S. Hurricane exposed bonds on the secondary market in July. Excluding bonds which expire in less than one year, the weighted average price of U.S. Hurricane bonds decreased 1.4 percent during the month, while the weighted average spread increased 7.7 percent (on a seasonally-adjusted basis)[2]. Similarly, the weighted average price of U.S. Multi-Peril bonds decreased 0.7 percent while the weighted average spread increased 3.2 percent (on a seasonally-adjusted basis)[2]. Trading in the month of July was relatively light as investors began the hurricane season with their portfolios positioned prior to what was predicted to be a very active hurricane season.

Trading rebounded in August with heavy volumes in short-dated U.S. Hurricane bonds as well as Europe Wind bonds. Despite concern with Hurricane Earl, investors generally held on to their positions in recent wind-pool bonds (Johnston Re Ltd. Series 2010, Parkton Re Ltd. Series 2009, and Shore Re Ltd.). Fortunately, Hurricane Earl only glanced the Eastern U.S. coast incurring little U.S. loss and eventually making landfall in Nova Scotia where it had no impact on outstanding bonds. Prices of U.S. Hurricane bonds took a short-lived mark-to-market loss during the storm but quickly rebounded once the storm passed. For the month of August as a whole, the price of U.S. Hurricane bonds reversed. Excluding bonds expiring in less than one year, the weighted average price of U.S. Hurricane bonds in August increased 0.2 percent while the weighted average spread increased by 5.4 percent (on a seasonally-adjusted basis)[2]. Similarly, the weighted average price of U.S. Multi-Peril bonds increased 0.9 percent while the weighted average spread decreased 0.2 percent (on a seasonally-adjusted basis)[2].

In September, the market began to experience greater demand for U.S. Hurricane bonds. We generally expect rapid price increases after the midpoint of the hurricane season since, for each of these bonds, the declining risk causes a reduction in the risk premium through an increase in the bond price. In addition, as these bonds experienced relatively discounted levels, several investors traded on the expectation that prices would quickly increase if the season ended without a major loss. With greater investor interest throughout the month, prices increased and spreads declined for U.S. Hurricane and U.S. Multi-peril bonds. In fact, the September weighted average price increase for U.S. Hurricane was 3.9 percent over the previous month while the weighted average spread decreased 11.8 percent (on a seasonally-adjusted basis)[2]. U.S. Multi-peril pricing saw similar results, increasing in price by 2.8 percent and decreasing in seasonally adjusted spread by 8.3 percent.

Catastrophe Bonds On Risk By Peril (As at 9/30/2010)



Source: Aon Benfield Securities

Throughout the quarter, investor demand remained strong for diversifying perils. The issuance of Green Valley Ltd. Series 2 benefited from this increased demand in September. Green Valley Ltd. Series 2 was oversubscribed and closed at 350 basis points, 25 basis points tighter than original guidance. On the secondary market, prices for divsersifying perils experienced consistent increases throughout the quarter as investors searched for diversification away from U.S. peak zone perils.

Assuming a continued uneventful 2010 U.S. Hurricane season, we believe that investor capacity for U.S. Hurricane exposed deals will increase. $675 million of U.S. Hurricane exposed catastrophe bonds will mature in the fourth quarter of 2010, and $4.3 billion will mature before June 30, 2011. Investors will look to extend the duration of their portfolios by adding new bonds, in addition to increasing positions in existing bonds with one or more full hurricane seasons remaining. For this reason, we expect continued spread softening for catastrophe bonds, assuming that there are no events that cause loss to any existing bonds. These expectations for the catastrophe bond market are consistent with Aon Benfield's expectations for continued softening in the traditional reinsurance market.

[2] Note that this may seem counterintuitive since price and spread typically move in opposite directions; when calculating the spread on an adjusted basis which takes out the effect of seasonality, however, this relationship does not always hold true.

European ILS Markets Remain Pensive

The traditional reinsurance market across Europe continues to offer a very competitively priced ultimate net loss product. Despite this trend, some European sponsors have recognized the opportunity to secure well priced multi-year collateralized capacity from the capital markets, such as the Green Valley Ltd. Series 2 issue. We expect to see more than €500 million in new issuances of diversifying Europe Windstorm transactions come to market before the end of 2010.

With this new issuance expectation and other new initiatives relating to the Europe Windstorm peril, such as the recent and proposed updates to catastrophe models and the development of PERILS AG, we are beginning to see the European market evolve to become a more frequent participant in the ILS market.

Unlike hurricanes, which have a relatively uniform and symmetrical structure, European extratropical cyclones are more complex weather structures. This complexity generates modeling challenges. At Standard & Poor's recent European ILS conference, the major catastrophe modeling firms were asked to evaluate a hypothetical Europe Windstorm catastrophe bond with a weighted industry loss trigger. Although there was a reasonable consensus regarding industry exposures across the major European territories, the model results for the hypothetical bond highlighted differing approaches among the modeling vendors. Differing model results are not a bad, or unexpected, outcome in view of the complexity of the hazard though they do create uncertainty amongst investors. However, with the development of independent exposure and loss information from agencies such as PERILS AG, we should begin to see less variability in the industry exposure and vulnerability factors contributing to future model updates across the firms. Reduced model uncertainty will be a positive factor for the ILS market and will lead to greater price transparency.

Related Markets Update

Since our last update in June 2010, PERILS AG has revealed that the new European index has been used as the basis for Industry Loss Warranties with a total notional value of $405 million. Together with the use of the PERILS AG index in catastrophe bonds, this shows a growing market acceptance of the new index, and a continuing demand for robust tailored non-indemnity structures.

The Magnitude 7.0 New Zealand earthquake that occurred on September 4th has had limited impact on the collateralized reinsurance or ILW space. Many of the covers offered by the sector either attached above the loss threshold or excluded New Zealand (focusing on named peak territories). However, the event may have the potential to cause collateral to be held as covers renew at the beginning of 2011, potentially impacting available capacity for 2011 on the margin.

About Aon Benfield Securities

Aon Benfield Securities, Inc. and Aon Benfield Securities Limited (collectively, "Aon Benfield Securities") provide insurance and reinsurance clients with a full suite of insurance-linked securities products, including catastrophe bonds, contingent capital, collateralized reinsurance, industry loss warranties, sidecars and derivative products.

As a recognized leader in this investment banking market, Aon Benfield Securities is helping to redefine capital by offering expert underwriting and placement of new issues, financial advisory services, as well as securities trading in the secondary market. Aon Benfield Securities' integration with Aon Benfield's reinsurance operation expands its capability to provide analytics, modeling, rating agency, and other consultative services.

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About Aon Benfield

Aon Benfield is redefining the role of the reinsurance intermediary and capital advisor. Aon Benfield offers unbiased capital advice and customized access to reinsurance and alternative markets around the globe. As a trusted advocate, we provide local reach to the world's markets, an unparalleled investment in innovative analytics, including catastrophe management, actuarial, and rating agency advisory, and the right professionals to advise clients in making the optimal capital choice for their business. With an international network of more than 80 offices in 50 countries, our worldwide client base is able to access the broadest portfolio of integrated capital solutions and services.

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