



2010 Auction Report

Auction Three, 28th/29th September 2010

Highlights

- Almost all prices down
- Only four syndicates traded at a higher price
- Members appear to have elected to keep capacity rather than try to sell into a falling market.
- Despite falling prices, the average value of a Member's portfolio is still worth more than it was at 2009 prices, when the 25% average pre-emption for 2010 is taken into account.

Auction Three Summary

	2010 Auction One	2010 Auction Two	2010 Auction Three	2010 All Auctions	2009 All*
Capacity successfully traded	£55.3m	£55.5m	£50.0m	£160.8m	£161.5m
Subscription (buy) orders	£248.2m	£439.3m	£308.2m	£776.0m	£733.2m
Tender (sale) orders	£115.8m	£109.9m	£81.4m	£307.1m	£230.3m
Bilateral trades	0	£13.9m	£4.1m	£17.9m	£14.3m
No. of syndicates traded	23	23	23	23	23
Average paid to acquire capacity	22.3p	16.6p	12.4p	17.1p	23.6p
Average of all Lloyd's capacity	28.7p	26.9p	22.5p	26.6p	31.8p

* Excludes Auction Four

Auction Three – an overview

We noted in our Auction Two bulletin that, once momentum has been established, price movements tend to all be in the same direction. So, in years when Auction Two prices are higher than Auction One, Auction Three prices tend to be higher still. When prices fall in Auction Two, Auction Three prices tend to be lower still. Since Lloyd's moved to the current format of three September auctions, only the 2001 auctions have bucked this trend. 2001, of course, is a unique auction period for many reasons.

As Auction Three is the last chance to sell, many sellers will give up trying to influence pricing and tender their capacity at the lowest possible price in order to secure a sale. 46% of capacity was tendered at less than 1p, compared to 28% in Auction One and 40% in Auction Two. Others hold out for their price and, if it fails to materialise, will trade into next year with the capacity. This meant there was plenty of capacity on sought after syndicates that remained unsold, including £3.8m on Syndicate 33 (tendered at 44p to 60p) £2m on 510 (from 10p to 30p) £2m on 570 (at 43p and up) and £1.0m on 2791. Interestingly, sellers expectations were not that high. Had prices held up to Auction Two levels, £10m more of the capacity tendered would have changed hands. At Auction One prices, volumes traded would have been more than £70m and less than £10m would have remained unsold.

Although some individual syndicates may have bucked the declining pricing trends, only two peaked in value at Auction Three. These were Syndicate 318 and Syndicate 2526.

Syndicate 318 was again heavily purchased by the aligned vehicle, **Beaufort Dedicated**, which has increased its share by more than 10 percentage points this year to 84.7% and will be required to make an offer to the remaining members next year. This offer will be at no less than the maximum price that the vehicle has paid to acquire capacity, which we understand to be Auction Three's price of 7.5p. This matched the price paid by Beaufort to acquire capacity in Auction Two's controversial bilateral deal, with the outcome of Lloyd's inquiry reported in our previous Auction Two report currently awaited. Despite placing some lower bids on Day One, Beaufort came in with a bid for £20m on Day Two at 7.5p which easily mopped up all but the highest priced sellers.

Conversely, **Syndicate 2526** capacity had been sold in Auctions One and Two by current managing agent, **Alterra**, in advance of a move to Whittington. There was no further capacity tendered by Alterra in Auction Three and volumes traded fell from £1.6m to £221,000, with a small increase in pricing.

A number of managing agents acted to mop up capacity that remained unsold at low prices after Auction Two. **Kiln** made its first auction purchase for some years, picking up just under £2m of **Syndicate 807** at 3p, comfortably trumping all other bidders for a syndicate that had been available for less than 1p in Auction Two. Dedicated vehicle, **Argenta Underwriting No. 2 Limited**, picked up £2.5m of **Syndicate 2121** at this year's low price of 0.14p and **Canopus** swept up £15m on **Syndicate 260** at a similar price.

Argo brought its total purchases for the year to more than £7m by adding another £1.7m of managed capacity on **Syndicate 1200**. Argo has bought three quarters of the capacity traded on the syndicate this year and has increased its aligned share by more than two percentage points to almost 83%.

MAP Syndicate 2791 was subject to a bilateral deal between Hampden and Atrium's spread underwriting vehicle. Atrium has been seeking a buyer for the last vestiges of a former spread portfolio and offered capacity on Syndicate 2791 unsuccessfully at 30p in Auction One, with partial success at 25p in Auction Two and parted with a further chunk of £3.4m at 17p in Auction Three. Interaction between the auction and the bilateral deals meant that some would-be buyers underbid the auction's average of 22.9p, but were allocated capacity at 17p.

Omega trumped all-comers in Auction Two with a bid of 30p for **Syndicate 958** but failed to show in Auction Three. While some increased their price to outbid Omega, others low-balled and hoped for the best. The upshot was one of the largest spreads of the day (spread referring to the difference in price between the highest bid and the lowest one at which capacity was allocated), with bids as low as 15.3p securing a line on the syndicate.



Syndicate 386 traded at less than £1 for the first time this year. The nuclear **Syndicate 1176** saw the usual small quantity traded at a slightly lower price. Low volumes available and the high absolute price meant that no buyer secured more than £100,000 on either. With a large number of bespoke buyers, the spreads on both these syndicates are large. For 386, successful bids ranged from 111p down to 80p. The spread on 1176 was even larger: £15,000 was bought at 265p and £7,654 at 180p.

Consistently the third most expensive syndicate at auction, **Syndicate 727** was again bought by **Meacock Underwriting** and Mrs Meacock, who between them have acquired almost two thirds of the £1.9m that has changed hands on the syndicate this year. Separately, Michael Meacock, who is the only remaining Active Underwriter who continues with unlimited liability, added a further £75,000 on life Syndicate 308 (bringing this year's purchases to £200,000) and £100,000 on Syndicate 2010.

Beazley's strategy of placing a high "sweeper" bid bore fruit. In each Auction this year, Beazley has bid for £100m of **Syndicate 623** at 25p. There was no success in the first two auctions, but the drop in price in Auction Three met a partial success, increasing the aligned share by 0.04 percentage points or just over £500,000. The same strategy was followed by **Hiscox** and **Atrium** for their managed syndicates. Hiscox bid for £20m of **Syndicate 33** at 10p (and were more than 10p away from any action), with MAPAs and bespoke members adding to their shares. Atrium was close on **Syndicate 609** (bidding 20p for £10m), but 25.4p was the minimum successful price. An identical bid for **Syndicate 570** was well short. Capacity on this syndicate has been scarce and expensive all month, and has now established itself as routinely more expensive than its sibling.

Kiln Syndicates 510 and 557 both continued to trade down from their peaks in Auction One. 510 halved in value between Auction One and Auction Three, a fact which seems to owe more to the copious supply, as almost every third party member has a large share, rather than any adverse sentiment on the part of sellers. As for Syndicate 557, the price continues to look relatively high given that buyers will be de-empted for 2011 by almost half and similar books of business are freely available via the Special Purpose Syndicate (SPS) system.

Life **Syndicate 779** continued to be out of favour, with more than 10% of total capacity changing hands through this year's auctions. From a high at auction of almost 20p last year, the price has fallen to little more than 1.4p, with much capacity re-entered at a lower price in this auction to try to ensure a sale. Unlike Auction Two, all capacity tendered at 0.1p did find a buyer. The winner from the shaky confidence in the Jubilee operations seems to be **Kiln Life Syndicate 308**. A single private seller with a very large stake has been prepared to sell at 15p in each auction, with some takers each time. The auction allocation process meant that some buyers were able to secure the capacity at less than 11p while the seller received the auction average of 15p, as some members outbid the tender price to ensure priority.

Syndicate 218 was another faller, with £2.6m changing hands at 5.6p. As in Auction Two, some bidders were successful at 5p or less, but the fall in price was attributed to no buyers bidding more than 10p. Just over £1m remained unsold, half of which was sellers hoping for prices up to 11p.

Cathedral Syndicate 2010 was one of the bargains of Auction Two, with one 15p bid being successful despite being almost 25p less than the strike price. This drew in the bargain hunters, most of whom left empty handed. The lowest successful bid came in at 25.3p. However, the spread of bidders narrowed considerably, with the strike price falling almost 25% to 30.3p.

Sellers outnumbered buyers on **Syndicate 1969**, trading for the first time in 2010. £125,000 changed hands at under 0.3p, but another £5.7m remained unsold. As this represents both almost 10% of the syndicate capacity and almost 40% of the expected pre-emption offer, we expect much, if not all, of the potential 'drop' will be available to members who would like free capacity outside the auction.

Lloyd's Interim Results

Lloyd's released its interim results for the half year ended 30 June 2010 last week.

	<i>Half Year to 30 June 2010</i>	<i>Half Year to 30 June 2009</i>	<i>Full Year to 31 December 2009</i>
Gross Written Premium	£13,490m	£13,462m	£21,973m
Profit Before Tax	£628m	£1,322m	£3,868m
Combined ratio	98.7%	91.6%	86.1%
Return on Capital (Annualised)	7.0%	17.5%	23.9%

It is often difficult to read too much into the half-year figures released by the Market. Historically, the impact of major catastrophe losses falls more severely on the second half of the year, coinciding as it does with the US hurricane season, and any reserve release or shortfall will be more meaningful following the annual review of outstanding claims' files in accordance with Lloyd's practice of setting a reinsurance to close at year end. Also, in recent years, swings in exchange rates have meant that foreign exchange movements have been a major element of the result.

This year perhaps it is possible to divine more, especially as foreign exchange movements were almost negligible. Catastrophe losses in the first half year have surpassed any earlier year but, despite the New Zealand earthquake, the trend has not continued into the 3rd quarter (accepting the fact that the hurricane season still has two months to go). Lloyd's aggregate estimates of the costs of the Chilean earthquake and the Deepwater Horizon rig loss are unchanged at US\$1.4m and \$300m to \$600m respectively. There is an overall release from reserves despite the widely reported deterioration in the UK motor class. Although press commentaries have highlighted the 50% fall in profits declared at the half year stage, we find the results creditable and encouraging.

Premium volumes have remained almost static, although the entry of new syndicates during 2009 and 2010 means that established syndicates have been reducing their premium volumes. Reserve releases are reported across most classes of business, excepting UK Motor where there is an overall deficit reported at £250m. Nonetheless, overall reserve movements improved the half year combined ratio by 4.6%. The catastrophe losses, including Chile and Deepwater mentioned above, added 17.1% to the combined ratio. There is something here for you whether you see your glass half empty or half full; without the releases from reserves, the combined ratio would have exceeded 100% (at 103.3%), if the level of catastrophe losses had mirrored 2009, the ratio would have been less than 85%.



Lloyd's investments continue to be held in very low risk assets. Equities and alternative assets represent less than 5% of the total assets, with corporate bonds rated less than "A" comprising less than 2.5% of the total. Unsurprisingly, given the current environment, investment returns are low, producing an annualised rate of 1.3% on invested assets.

The full results and accompanying analyst presentation can be found on the Argenta website at <http://tinyurl.com/3aa7lbi>.

Auction Four

A fourth auction will be held on Wednesday 10 and Thursday 11 November. As noted in our auction guidance notes issued in August, this is a limited auction and rules for the inclusion of capacity in this auction include:

- disposals of capacity in cases where the final approved capacity of a syndicate for 2011 exceeds the amount indicated in the Syndicate's Business Forecast (**SBF**) (such disposals being limited to a member's share of the difference between the two amounts);
- transactions in capacity on syndicates where the indicative capital ratio for the syndicate (as output by the Risk Based Capital modelling software, adjusted for syndicate ICA submissions) has increased by 10% or more between 12 August and 29 October 2010; and
- transactions in capacity on syndicates where after 17 September 2010 there has been a material change in the syndicate's 2011 business plan as defined in Auction Rule 4(4), that is:
 - a change in the active underwriter; or
 - the introduction of a new class of business; or
 - an increase in the ultimate loss ratio; or
 - a change in utilisation (where utilisation is the ratio of a syndicate's gross premiums written to its capacity); or
 - an increase or decrease in business from any one source; or
 - in any other circumstance where the Auction Official confirms that in his view there has been a material change to a syndicate's business plan.

Members may only subscribe for capacity in Auction Four if they have, or expect to have, sufficient surplus funds at Lloyd's (**FAL**) (as at the coming-into-line date of 29 November 2010) to support any further capacity which they acquire. No additional funds can be supplied after the coming-into-line date.

Subject to Lloyd's final approval of syndicates' business plans by 28 October, the Auction Official is expected to announce on 3 November details of those syndicates which will be admitted to Auction Four, at which point we will advise you accordingly.

Special Purpose Syndicates

Many of our members have availed themselves of underwriting via the special purposes syndicates (SPS). Each of these is an annually renewed quota share reinsurance contract between a host syndicate and specially created counter-party syndicate. We have now commenced negotiations with each of the agents involved in managing SPS, all of whom we expect to renew. We will be writing to all members who currently have SPS within their portfolios, setting out base information for each syndicate, together with the impact on portfolio characteristics (including risk ratings) of their inclusion, and invite participants to renew their shares for 2011. We expect there will be some opportunities to increase shares within SPS or to join new SPS. If you wish to do this, please, in the first instance, speak to your Client Director. Existing SPS are as follows.

Syndicate	Managing Agent	Description
6103	Managing Agency Partners	Whole account quota share of Syndicate 2791's US property reinsurance account
6104	Hiscox Syndicates	Whole account quota share of Syndicate 33's reinsurance account
6105	Ark Syndicate Management	Whole account quota share of Syndicate 4020's composite account
6106	Amlin Underwriting	Whole account quota share of Syndicate 2001's reinsurance division
6107	Beazley Furlonge	Whole account quota share of Beazley Syndicate 623/2623's reinsurance division

Syndicate 1110 – Withdrawal of Pre-emption

As you will be aware from our 2010 *Syndicate Profiles* book, published in August, we were able to add Syndicate 1110, the specialist engineering syndicate managed by Argenta which commenced trading for the 2010 year of account, to the list of syndicates recommended for support for 2011. Those who attended or viewed via Argenta's website, our pre-auction client meeting on 1 September will have heard the presentation given by the underwriter, Neil Fitzgerald.

The business plan for 2011 was based on the assumption that expected improvements in the classes of business in which the syndicate operates would allow it to increase capacity from £53m in 2010 to £65.2m for 2011. However, it is now apparent that, in spite of good progress in developing the syndicate's core book of business, markets remain more competitive than anticipated. Rather than risking compromising pricing standards, Syndicate 1110 has therefore decided that it will maximise utilisation of the existing capacity with high quality business and will not be making a pre-emption offer for 2011.

As the pre-emption has been withdrawn, there is now unlikely to be additional capacity available to be offered to those wishing to join the syndicate for 2011 although this remains under discussion. We will advise our clients as soon as the position has been confirmed.



Auction Three – In Numbers

Only four price rises

<i>Syndicate</i>	<i>Managing Agent</i>	<i>Auction Two Price</i>	<i>Auction Three Price</i>	<i>Price Increase</i>
807	R.J. Kiln & Co	0.81	3.00	270.8%
1969	Flagstone Re	0.10	0.28	179.0%
318	Beaufort Syndicate Management	4.91	7.50	52.7%
2526	Alterra at Lloyd's	31.15	32.36	3.9%

Top five price falls

<i>Syndicate</i>	<i>Managing Agent</i>	<i>Auction Two Price</i>	<i>Auction Three Price</i>	<i>Price Decrease</i>
2121	Argenta Syndicate Management	0.61	0.14	-77.1%
260	Canopus Managing Agents	0.27	0.10	-61.6%
779	Jubilee Managing Agents	3.22	1.41	-56.3%
33	Hiscox Syndicate Management	44.41	32.28	-27.3%
2791	Managing Agency Partners	25.81	19.19	-25.6%

Top five sellers

<i>Syndicate</i>	<i>Capacity</i>	<i>Seller</i>
2791	£4,051,794	Atrium 5 Limited
260	£2,401,233	Hampden Agencies MAPA 7208
623	£1,720,904	Argenta SLP
260	£1,467,352	Hampden Agencies MAPA 7066
260	£1,261,212	Hampden Agencies MAPA 7210

Top five buyers

<i>Syndicate</i>	<i>Capacity</i>	<i>Buyer</i>
260	£15,113,804	Canopus Capital Two Limited
318	£3,949,977	Beaufort Dedicated No 2 Limited
2791	£3,205,602	Hampden Agencies MAPA 7218
2121	£2,591,718	Argenta Underwriting No 2 Limited
807	£1,945,640	Kiln Underwriting Ltd

Auction Summary

Synd	Un - adjusted 2009 Average Price	Adjusted 2009 Average Price	Pre/(De)- emption	Aligned Capacity	Auction One Price p/£1	Auction One Volume (£000s)	Auction Two Price p/£1	Auction Two Volume (£000s)	Auction Three Price p/£1	Auction Three Volume (£000s)	Average Price p/£1	Total Volume (£000s)
0033	46.61	34.95	(10.0%)	72.5%	41.87	4,437	44.41	2,809	32.28	1,997	40.57	9,242
0218	43.26	40.25		64.0%	9.43	5,282	6.74	7,376	5.56	2,641	7.46	15,299
0260	6.76	6.30		58.8%	1.34	1,520	0.27	1,684	0.10	15,609	0.22	18,813
0308	21.64	15.87		52.1%	15.00	691	15.00	1,175	15.00	1,052	15.00	2,918
0318	12.72	11.40		73.7%	5.09	1,555	4.91	23,797	7.50	3,950	5.27	29,303
0386	107.51	100.11		69.6%	112.56	1,027	102.00	906	91.29	547	104.01	2,480
0510	17.07	11.69		52.8%	18.22	6,594	10.53	2,295	9.38	2,393	14.78	11,283
0557	7.40	7.40	(49.8%)	0.0%	11.84	1,097	10.00	2,789	7.59	888	9.97	4,774
0570	45.67	39.50		24.8%	45.90	1,253	46.41	853	42.48	633	45.27	2,739
0609	38.98	28.31		25.8%	38.00	2,425	37.00	2,162	30.75	1,533	35.83	6,120
0623	34.46	22.91		82.5%	34.13	3,322	35.04	3,004	29.71	3,087	32.97	9,413
0727	41.07	37.90		<25%	47.81	625	50.09	504	45.08	770	47.31	1,899
0779	17.01	18.90		<25%	9.59	1,027	3.22	958	1.41	1,155	4.64	3,141
0807	4.24	3.65		51.1%	3.10	2,448	0.81	2,094	3.00	1,946	2.33	6,488
0958	37.20	33.15		38.8%	24.55	2,702	30.00	4,678	25.80	1,984	27.54	9,364
1176	166.99	166.99		54.8%	222.69	47	239.00	94	220.27	95	228.22	237
1200	2.98	2.98	(7.1%)	82.30%	5.42	6,075	7.15	1,798	6.23	1,925	5.90	9,798
1969			23.9%	26.9%	1.29	476	0.10	123	0.28	126	0.91	724
2010	43.34	37.15		57.8%	44.69	1,416	39.80	1,400	30.32	1,167	38.76	3,983
2121	2.10	1.56	14.3%	29.3%	2.23	3,388	0.61	1,013	0.14	3,779	1.06	8,180
2525	31.22	31.22		2.0%	33.22	521	35.39	154	34.47	105	33.82	780
2526	27.07	27.07	57.2%	27.0%	29.53	3,483	31.15	1,621	32.36	221	30.14	5,324
2791	26.12	21.10		20.9%	29.90	3,884	25.81	6,082	19.19	6,451	24.18	16,417

Note

In addition to auction trades of £9.9m, there were bilateral deals (i.e. non-auction trades) in Auction Two for capacity on Syndicate 318 of £12,840,359 at a price of 7.5p per £1. A further £963,027 of capacity tendered in the auction interacted with these bilateral deals, bringing the total capacity traded on the syndicate to £23,797,383, at an average price of 4.91p.

There were two bilateral deals for an aggregate £3,418,053 of capacity on Syndicate 2791 at 17p in Auction Three. A further £581,069 of capacity subscribed for in the auction interacted with these bilateral deals, bringing the total capacity traded to £6,450,939 at an average of 19.19p.



Connected Party Trades

The table below shows Auction Three transactions that were successfully entered into by Members with Argenta Private Capital (**APCL**) connected person status.

<i>Syndicate</i>	<i>Type</i>	<i>Capacity</i>	<i>Member</i>	<i>Status</i>
2121	Subscription	2,591,718	Argenta Underwriting No. 2 Limited	Aligned Corporate Member
386	Subscription	3,000	E S Harborne	Consultant
2526	Subscription	7,000	E S Harborne	Consultant
308	Subscription	100,000	Aardvark Underwriting Ltd (David Newton)	Third Party Advisor
570	Subscription	10,000	Minhotex LLP (David Harrison)	Director
623	Subscription	30,000	Minhotex LLP (David Harrison)	Director
2121	Tender	3,750	Monksfield LLP (David Monksfield)	Director
33	Subscription	80,000	Talisman Corporate Underwriting 2000 Ltd	¹
218	Subscription	75,884	Talisman Corporate Underwriting 2000 Ltd	¹
386	Subscription	20,000	Talisman Corporate Underwriting 2000 Ltd	¹
570	Subscription	30,171	Talisman Corporate Underwriting 2000 Ltd	¹
609	Subscription	98,769	Talisman Corporate Underwriting 2000 Ltd	¹
623	Subscription	88,555	Talisman Corporate Underwriting 2000 Ltd	¹
958	Subscription	77,451	Talisman Corporate Underwriting 2000 Ltd	¹
2010	Subscription	72,948	Talisman Corporate Underwriting 2000 Ltd	¹
2791	Subscription	98,758	Talisman Corporate Underwriting 2000 Ltd	¹
318	Tender	28,750	Kling Investment Limited	²
2121	Tender	31,250	Kling Investment Limited	²
2121	Tender	50,000	BHC Winton Underwriting II Limited	²
260	Subscription	50,000	BHC Winton Underwriting III Limited	²
2121	Tender	161,331	BHC Winton Underwriting III Limited	²
2010	Tender	33,241	The Michael Deeny LLP	Council member
623	Tender	100,899	The Silent Scorpion LLP (Rona Delves Broughton)	Council member
2121	Tender	216,286	The Silent Scorpion LLP (Rona Delves Broughton)	Council member
2526	Tender	199,963	The Silent Scorpion LLP (Rona Delves Broughton)	Council member

Notes

¹ David Monksfield and Paul Sandilands (respectively executive and non-executive director of APCL) are directors of Talisman Corporate Underwriting 2000 Ltd.

² Alan Tucker (executive director of APCL and non-executive director of Argenta Syndicate Management Limited) is a director of the BHC corporate members and a director of Kling Investments Limited.

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