

July 29, 2008

British Marine Luxembourg S.A.

Primary Credit Analyst:

Ali Karakuyu, London (44) 20-7176-7301; ali_karakuyu@standardandpoors.com

Secondary Credit Analyst:

Rowena Potter, London (44) 20-7176-7070; rowena_potter@standardandpoors.com

Table Of Contents

Rationale

Outlook

Corporate Profile: Fixed-Premium Provider Writing Both P&I And H&M Business

Competitive Position: Ability To Defend Niche And Generate Profits Throughout Market Cycle Supports Strong Competitive Position

Management And Corporate Strategy: Strong Track Record In The Small-Vessel Sector

Enterprise Risk Management: Strong Risk Management Framework With A Positive Trend Driven By The Group

Accounting: Conservative

Operating Performance: Strong Earnings, Supported By Strong Underwriting Discipline

Investments: Low Appetite For Investment Risk

Liquidity: Strong Cash Flow

Table Of Contents (cont.)

Capitalization: Strong Capitalization Supported By Very High Quality Of Capital

Financial Flexibility: A Core Member Of The QBE Group

British Marine Luxembourg S.A.

Rationale

The ratings on Luxembourg-based marine insurer British Marine Luxembourg S.A. (BM) reflect the company's core status to Australia-based QBE Insurance Group Ltd. (QBE; main operating entities are rated A+/Stable/--). BM's core status reflects the strength of QBE's explicit support of BM. This comes in the form of a 90% quota share provided to BM by Bermuda-based Equator Reinsurances Ltd. (Equator Re; A+/Stable/--), a core entity of QBE, with effect from Jan. 1, 2007.

Operating Company Covered By This Report

Financial Strength Rating

Local Currency

A+/Stable/--

Standard & Poor's Ratings Services expects BM's existing relationships with retail brokers to support the QBE Europe division's strategic push to increase its penetration outside the wholesale arena. New business opportunities have emerged through leveraging existing market relationships between QBE entities and local market participants.

Outlook

The stable outlook on BM reflects the stable outlook on other core entities of QBE. As a core subsidiary of QBE, the ratings on BM will move in tandem with those on the parent.

Preservation of BM's core status will be contingent on the continuation of the group's explicit support, and the ongoing maintenance of BM's stand-alone capitalization at a level at least consistent with its ratings.

The following factors relate to BM's stand-alone characteristics and not directly to its public ratings.

Corporate Profile: Fixed-Premium Provider Writing Both P&I And H&M Business

BM writes, by gross premiums written, 62% protection and indemnity (P&I), 37% hull and machinery (H&M) business and 1% British Marine Transport Solution (BMTS) products (formerly known as International Transport Solutions), with a total gross premium written of \$172.1 million for year-end Dec. 2007, compared with \$136.4 million for the 10 months to Dec. 31, 2006. The company offers cover of up to \$1 billion for P&I business, up to \$20 million for its H&M account, and up to \$5 million for BMTS products (see "Competitive Position: Ability To Defend Niche And Generate Profits Throughout Market Cycle Supports Strong Competitive Position" for details).

After 124 years as a traditional mutual marine insurer, BM demutualized in February 2000 and formed a significant fixed-premium alternative to the traditional P&I market providers. The demutualization was backed by Capital Z, a U.S.-based investment fund. In November 2005, BM was acquired by QBE. It continues to operate as a stand-alone business unit, but benefits from financial and strategic support as a member of QBE. Management services are provided by British Marine Managers Ltd. (BMM) which is a subsidiary of BM.

Competitive Position: Ability To Defend Niche And Generate Profits Throughout Market Cycle Supports Strong Competitive Position

Table 1

British Marine Luxembourg S.A./Business Statistics (Consolidated)					
--Year ended Feb. 20--					
(Mil. \$)	2007*	2006**	2006	2005	2004
Gross premiums written	172.1	136.4	135.3	121.2	97.2
Annual change (%)	26.2	0.8	11.6	24.8	29.4
Net premiums written	151.1	120.1	116.1	109.7	88.7
Annual change (%)	25.9	3.5	5.8	23.8	44.2
Gross premiums written by line of business (%)					
P&I	62.0	60.0	56.0	52.0	49.0
H&M	37.0	40.0	44.0	48.0	51.0
Transport solutions	1.0	0.0	0.0	0.0	0.0
Total	100.0	100.0	100.0	100.0	100.00

*Figures represent calendar-year 2007. **Figures represent 10 months from Feb. 20, 2006, to Dec. 31, 2006. P&I--Protection and indemnity. H&M--Hull and machinery.

Competitive position is strong, reflecting BM's ability to defend its niche position in the small-vessel sector and the fact that it offers a unique proposition to its target clientele via its willingness to accept 100% of the risks it chooses to underwrite. Prospectively, competitive position will continue to strengthen as a result of BM's close association with the QBE brand. BM is leveraging existing market relationships between QBE entities and local market participants, particularly in southeast Asia, in order to broaden its product offering and increase geographic diversification.

One of BM's key strengths is its unique position to offer both a fixed-premium P&I product to small shipowners and, for H&M, to provide a level of service and closeness to the market more akin to a mutual than a traditional London market insurer. Furthermore, the company is not heavily reliant on any individual broker from the large range that it uses. Its exposure to London-based wholesale brokers remains extremely low.

Unlike the traditional P&I clubs, BM cannot make an unbudgeted supplementary call. This is a positive factor for policyholders as, should BM experience a poor year of claims development, those policyholders will not be liable to contribute any more than the premiums they have already paid. A further advantage that BM has over its peers in the International Group of Protection & Indemnity Clubs (IG) is that, unlike IG members, it does not impose general increases at renewal and prices individual risks based on performance. This is particularly pertinent in the small-vessel sector, where owners of small fleets are perhaps less willing to pay higher premiums when they themselves have not incurred any losses. Significant increases are imposed on those policyholders with less favorable performance, and due to the loyalty of its shipowner clients, much of this business is retained at the revised terms put forward by the company. Policyholders with good claims records experience increases reflective of claims inflation or increased reinsurance costs. This policy also gives BM an advantage over the local market insurers with which it competes, as it has the expertise and granularity of data to price each vessel individually. This high level of underwriting expertise enables BM to continue to profitably develop those markets that have proven to be less attractive to the larger brokers and insurers.

Key factors for the maintenance of the company's strong competitive position are its ability to produce profits throughout the cycle, to defend its niche position in the small-vessel sector, and to increase local market penetration via the QBE network of companies.

Historical

The company's gross premium income for the P&I account increased significantly to \$107.1 million in 2007 (compared to \$88.5 million in 2006) with more than half of this growth emanating from acquisitions made by existing clients. BM's P&I account has grown consistently over the last five years with premium income increasing from 45% of total premium in 2002 to 62% in 2007. The company experienced a strong growth at the February 2008 renewal, with a 24% premium increase compared with February 2007. At the same time, BM achieved a very high premium retention level of 97% (excluding vessels cancelled, sold, or scrapped) while achieving an average premium increase of 4.5% for the renewed book.

BM adopts a proactive stance to writing P&I business, and will be seeking to increase this account geographically via the QBE network. Competition on the P&I account is largely from traditional IG clubs. Partly because of the large general increases imposed by most of the IG clubs at the February 2008 renewal, the company saw a significant number of new business opportunities. As a result the gross tonnage gained from the IG clubs increased to 1.4 million gross tons (gt) at February 2008 renewal compared to 0.5 million gt at February 2007.

In absolute terms, the H&M book of business for 2007 remained on a par with the prior year, with a gross premium income of \$63.1 million in 2007 (\$67.5 million in 2006). The slight reduction in premium is largely due to competitors undercutting BM's renewal premiums. The H&M portfolio consists of a mixture of specialist vessels including tugs, support vessels, and smooth-water vessels such as river barges. The company's proximity to the shipowners and high service level give it a tangible advantage over some of its more broad-based competition in the London market. BM has dedicated significant resources to maintaining its high service level; for example, it currently has one claims handler per underwriter.

In response to client interest, BM launched BMTS in 2007 to underwrite intermodal and professional liability classes. The gross premium income for this account equated to \$1.8 million in 2007. The lower than expected premium was largely due to delayed launch of the product during 2007 and excessive price competition in certain products.

Prospective

Standard & Poor's considers that BM's competitive position will remain strong as the company defends and grows its position within its niche market and demonstrates its ability to generate profits throughout the cycle. This is evidenced by continuing significant growth in the company's P&I business, for which the gross premium income is likely to increase significantly by about 25% in 2008 following the successful February 2008 renewal. As a result of the increased competitive pressure in the H&M market, we expect the gross premium income for this account to reduce by about 10% in 2008 from the 2007 level. The premium income from BMTS products is likely to remain low at about \$5 million in 2008. Overall, the company is likely to experience a strong growth with an expected premium increase by about 20% in 2008 supported by the already strong growth at year to-date.

Standard & Poor's believes that BM will continue to benefit from cross-selling opportunities with other members of QBE.

Management And Corporate Strategy: Strong Track Record In The Small-Vessel Sector

The current management team is considered a positive factor for the rating. BM's strategy is, and will remain, to provide cover for small vessels, although a very small proportion of the portfolio will continue to relate to vessels in excess of 10,000 gt.

Strategy

BM's strategy is focused on shipowners within the small-vessel sector. The company adopts a proactive stance for P&I, and a reactive approach to H&M business. The management of BM continues to build its small-vessel franchise through the existing broker network, which has been strengthened by QBE's offices. BM continues to leverage its broker relationships within retail markets, as evidenced by its penetration into new markets such as Bulgaria and Vietnam during 2007.

The company's aim is to maintain and write business only at profitable levels, and BM has demonstrated its determination to stick to this strategy by withdrawing from certain markets that remain unprofitable, as evidenced by the reduction in H&M premium volume.

Operational management

Following the change in ownership in 2005, BM retained most of its existing management team. BM continues to settle comfortably within the QBE group, leveraging on regional offices worldwide. In addition, BM benefits from the services provided by the group as evidenced by the group actuaries' input for technical pricing. BM's board includes representation from QBE. The CEO of BMM devotes a significant amount of his time to client relationship management, a key competence for acquiring and retaining business within the small-vessel sector.

BM continues to invest in its internal systems, with the ultimate aim of improving the service quality to its clients and improving access to its data for planning and pricing.

Financial management

BM has strong financial management. The company focuses on the goal outlined in the business plan: to underwrite to internally calibrated target loss ratios for both H&M and P&I in order to achieve an attractive underwriting result. In line with QBE policy, the integration of BM into QBE led to significant dividend payments. Nevertheless, the capital adequacy ratio is extremely strong.

Enterprise Risk Management: Strong Risk Management Framework With A Positive Trend Driven By The Group

Standard & Poor's views QBE group's and, consequently, BM's enterprise risk management (ERM) as strong with a positive trend. The group's risk management framework has improved in many aspects, but has been in place only for about seven years. Greater maturity and confidence of its framework, combined with strong evidence that an excellent risk culture is entrenched into the organization across all management levels, can support a higher ERM score.

The overall relevance of ERM for the ratings on BM is currently regarded as low, given the company's relatively small size and sole focus on marine-related business. Nevertheless, BM has been enhancing its risk management framework to bring it in line with that of the group as evidenced by the development of the risk register which is based on the group model. In addition, the wider support and availability of resources and expertise has helped to enhance BM's existing strong business disciplines.

Accounting: Conservative

During 2006 BM changed its reporting date to Dec. 31 from Feb. 20 to align with QBE. Therefore, results at Dec. 31, 2006, are reflective of the 10-month period from Feb. 20, 2006. The figures and ratios disclosed in this report since February 2006 are based on unaudited consolidated accounts of BM before the quota share arrangement with Equator Re, which were provided by BM.

BM is licensed and regulated in Luxembourg by the Commissariat aux Assurances, and therefore publishes audited nonconsolidated accounts in accordance with the local requirements. Non-consolidated accounts are used to populate our risk-based capital model.

Operating Performance: Strong Earnings, Supported By Strong Underwriting Discipline

Table 2

British Marine Luxembourg S.A./Operating Statistics (Consolidated)					
--Year ended Feb. 20--					
(Mil. \$)	2007*	2006**	2006	2005	2004
Pretax result	23.5	29.9	20.7	29.6	26.2
Loss ratio (%)	64.9	63.3	54.3	52.1	64.4
Expense ratio (%)	27.3	21.1	27.5	25.5	23.0
Combined ratio (%)	92.2	84.4	81.4	77.6	87.4

*Figures represent calendar-year 2007. **Figures represent 10 months from Feb. 20, 2006, to Dec. 31, 2006.

Operating performance is strong. The combined ratio for year-end 2007 was 92.2% (84.4% for the 10 months ended Dec. 31, 2006), which is slightly worse than expectations. This difference is due to one-off expense items and adverse claims developments. On a consolidated basis, the company posted a reduced but still strong pre-tax profit of \$23.5 million in 2007 (compared to \$29.9 million for the 10 months ended Dec. 31, 2006). BM's strong operating performance is an indication of the quality of the underlying book of business and the rigor applied to underwriting since demutualization in February 2000, rather than a fortunate lack of large or multiple claims. Underwriting discipline is strong, as demonstrated by the continuation of the company's good risk selection and pricing.

Historical

Despite the adverse claims development, the underwriting performance in 2007 was strong. The overall loss ratio which stood at 64.9% in 2007 (63.3% for the 10 months ended Dec. 31, 2006) compares favorably to most of BM's peers. The increase in expense ratio to 27.3% in 2007 (21.1% in 2006) is partly due to the adverse impact of the U.S. dollar as the company's expenses are predominately denominated in sterling, and staff costs. Investment

returns for the year strengthened, but remain modest; BM does not rely upon realized and unrealized gains to bolster its bottom-line profits. Overall operating performance was strong, as demonstrated by a high return on equity of approximately 16.5% at year-end Dec. 31, 2007 (24% for the 10 months ended Dec. 31, 2006).

Prospective

Operating performance will remain strong, with the combined ratio expected to deteriorate to a level between 95%-100% in 2008. This deterioration is largely due to two large claims during Q1 2008 and to an increase in claims above \$500,000. Standard & Poor's expects BM to sustain its strong profit levels without the benefit of a hard market in hull insurance or significant increases in P&I premium rates. In line with QBE's policy, a significant portion of future profits will be distributed to QBE.

Investments: Low Appetite For Investment Risk

Table 3

British Marine Luxembourg S.A./Operating Statistics (Consolidated)					
--Year ended Feb. 20--					
(Mil. \$)	2007*	2006**	2006	2005	2004
Portfolio performance					
Net investment income	8.8	9.2	8.4	6.0	5.6
Net investment yield (%)	3.4	3.3	3.3	2.8	3.2
Portfolio composition (%)					
Fixed-income securities	74.0	76.0	76.0	72.4	72.3
Variable-interest securities	0.0	0.0	0.0	1.9	2.3
Cash and bank deposits	26.0	24.0	24.0	25.8	25.4
Total	100.0	100.0	100.0	100.0	100.0

*Figures represent calendar-year 2007. **Figures represent 10 months from Feb. 20, 2006, to Dec. 31, 2006.

Investment strategy remains conservative and is in line with both QBE's investment strategy and with BM's goal of pursuing an investment policy that does not place the capital of the company at risk. The majority of investments are held in bonds (74% in 2007), with the remainder in cash and deposits.

Recently the investment policy was changed to enable the company to invest up to 10% of shareholders' funds in equities. Resulting from the current market conditions the company has no appetite for investing in equities. Investment yield in 2007 excluding realized gains/losses remained modest at approximately 3.4% (3.3% in 2006).

Credit risk

BM's bond portfolio is managed externally and consists largely of government bonds. Investment guidelines state that these bonds must be rated 'AA-' or higher by Standard & Poor's.

Market risk

A large bond portfolio leaves BM exposed to changes in interest rates, although the short-term duration of the portfolio dilutes this risk to some degree.

Asset-liability management

BM regularly reviews the duration of both its assets and liabilities to avoid mismatching.

Liquidity: Strong Cash Flow

Liquidity is strong, with substantial cash deposits in addition to credit facilities open to BM at short notice. These facilities include a bank guarantee facility of £20.0 million. Letters of credit (LOCs) have been provided for all non-Lloyd's security on the upper layer of the P&I reinsurance program. BM's cash flow is underpinned by its strong approach to credit control, with debts outstanding more than 90 days being less than 2% of premiums booked over the 12 months to date.

Capitalization: Strong Capitalization Supported By Very High Quality Of Capital

BM's capitalization is strong overall, and the capital adequacy ratio, as measured by Standard & Poor's risk-based capital model, is currently extremely strong. Offsetting this strength is BM's heavy reliance on a strong reinsurance program in order to write the large P&I limits. On a consolidated basis the absolute size of the capital base reduced to \$105.1 million in 2007 compared to \$124.5 million in 2006. This reduction reflects the upstream of capital in the form of dividend payments amounting to \$59.3 million to the parent company. We expect the capitalization of BM to remain strong overall.

Quality of capital

Quality of capital is very high, with BM benefiting from an unleveraged balance sheet that places limited reliance on "soft" components of capital.

Reserves

Claims reserves are set up on a case-by-case basis, and are reviewed both within a six-month period of occurrence and whenever a payment is made from the reserve. In addition, all new claims that are likely to exceed £100 thousand are brought to the management team for review. An actuarial review of reserves occurs each quarter, with an independent sign-off taking place each year.

Reinsurance

Reinsurance protection is strong. BM has maintained its excess-of-loss program for the P&I, H&M, and intermodal business. BM has a catastrophe-type reinsurance to cover aggregation of net retained claims that could potentially arise from one catastrophic event and clash of retentions across different classes (including intermodal business) or within classes.

The company purchases reinsurance on a risks-attaching basis, and the limits match the maximum original policy limits, with the reinsurers following the original terms and conditions set by BM on the underwriting policy.

Protection is placed with Munich Reinsurance Co. (AA-/Stable/--) and Hannover Rückversicherung-AG (AA-/Stable/--) for the lower layers, with the London market, XL Europe Ltd. (A+/Stable/--), AXIS Re Ltd. (A/Positive/--), and various U.S.-based reinsurers providing the higher protection. All reinsurers carry a Standard & Poor's rating of 'A' or above. LOCs have been provided for all non-Lloyd's security on the upper layer (\$900 million in excess of \$100 million) of the P&I program.

Financial Flexibility: A Core Member Of The QBE Group

Financial flexibility (defined as the ability to source capital relative to capital requirements) has strengthened following BM's acquisition by QBE, and is considered strong. Although BM is not expected to have any capital needs in the immediate future, support could be provided from QBE if necessary.

Ratings Detail (As Of July 29, 2008)*

Operating Company Covered By This Report

British Marine Luxembourg S.A.

Financial Strength Rating

Local Currency

A+/Stable/--

Counterparty Credit Rating

Local Currency

A+/Stable/--

Domicile

Luxembourg

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

Additional Contact:

Insurance Ratings Europe; Insurancelnteractive_Europe@standardandpoors.com

Additional Contact:

Insurance Ratings Europe; Insurancelnteractive_Europe@standardandpoors.com

Copyright © 2008 Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P). S&P and/or its third party licensors have exclusive proprietary rights in the data or information provided herein. This data/information may only be used internally for business purposes and shall not be used for any unlawful or unauthorized purposes. Dissemination, distribution or reproduction of this data/information in any form is strictly prohibited except with the prior written permission of S&P. Because of the possibility of human or mechanical error by S&P, its affiliates or its third party licensors, S&P, its affiliates and its third party licensors do not guarantee the accuracy, adequacy, completeness or availability of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. S&P GIVES NO EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE. In no event shall S&P, its affiliates and its third party licensors be liable for any direct, indirect, special or consequential damages in connection with subscriber's or others use of the data/information contained herein. Access to the data or information contained herein is subject to termination in the event any agreement with a third-party of information or software is terminated.

Analytic services provided by Standard & Poor's Ratings Services (Ratings Services) are the result of separate activities designed to preserve the independence and objectivity of ratings opinions. The credit ratings and observations contained herein are solely statements of opinion and not statements of fact or recommendations to purchase, hold, or sell any securities or make any other investment decisions. Accordingly, any user of the information contained herein should not rely on any credit rating or other opinion contained herein in making any investment decision. Ratings are based on information received by Ratings Services. Other divisions of Standard & Poor's may have information that is not available to Ratings Services. Standard & Poor's has established policies and procedures to maintain the confidentiality of non-public information received during the ratings process.

Ratings Services receives compensation for its ratings. Such compensation is normally paid either by the issuers of such securities or third parties participating in marketing the securities. While Standard & Poor's reserves the right to disseminate the rating, it receives no payment for doing so, except for subscriptions to its publications. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

Any Passwords/user IDs issued by S&P to users are single user-dedicated and may ONLY be used by the individual to whom they have been assigned. No sharing of passwords/user IDs and no simultaneous access via the same password/user ID is permitted. To reprint, translate, or use the data or information other than as provided herein, contact Client Services, 55 Water Street, New York, NY 10041; (1)212.438.9823 or by e-mail to: research_request@standardandpoors.com.