

VALIDUS HOLDINGS LTD

Form 10-Q

August 05, 2011

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**Form 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended June 30, 2011**

**Commission file number 001-33606**

**VALIDUS HOLDINGS, LTD.**

*(Exact name of registrant as specified in its charter)*

**BERMUDA**

*(State or other jurisdiction of  
incorporation or organization)*

**98-0501001**

*(I.R.S. Employer  
Identification No.)*

**29 Richmond Road, Pembroke, Bermuda HM 08**

*(Address of principal executive offices and zip code)*

**(441) 278-9000**

*(Registrant's telephone number, including area code)*

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

**Yes  No**

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

**Yes  No**

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated  
filer

Accelerated filer

Non-accelerated filer

Smaller reporting  
company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

**Yes  No**

As of August 3, 2011 there were 99,032,232 outstanding Common Shares, \$0.175 par value per share, of the registrant.

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**Table of Contents****PART I. FINANCIAL INFORMATION****ITEM I. FINANCIAL STATEMENTS****Validus Holdings, Ltd.**

Consolidated Balance Sheets

**As at June 30, 2011 (unaudited) and December 31, 2010**

(Expressed in thousands of U.S. dollars, except share and per share information)

|  | <b>June 30,<br/>2011<br/>(unaudited)</b> | <b>December<br/>31,<br/>2010</b> |
|--|--|----------------------------------|
| <b>Assets</b>  |  |                                  |
| Fixed maturities, at fair value (amortized cost: 2011 - \$4,539,998; 2010 - \$4,772,037)   | \$ 4,603,534                             | \$ 4,823,867                     |
| Short-term investments, at fair value (amortized cost: 2011 - \$725,230; 2010 - \$273,444) | 725,258                                  | 273,514                          |
| Other investments, at fair value (amortized cost: 2011 - \$15,018; 2010 - \$18,392)        | 18,746                                   | 21,478                           |
| Cash and cash equivalents  | 815,921                                  | 620,740                          |
| <br>   |  |                                  |
| Total investments and cash   | 6,163,459                                | 5,739,599                        |
| Premiums receivable  | 1,046,775                                | 568,761                          |
| Deferred acquisition costs   | 176,724                                  | 123,897                          |
| Prepaid reinsurance premiums   | 177,729                                  | 71,417                           |
| Securities lending collateral  | 21,409                                   | 22,328                           |
| Loss reserves recoverable  | 439,805                                  | 283,134                          |
| Paid losses recoverable  | 30,854                                   | 27,996                           |
| Income taxes recoverable   | 3,503                                    | 1,142                            |
| Intangible assets  | 116,813                                  | 118,893                          |
| Goodwill   | 20,393                                   | 20,393                           |
| Accrued investment income  | 21,320                                   | 33,726                           |
| Other assets   | 41,004                                   | 49,592                           |
| <br>   |  |                                  |
| <b>Total assets</b>  | <b>\$ 8,259,788</b>                      | <b>\$ 7,060,878</b>              |
| <br>   |  |                                  |
| <b>Liabilities</b>   |  |                                  |
| Reserve for losses and loss expenses   | \$ 2,620,360                             | \$ 2,035,973                     |
| Unearned premiums  | 1,192,772                                | 728,516                          |
| Reinsurance balances payable   | 181,013                                  | 63,667                           |
| Securities lending payable   | 22,133                                   | 23,093                           |
| Deferred income taxes  | 22,122                                   | 24,908                           |
| Net payable for investments purchased  | 49,479                                   | 43,896                           |
| Accounts payable and accrued expenses  | 91,969                                   | 99,320                           |
| Senior notes payable   | 246,928                                  | 246,874                          |
| Debentures payable   | 289,800                                  | 289,800                          |
| <br>   |  |                                  |
| <b>Total liabilities</b>   | <b>\$ 4,716,576</b>                      | <b>\$ 3,556,047</b>              |

## Commitments and contingent liabilities

**Shareholders equity**

|  |                     |                     |
|--|---------------------|---------------------|
| Common shares, 571,428,571 authorized, par value \$0.175 (Issued: 2011 - 133,795,913; 2010 - 132,838,111; Outstanding: 2011 - 98,763,928; 2010 - 98,001,226) | \$ 23,414           | \$ 23,247           |
| Treasury shares (2011 - 35,031,985; 2010 - 34,836,885)   | (6,131)             | (6,096)             |
| Additional paid-in-capital   | 1,880,748           | 1,860,960           |
| Accumulated other comprehensive (loss)   | (4,519)             | (5,455)             |
| Retained earnings  | 1,514,805           | 1,632,175           |
| <b>Total shareholders equity available to Validus</b>  | <b>3,408,317</b>    | <b>3,504,831</b>    |
| Noncontrolling interest  | 134,895             |                     |
| <b>Total shareholders equity</b>   | <b>\$ 3,543,212</b> | <b>\$ 3,504,831</b> |
| <b>Total liabilities and shareholders equity</b>   | <b>\$ 8,259,788</b> | <b>\$ 7,060,878</b> |

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

**Table of Contents****Validus Holdings, Ltd.**

Consolidated Statements of Operations and Comprehensive Income (Loss)

**For the Three and Six Months Ended June 30, 2011 and 2010 (unaudited)**

(Expressed in thousands of U.S. dollars, except share and per share information)

|  | <b>Three Months Ended</b> |                      | <b>Six Months Ended</b> |                      |
|--|---------------------------|----------------------|-------------------------|----------------------|
|  | <b>June 30,</b>           | <b>June 30, 2010</b> | <b>June 30,</b>         | <b>June 30, 2010</b> |
|  | <b>2011</b>               | <b>(unaudited)</b>   | <b>2011</b>             | <b>(unaudited)</b>   |
|  | <b>(unaudited)</b>        | <b>(unaudited)</b>   | <b>(unaudited)</b>      | <b>(unaudited)</b>   |
| <b>Revenues</b>  |                           |                      |                         |                      |
| Gross premiums written                                       | \$ 605,387                | \$ 516,861           | \$ 1,455,283            | \$ 1,387,795         |
| Reinsurance premiums ceded                                   | (132,346)                 | (67,726)             | (242,166)               | (158,465)            |
| Net premiums written   | 473,041                   | 449,135              | 1,213,117               | 1,229,330            |
| Change in unearned premiums                                  | (47,401)                  | (11,191)             | (357,944)               | (333,692)            |
| Net premiums earned  | 425,640                   | 437,944              | 855,173                 | 895,638              |
| Net investment income  | 26,494                    | 34,809               | 56,469                  | 69,108               |
| Net realized gains on investments                            | 11,552                    | 12,441               | 17,931                  | 23,839               |
| Net unrealized gains on investments                          | 18,526                    | 41,640               | 5,698                   | 57,053               |
| Other income   | 595                       | 2,697                | 2,201                   | 3,585                |
| Foreign exchange (losses)                                    | (1,991)                   | (4,099)              | (2,458)                 | (12,863)             |
| <b>Total revenues</b>  | <b>480,816</b>            | <b>525,432</b>       | <b>935,014</b>          | <b>1,036,360</b>     |
| <b>Expenses</b>  |                           |                      |                         |                      |
| Losses and loss expenses                                     | 207,307                   | 194,894              | 683,505                 | 673,425              |
| Policy acquisition costs                                     | 78,230                    | 74,126               | 155,526                 | 150,302              |
| General and administrative expenses                          | 60,841                    | 52,379               | 109,318                 | 105,948              |
| Share compensation expenses                                  | 7,628                     | 6,846                | 19,677                  | 13,422               |
| Finance expenses   | 16,361                    | 13,218               | 30,362                  | 28,369               |
| <b>Total expenses</b>  | <b>370,367</b>            | <b>341,463</b>       | <b>998,388</b>          | <b>971,466</b>       |
| <b>Net income (loss) before taxes</b>                        | <b>110,449</b>            | <b>183,969</b>       | <b>(63,374)</b>         | <b>64,894</b>        |
| Tax benefit (expense)  | 29                        | (4,187)              | 1,488                   | (3,490)              |
| <b>Net income (loss)</b>                                     | <b>\$ 110,478</b>         | <b>\$ 179,782</b>    | <b>\$ (61,886)</b>      | <b>\$ 61,404</b>     |
| Net income attributable to noncontrolling interest           | (594)                     |                      | (594)                   |                      |
| <b>Net income (loss) available (attributable) to Validus</b> | <b>\$ 109,884</b>         | <b>\$ 179,782</b>    | <b>\$ (62,480)</b>      | <b>\$ 61,404</b>     |

**Comprehensive income**

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|  |             |             |             |             |
|--|-------------|-------------|-------------|-------------|
| Foreign currency translation adjustments   | (21)        | (68)        | 936         | (1,875)     |
| <b>Comprehensive income (loss) available (attributable) to Validus</b>                   | \$ 109,863  | \$ 179,714  | \$ (61,544) | \$ 59,529   |
| <b>Earnings per share</b>  |             |             |             |             |
| Weighted average number of common shares and common share equivalents outstanding        |             |             |             |             |
| Basic  | 98,385,924  | 121,009,553 | 98,165,132  | 123,821,415 |
| Diluted  | 104,562,450 | 125,152,300 | 98,165,132  | 125,661,729 |
| <b>Basic earnings (loss) per share available (attributable) to common shareholders</b>   | \$ 1.10     | \$ 1.47     | \$ (0.68)   | \$ 0.47     |
| <b>Diluted earnings (loss) per share available (attributable) to common shareholders</b> | \$ 1.05     | \$ 1.44     | \$ (0.68)   | \$ 0.46     |
| <b>Cash dividends declared per share</b>   | \$ 0.25     | \$ 0.22     | \$ 0.50     | \$ 0.44     |

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

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Consolidated Statements of Shareholders' Equity

**For the Six Months Ended June 30, 2011 and 2010 (unaudited)**

(Expressed in thousands of U.S. dollars, except share and per share information)

|  | <b>June 30, 2011<br/>(unaudited)</b> | <b>June 30, 2010<br/>(unaudited)</b> |
|--|--------------------------------------|--------------------------------------|
| <b>Common shares</b>                                   |                                      |                                      |
| Balance Beginning of period                            | \$ 23,247                            | \$ 23,033                            |
| Common shares issued, net                              | 167                                  | 68                                   |
| Balance End of period                                  | \$ 23,414                            | \$ 23,101                            |
| <b>Treasury shares</b>                                 |                                      |                                      |
| Balance Beginning of period                            | \$ (6,096)                           | \$ (553)                             |
| Repurchase of common shares                            | (35)                                 | (3,052)                              |
| Balance End of period                                  | \$ (6,131)                           | \$ (3,605)                           |
| <b>Additional paid-in capital</b>                      |                                      |                                      |
| Balance Beginning of period                            | \$ 1,860,960                         | \$ 2,675,680                         |
| Common shares issued, net                              | 6,071                                | (80)                                 |
| Repurchase of common shares                            | (5,960)                              | (441,027)                            |
| Share compensation expenses                            | 19,677                               | 13,422                               |
| Balance End of period                                  | \$ 1,880,748                         | \$ 2,247,995                         |
| <b>Accumulated other comprehensive (loss)</b>          |                                      |                                      |
| Balance Beginning of period                            | \$ (5,455)                           | \$ (4,851)                           |
| Foreign currency translation adjustments               | 936                                  | (1,875)                              |
| Balance End of period                                  | \$ (4,519)                           | \$ (6,726)                           |
| <b>Retained earnings</b>                               |                                      |                                      |
| Balance Beginning of period                            | \$ 1,632,175                         | \$ 1,337,811                         |
| Dividends  | (54,890)                             | (57,054)                             |
| Net (loss) income                                      | (61,886)                             | 61,404                               |
| Net income attributable to noncontrolling interest     | (594)                                |                                      |
| Balance End of period                                  | \$ 1,514,805                         | \$ 1,342,161                         |
| <b>Total shareholders' equity available to Validus</b> | <b>\$ 3,408,317</b>                  | <b>\$ 3,602,926</b>                  |
| <b>Noncontrolling interest</b>                         | <b>134,895</b>                       |                                      |



|                                  |              |              |
|----------------------------------|--------------|--------------|
| <b>Total shareholders equity</b> | \$ 3,543,212 | \$ 3,602,926 |
|----------------------------------|--------------|--------------|

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

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Consolidated Statements of Cash Flows

**For the Six Months Ended June 30, 2011 and 2010 (unaudited)**

(Expressed in thousands of U.S. dollars, except share and per share information)

|   | <b>June 30,<br/>2011<br/>(unaudited)</b> | <b>June 30,<br/>2010<br/>(unaudited)</b> |
|---|--|--|
| <b>Cash flows provided by (used in) operating activities</b>                            |  |  |
| Net (loss) income   | \$ (61,886)                              | \$ 61,404                                |
| Adjustments to reconcile net income to cash provided by (used in) operating activities: |  |  |
| Share compensation expenses   | 19,677                                   | 13,422                                   |
| Amortization of discount on senior notes  | 54                                       | 27                                       |
| Net realized (gains) on investments   | (17,931)                                 | (23,839)                                 |
| Net unrealized (gains) on investments   | (5,698)                                  | (57,053)                                 |
| Amortization of intangible assets   | 2,080                                    | 2,080                                    |
| Foreign exchange (gains) losses on cash and cash equivalents included in net income     | (12,729)                                 | 17,129                                   |
| Amortization of premium on fixed maturities   | 16,247                                   | 8,410                                    |
| Change in:  |  |  |
| Premiums receivable   | (475,119)                                | (383,671)                                |
| Deferred acquisition costs  | (52,827)                                 | (53,628)                                 |
| Prepaid reinsurance premiums  | (106,312)                                | (112,607)                                |
| Loss reserves recoverable   | (155,002)                                | (13,488)                                 |
| Paid losses recoverable   | (2,825)                                  | (9,364)                                  |
| Income taxes recoverable  | (2,400)                                  | 860                                      |
| Accrued investment income   | 12,406                                   | (653)                                    |
| Other assets  | 9,351                                    | (11,550)                                 |
| Reserve for losses and loss expenses  | 575,832                                  | 367,779                                  |
| Unearned premiums   | 464,256                                  | 452,499                                  |
| Reinsurance balances payable  | 116,080                                  | 35,240                                   |
| Deferred income taxes   | (2,611)                                  | 1,452                                    |
| Accounts payable and accrued expenses   | (11,029)                                 | (30,867)                                 |
| <b>Net cash provided by operating activities</b>  | <b>309,614</b>                           | <b>263,582</b>                           |
| <b>Cash flows provided by (used in) investing activities</b>                            |  |  |
| Proceeds on sales of investments  | 2,654,804                                | 2,933,352                                |
| Proceeds on maturities of investments   | 195,055                                  | 198,637                                  |
| Purchases of fixed maturities   | (2,613,981)                              | (3,244,072)                              |
| (Purchases) sales of short-term investments, net  | (451,706)                                | 211,801                                  |
| Sales of other investments  | 3,809                                    | 11,610                                   |
| Decrease (increase) in securities lending collateral                                    | 960                                      | (9,894)                                  |
| <b>Net cash (used in) provided by investing activities</b>                              | <b>(211,059)</b>                         | <b>101,434</b>                           |

**Cash flows provided by (used in) financing activities**

|   |                   |                   |
|---|-------------------|-------------------|
| Net proceeds on issuance of senior notes                                    |                   | 246,793           |
| Issuance (redemption) of common shares, net                                 | 6,238             | (12)              |
| Purchases of common shares under share repurchase program                   | (5,995)           | (444,079)         |
| Dividends paid  | (54,000)          | (55,994)          |
| (Decrease) increase in securities lending payable                           | (960)             | 9,894             |
| Third party investment in noncontrolling interest                           | 134,301           |                   |
| <b>Net cash provided by (used in) by financing activities</b>               | <b>79,584</b>     | <b>(243,398)</b>  |
| <b>Effect of foreign currency rate changes on cash and cash equivalents</b> | <b>17,042</b>     | <b>(16,714)</b>   |
| <b>Net increase in cash</b>   | <b>195,181</b>    | <b>104,904</b>    |
| <b>Cash and cash equivalents beginning of period</b>                        | <b>\$ 620,740</b> | <b>\$ 387,585</b> |
| <b>Cash and cash equivalents end of period</b>                              | <b>\$ 815,921</b> | <b>\$ 492,489</b> |
| <b>Taxes (recovered) paid during the period</b>                             | <b>\$ (3,373)</b> | <b>\$ 1,335</b>   |
| <b>Interest paid during the period</b>                                      | <b>\$ 23,823</b>  | <b>\$ 12,729</b>  |

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

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Notes to Consolidated Financial Statements (unaudited)

(Expressed in thousands of U.S. dollars, except share and per share information)

**1. Basis of preparation and consolidation**

These unaudited consolidated financial statements include Validus Holdings, Ltd. and its wholly and majority owned subsidiaries (together, the Company ) and have been prepared in accordance with generally accepted accounting principles in the United States of America ( U.S. GAAP ) for interim financial information and with the instructions to Form 10-Q and Article 10 in Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In addition, the year-end balance sheet data was derived from audited financial statements but does not include all disclosures required by U.S. GAAP. This Quarterly Report should be read in conjunction with the financial statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010, as filed with the U.S. Securities and Exchange Commission (the SEC ).

In the opinion of management, these unaudited consolidated financial statements reflect all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the Company s financial position and results of operations as at the end of and for the periods presented. Certain amounts in prior periods have been reclassified to conform to current period presentation. All significant intercompany accounts and transactions have been eliminated. The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. The major estimates reflected in the Company s consolidated financial statements include the reserve for losses and loss expenses, premium estimates for business written on a line slip or proportional basis, the valuation of goodwill and intangible assets, reinsurance recoverable balances including the provision for unrecoverable reinsurance recoverable balances and investment valuation. Actual results could differ from those estimates. The results of operations for any interim period are not necessarily indicative of the results for a full year. The term ASC used in these notes refers to Accounting Standard Codifications issued by the United States Financial Accounting Standards Board ( FASB ).

On May 25, 2011, the Company joined with other investors in capitalizing AlphaCat Re 2011, Ltd. ( AlphaCat Re 2011 ) a new special purpose sidecar reinsurer formed for the purpose of writing collateralized reinsurance and retrocessional reinsurance. Validus Reinsurance, Ltd. ( Validus Re ) has an equity interest in AlphaCat Re 2011 and as Validus Re holds a majority of AlphaCat Re 2011 s outstanding voting rights, the financial statements of AlphaCat Re 2011 are included in the consolidated financial statements of the Company. The portion of AlphaCat Re 2011 s earnings attributable to third party investors for the three months ended June 30, 2011 is recorded in the consolidated statement of operations and comprehensive income as net income attributable to noncontrolling interest. Refer to Note 4 Noncontrolling interest for further information.

**2. Recent accounting pronouncements**

In May 2011, the FASB issued Accounting Standards Update No. 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs* ( ASU 2011-04 ). The objective of ASU 2011-04 is to provide common fair value measurement and disclosure requirements in U.S. GAAP and IFRSs. Consequently, the amendments change the wording used to describe many of the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. For many of the requirements, the amendments do not result in a change in the application of the requirements in Topic 820 *Fair Value Measurements* .

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Notes to Consolidated Financial Statements (unaudited)

(Expressed in thousands of U.S. dollars, except share and per share information)

ASU 2011-04 is effective for interim and annual periods beginning after December 15, 2011. The Company is currently evaluating the impact of this guidance, however it is not expected to have a material impact on the Company's consolidated financial statements.

In June 2011, the FASB issued Accounting Standards Update No. 2011-05, *Presentation of Comprehensive Income* (ASU 2011-05). The objective of ASU 2011-05 is to improve the comparability, consistency and transparency of financial reporting and to increase the prominence of items reported in other comprehensive income. ASU 2011-05 is effective for interim and annual periods beginning after December 15, 2011. The Company is currently evaluating the impact of this guidance; however, since this update affects disclosures only, it is not expected to have an impact on the Company's consolidated financial statements.

**3. Investments**

The Company's investments in fixed maturities are classified as trading and carried at fair value, with related net unrealized gains or losses included in earnings. The Company has adopted all authoritative guidance in effect as of the balance sheet date regarding certain market conditions that allow for fair value measurements that incorporate unobservable inputs where active market transaction based measurements are unavailable.

**(a) Classification within the fair value hierarchy**

Under U.S. GAAP, a company must determine the appropriate level in the fair value hierarchy for each fair value measurement. The fair value hierarchy prioritizes the inputs, which refer broadly to assumptions market participants would use in pricing an asset or liability, into three levels. It gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The level in the fair value hierarchy within which a fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices within Level 1 that are observable for the asset or liability, either directly or indirectly. A significant adjustment to a Level 2 input could result in the Level 2 measurement becoming a Level 3 measurement. Level 3 inputs are unobservable inputs for the asset or liability.

Level 1 primarily consists of financial instruments whose value is based on quoted market prices or alternative indices including overnight repos and commercial paper. Level 2 includes financial instruments that are valued through independent external sources using models or other valuation methodologies. These models are primarily industry-standard models that consider various assumptions, including time value, yield curve, prepayment speeds, default rates, loss severity, current market and contractual prices for the underlying financial instruments, as well as other relevant economic measures. Substantially all of these assumptions are observable in the marketplace, can be derived from observable data or are supported by observable levels at which transactions are executed in the marketplace. The Company performs internal procedures on the valuations received from independent external sources. Financial instruments in this category include U.S. and U.K. Treasuries, sovereign debt, corporate debt, catastrophe bonds, U.S. agency and non-agency mortgage and asset-backed securities and bank loans. Level 3 includes financial instruments that are valued using market approach and income approach valuation techniques. These models incorporate both observable and unobservable inputs. A hedge fund is the only financial instrument in this category as at June 30, 2011.

The Company's management and external investment advisors had noted illiquidity and dislocation in the non-Agency RMBS market for the period September 30, 2008 through to June 30, 2010. During this period, the Company identified certain non-Agency RMBS securities in its portfolio trading in inactive markets (identified RMBS securities). In order to gauge market activity for the identified RMBS securities, the Company, with assistance from external investment advisors, reviewed the pricing sources for each security in the portfolio. The Company utilized various pricing vendors to obtain market pricing information for investment securities.



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Consistent with U.S. GAAP, market approach fair value measurements for securities trading in inactive markets are not determinative. In weighing the fair value measurements resulting from market approach and income approach valuation techniques, the Company previously placed less reliance on the market approach fair value measurements. The income approach valuation technique determines the fair value of each security on the basis of contractual cash flows, discounted using a risk-adjusted discount rate. As the income approach valuation technique incorporates both observable and significant unobservable inputs, the securities were included as Level 3 assets with respect to the fair value hierarchy. The foundation for the income approach was the amount and timing of future cash flows.

During the three month period ended September 30, 2010, the Company, with assistance from external investment advisors, determined that market activity had increased for the identified RMBS securities. Therefore, a market approach valuation technique was adopted for the identified RMBS securities. Because the market approach incorporates observable inputs, the identified RMBS securities are classified as Level 2 with respect to the fair value hierarchy at September 30, 2010. During the three months ended December 31, 2010, the Company liquidated substantially all of the identified RMBS securities which had previously been classified as Level 3 securities.

Other investments consist of an investment in a fund of hedge funds and a deferred compensation trust held in mutual funds. The fund of hedge funds is a side pocket valued at \$9,776 at June 30, 2011. While a redemption request has been submitted, the timing of receipt of proceeds on the side pocket is unknown. The fund's administrator provides monthly reported net asset values (NAV) with a one-month delay in its valuation. As a result, the funds administrator's May 31, 2011 NAV was used as a partial basis for fair value measurement in the Company's June 30, 2011 balance sheet. The fund manager provides an estimate of the performance of the fund for the following month based on the estimated performance provided from the underlying third-party funds. The Company utilizes the fund investment manager's primary market approach estimated NAV that incorporates relevant valuation sources on a timely basis. As this valuation technique incorporates both observable and significant unobservable inputs, the fund of hedge funds is classified as a Level 3 asset. To determine the reasonableness of the estimated NAV, the Company assesses the variance between the estimated NAV and the one-month delayed fund administrator's NAV. Immaterial variances are recorded in the following reporting period.

At June 30, 2011, the Company's investments were allocated between Levels 1, 2 and 3 as follows:

|   | <b>Level 1</b>    | <b>Level 2</b>      | <b>Level 3</b>  | <b>Total</b>        |
|---|-------------------|---------------------|-----------------|---------------------|
| U.S. Government and Government Agency             | \$                | \$ 838,912          | \$              | \$ 838,912          |
| Non-U.S. Government and Government Agency         |                   | 476,590             |                 | 476,590             |
| States, municipalities, political subdivision     |                   | 29,576              |                 | 29,576              |
| Agency residential mortgage-backed securities     |                   | 470,933             |                 | 470,933             |
| Non-Agency residential mortgage-backed securities |                   | 51,223              |                 | 51,223              |
| U.S. corporate                                    |                   | 1,406,591           |                 | 1,406,591           |
| Non-U.S. corporate                                |                   | 628,045             |                 | 628,045             |
| Bank Loans  |                   | 387,201             |                 | 387,201             |
| Catastrophe bonds                                 |                   | 29,934              |                 | 29,934              |
| Asset-backed securities                           |                   | 276,273             |                 | 276,273             |
| Commercial mortgage-backed securities             |                   | 8,256               |                 | 8,256               |
| <b>Total fixed maturities</b>                     |                   | <b>4,603,534</b>    |                 | <b>4,603,534</b>    |
| Short-term investments                            | 679,184           | 46,074              |                 | 725,258             |
| Hedge fund  |                   |                     | 9,776           | 9,776               |
| Mutual funds                                      |                   | 8,970               |                 | 8,970               |
| <b>Total</b>                                      | <b>\$ 679,184</b> | <b>\$ 4,658,578</b> | <b>\$ 9,776</b> | <b>\$ 5,347,538</b> |





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At December 31, 2010, the Company's investments were allocated between Levels 1, 2 and 3 as follows:

|   | <b>Level 1</b>    | <b>Level 2</b>      | <b>Level 3</b>   | <b>Total</b>        |
|---|-------------------|---------------------|------------------|---------------------|
| U.S. Government and Government Agency             | \$                | \$ 1,677,166        | \$               | \$ 1,677,166        |
| Non-U.S. Government and Government Agency         |                   | 554,199             |                  | 554,199             |
| States, municipalities, political subdivision     |                   | 26,285              |                  | 26,285              |
| Agency residential mortgage-backed securities     |                   | 445,859             |                  | 445,859             |
| Non-Agency residential mortgage-backed securities |                   | 56,470              |                  | 56,470              |
| U.S. corporate                                    |                   | 1,308,406           |                  | 1,308,406           |
| Non-U.S. corporate                                |                   | 502,067             |                  | 502,067             |
| Bank loans  |                   | 52,566              |                  | 52,566              |
| Catastrophe bonds                                 |                   | 58,737              |                  | 58,737              |
| Asset-backed securities                           |                   | 123,569             |                  | 123,569             |
| Commercial mortgage-backed securities             |                   | 18,543              |                  | 18,543              |
| Total fixed maturities                            |                   | 4,823,867           |                  | 4,823,867           |
| Short-term investments                            | 259,261           | 14,253              |                  | 273,514             |
| Hedge fund  |                   |                     | 12,892           | 12,892              |
| Mutual funds                                      |                   | 8,586               |                  | 8,586               |
| <b>Total</b>                                      | <b>\$ 259,261</b> | <b>\$ 4,846,706</b> | <b>\$ 12,892</b> | <b>\$ 5,118,859</b> |

At June 30, 2011, Level 3 investments totaled \$9,776, representing 0.2% of total investments measured at fair value on a recurring basis. At December 31, 2010, Level 3 investments totaled \$12,892 representing 0.3% of total investments measured at fair value on a recurring basis.

The following tables present a reconciliation of the beginning and ending balances for all investments measured at fair value on a recurring basis using Level 3 inputs during the three and six month periods ending June 30, 2011 and 2010:

|   | <b>Three Months Ended June 30, 2011</b> |                    |                          |
|---|---|--------------------|--------------------------|
|   | <b>Fixed Maturity</b>                   | <b>Other</b>       | <b>Total Fair Market</b> |
|   | <b>Investments</b>                      | <b>Investments</b> | <b>Value</b>             |
| Level 3 investments - Beginning of period | \$                                      | \$ 10,713          | \$ 10,713                |
| Purchases                                 |   |                    |                          |
| Sales                                     |   | (1,247)            | (1,247)                  |
| Issuances                                 |   |                    |                          |
| Settlements                               |   |                    |                          |
| Realized gains                            |   | 175                | 175                      |
| Unrealized gains                          |   | 135                | 135                      |
| Amortization                              |   |                    |                          |
| Transfers                                 |   |                    |                          |
| Level 3 investments - End of period       | \$                                      | \$ 9,776           | \$ 9,776                 |



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|   | <b>Three Months Ended June 30, 2010</b> |                    |                   |
|---|---|--------------------|-------------------|
|   | <b>Fixed</b>                            |                    | <b>Total Fair</b> |
|   | <b>Maturity</b>                         | <b>Other</b>       | <b>Market</b>     |
|   | <b>Investments</b>                      | <b>Investments</b> | <b>Value</b>      |
| Level 3 investments - Beginning of period | \$ 76,943                               | \$ 21,919          | \$ 98,862         |
| Purchases                                 |   |                    |                   |
| Sales                                     |   | (2,710)            | (2,710)           |
| Issuances                                 |   |                    |                   |
| Settlements                               |   |                    |                   |
| Realized gains                            |   | 170                | 170               |
| Unrealized gains (losses)                 | 2,632                                   | (249)              | 2,383             |
| Amortization                              | (3,997)                                 |                    | (3,997)           |
| Transfers                                 |   |                    |                   |
| Level 3 investments End of period         | \$ 75,578                               | \$ 19,130          | \$ 94,708         |

|   | <b>Six Months Ended June 30, 2011</b> |                    |                   |
|---|---------------------------------------|--------------------|-------------------|
|   | <b>Fixed</b>                          |                    | <b>Total Fair</b> |
|   | <b>Maturity</b>                       | <b>Other</b>       | <b>Market</b>     |
|   | <b>Investments</b>                    | <b>Investments</b> | <b>Value</b>      |
| Level 3 investments - Beginning of period | \$                                    | \$ 12,892          | \$ 12,892         |
| Purchases                                 |                                       |                    |                   |
| Sales                                     |                                       | (3,809)            | (3,809)           |
| Issuances                                 |                                       |                    |                   |
| Settlements                               |                                       |                    |                   |
| Realized gains                            |                                       | 435                | 435               |
| Unrealized gains                          |                                       | 258                | 258               |
| Amortization                              |                                       |                    |                   |
| Transfers                                 |                                       |                    |                   |
| Level 3 investments End of period         | \$                                    | \$ 9,776           | \$ 9,776          |

|   | <b>Six Months Ended June 30, 2010</b> |                    |                   |
|---|---------------------------------------|--------------------|-------------------|
|   | <b>Fixed</b>                          |                    | <b>Total Fair</b> |
|   | <b>Maturity</b>                       | <b>Other</b>       | <b>Market</b>     |
|   | <b>Investments</b>                    | <b>Investments</b> | <b>Value</b>      |
| Level 3 investments - Beginning of period | \$ 85,336                             | \$ 25,670          | \$ 111,006        |
| Purchases                                 |                                       |                    |                   |
| Sales                                     |                                       | (7,094)            | (7,094)           |
| Issuances                                 |                                       |                    |                   |

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|                           |               |           |           |           |
|---------------------------|---------------|-----------|-----------|-----------|
| Settlements               |               |           |           |           |
| Realized gains            |               |           | 344       | 344       |
| Unrealized (losses) gains | (1,634)       |           | 210       | (1,424)   |
| Amortization              | (8,124)       |           |           | (8,124)   |
| Transfers                 |               |           |           |           |
| Level 3 investments       | End of period | \$ 75,578 | \$ 19,130 | \$ 94,708 |

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**(b) Net investment income**

Net investment income was derived from the following sources:

|   | <b>Three Months Ended</b> |                 | <b>Six Months Ended</b> |                 |
|---|---------------------------|-----------------|-------------------------|-----------------|
|   | <b>June</b>               | <b>June 30,</b> | <b>June</b>             | <b>June 30,</b> |
|   | <b>30,</b>                | <b>2010</b>     | <b>30,</b>              | <b>2010</b>     |
|   | <b>2011</b>               | <b>2010</b>     | <b>2011</b>             | <b>2010</b>     |
| Fixed maturities and short-term investments | \$ 27,535                 | \$ 36,346       | \$ 56,470               | \$ 72,101       |
| Cash and cash equivalents                   | 687                       | 311             | 3,268                   | 897             |
| Securities lending income                   | 8                         | 49              | 24                      | 119             |
| Total gross investment income               | 28,230                    | 36,706          | 59,762                  | 73,117          |
| Investment expenses                         | (1,736)                   | (1,897)         | (3,293)                 | (4,009)         |
| Net investment income                       | \$ 26,494                 | \$ 34,809       | \$ 56,469               | \$ 69,108       |

**(c) Fixed maturity and short-term investments**

The following represents an analysis of net realized gains and the change in net unrealized gains on investments:

|   | <b>Three Months Ended</b> |                  | <b>Six Months Ended</b> |                  |
|---|---------------------------|------------------|-------------------------|------------------|
|   | <b>June</b>               | <b>June 30,</b>  | <b>June 30,</b>         | <b>June 30,</b>  |
|   | <b>30,</b>                | <b>2010</b>      | <b>2011</b>             | <b>2010</b>      |
|   | <b>2011</b>               | <b>2010</b>      | <b>2011</b>             | <b>2010</b>      |
| Fixed maturities, short-term and other investments and cash equivalents           |                           |                  |                         |                  |
| Gross realized gains  | \$ 13,032                 | \$ 15,120        | \$ 28,797               | \$ 27,885        |
| Gross realized (losses)   | (1,480)                   | (2,679)          | (10,866)                | (4,046)          |
| Net realized gains on investments   | 11,552                    | 12,441           | 17,931                  | 23,839           |
| Net unrealized gains (losses) on securities lending                               | 11                        | (6)              | 41                      | (1,020)          |
| Change in net unrealized gains on investments                                     | 18,515                    | 41,646           | 5,657                   | 58,073           |
| <b>Total net realized gains and change in net unrealized gains on investments</b> | <b>\$ 30,078</b>          | <b>\$ 54,081</b> | <b>\$ 23,629</b>        | <b>\$ 80,892</b> |

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The amortized cost, gross unrealized gains and (losses) and estimated fair value of investments at June 30, 2011 were as follows:

|   | <b>Amortized<br/>Cost</b> | <b>Gross<br/>Unrealized<br/>Gains</b> | <b>Gross<br/>Unrealized<br/>Losses</b> | <b>Estimated Fair<br/>Value</b> |
|---|---------------------------|---------------------------------------|--|---------------------------------|
| U.S. Government and Government Agency             | \$ 828,627                | \$ 10,656                             | \$ (371)                               | \$ 838,912                      |
| Non-U.S. Government and Government Agency         | 470,438                   | 9,551                                 | (3,399)                                | 476,590                         |
| States, municipalities, political subdivision     | 29,199                    | 394                                   | (17)                                   | 29,576                          |
| Agency residential mortgage-backed securities     | 454,517                   | 16,899                                | (483)                                  | 470,933                         |
| Non-Agency residential mortgage-backed securities | 57,678                    | 148                                   | (6,603)                                | 51,223                          |
| U.S. corporate                                    | 1,378,760                 | 29,227                                | (1,396)                                | 1,406,591                       |
| Non-U.S. corporate                                | 618,411                   | 10,615                                | (981)                                  | 628,045                         |
| Bank loans  | 389,193                   | 702                                   | (2,694)                                | 387,201                         |
| Catastrophe bonds                                 | 29,550                    | 445                                   | (61)                                   | 29,934                          |
| Asset-backed securities                           | 275,417                   | 1,142                                 | (286)                                  | 276,273                         |
| Commercial mortgage-backed securities             | 8,208                     | 48                                    |  | 8,256                           |
| <b>Total fixed maturities</b>                     | <b>4,539,998</b>          | <b>79,827</b>                         | <b>(16,291)</b>                        | <b>4,603,534</b>                |
| <b>Total short-term investments</b>               | <b>725,230</b>            | <b>57</b>                             | <b>(29)</b>                            | <b>725,258</b>                  |
| <b>Total other investments</b>                    | <b>15,018</b>             | <b>3,728</b>                          |  | <b>18,746</b>                   |
| <b>Total</b>                                      | <b>\$ 5,280,246</b>       | <b>\$ 83,612</b>                      | <b>\$ (16,320)</b>                     | <b>\$ 5,347,538</b>             |

The amortized cost, gross unrealized gains and (losses) and estimated fair value of investments at December 31, 2010 were as follows:

|   | <b>Amortized<br/>Cost</b> | <b>Gross<br/>Unrealized<br/>Gains</b> | <b>Gross<br/>Unrealized<br/>Losses</b> | <b>Estimated Fair<br/>Value</b> |
|---|---------------------------|---------------------------------------|--|---------------------------------|
| U.S. Government and Government Agency         | \$ 1,665,050              | \$ 20,134                             | \$ (8,018)                             | \$ 1,677,166                    |
| Non-U.S. Government and Government Agency     | 550,759                   | 11,635                                | (8,195)                                | 554,199                         |
| States, municipalities, political subdivision | 26,365                    | 90                                    | (170)                                  | 26,285                          |
|   | 430,873                   | 15,491                                | (505)                                  | 445,859                         |

|   |                     |                  |                    |                     |
|---|---------------------|------------------|--------------------|---------------------|
| Agency residential mortgage-backed securities     |                     |                  |                    |                     |
| Non-Agency residential mortgage-backed securities | 62,020              | 64               | (5,614)            | 56,470              |
| U.S. corporate                                    | 1,288,078           | 28,526           | (8,198)            | 1,308,406           |
| Non-U.S. corporate                                | 497,689             | 7,939            | (3,561)            | 502,067             |
| Bank loans  | 52,612              | 58               | (104)              | 52,566              |
| Catastrophe bonds                                 | 56,991              | 2,042            | (296)              | 58,737              |
| Asset-backed securities                           | 123,354             | 605              | (390)              | 123,569             |
| Commercial mortgage-backed securities             | 18,246              | 299              | (2)                | 18,543              |
| <br>  |                     |                  |                    |                     |
| Total fixed maturities                            | 4,772,037           | 86,883           | (35,053)           | 4,823,867           |
| Total short-term investments                      | 273,444             | 70               |                    | 273,514             |
| Total other investments                           | 18,392              | 3,086            |                    | 21,478              |
| <br>  |                     |                  |                    |                     |
| <b>Total</b>                                      | <b>\$ 5,063,873</b> | <b>\$ 90,039</b> | <b>\$ (35,053)</b> | <b>\$ 5,118,859</b> |

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The following table sets forth certain information regarding the investment ratings of the Company's fixed maturities portfolio as at June 30, 2011 and December 31, 2010. Investment ratings are the lower of Moody's or Standard & Poor's rating for each investment security, presented in Standard & Poor's equivalent rating. For investments where Moody's and Standard & Poor's ratings are not available, Fitch ratings are used and presented in Standard & Poor's equivalent rating.

|                               | June 30, 2011              |               | December 31, 2010          |               |
|-------------------------------|----------------------------|---------------|----------------------------|---------------|
|                               | Estimated<br>Fair<br>Value | % of<br>Total | Estimated<br>Fair<br>Value | % of<br>Total |
| AAA                           | \$ 2,237,017               | 48.6%         | \$ 2,946,514               | 61.2%         |
| AA                            | 400,177                    | 8.7%          | 428,972                    | 8.9%          |
| A                             | 1,193,431                  | 25.9%         | 1,077,389                  | 22.3%         |
| BBB                           | 331,145                    | 7.2%          | 219,523                    | 4.6%          |
| Investment grade              | 4,161,770                  | 90.4%         | 4,672,398                  | 97.0%         |
| BB                            | 218,227                    | 4.7%          | 74,475                     | 1.5%          |
| B                             | 199,649                    | 4.3%          | 45,660                     | 0.9%          |
| CCC                           | 21,548                     | 0.5%          | 29,219                     | 0.6%          |
| CC                            |                            | 0.0%          |                            | 0.0%          |
| D/NR                          | 2,340                      | 0.1%          | 2,115                      | 0.0%          |
| Non-Investment grade          | 441,764                    | 9.6%          | 151,469                    | 3.0%          |
| <b>Total Fixed Maturities</b> | <b>\$ 4,603,534</b>        | <b>100.0%</b> | <b>\$ 4,823,867</b>        | <b>100.0%</b> |

The amortized cost and estimated fair value amounts for fixed maturity securities held at June 30, 2011 and December 31, 2010 are shown by contractual maturity. Actual maturity may differ from contractual maturity because certain borrowers may have the right to call or prepay certain obligations with or without call or prepayment penalties.

|   | June 30, 2011       |                            | December 31, 2010   |                            |
|---|---------------------|----------------------------|---------------------|----------------------------|
|   | Amortized<br>Cost   | Estimated<br>Fair<br>Value | Amortized<br>Cost   | Estimated<br>Fair<br>Value |
| Due in one year or less                     | \$ 427,713          | \$ 431,200                 | \$ 424,327          | \$ 426,167                 |
| Due after one year through five years       | 2,965,528           | 3,015,190                  | 3,498,334           | 3,540,408                  |
| Due after five years through ten years      | 344,337             | 343,859                    | 207,918             | 206,317                    |
| Due after ten years                         | 6,600               | 6,600                      | 6,965               | 6,534                      |
|   | 3,744,178           | 3,796,849                  | 4,137,544           | 4,179,426                  |
| Asset-backed and mortgage-backed securities | 795,820             | 806,685                    | 634,493             | 644,441                    |
| <b>Total</b>                                | <b>\$ 4,539,998</b> | <b>\$ 4,603,534</b>        | <b>\$ 4,772,037</b> | <b>\$ 4,823,867</b>        |



The Company has a five year, \$500,000 secured letter of credit facility provided by a syndicate of commercial banks. At June 30, 2011, approximately \$277,679 (December 31, 2010: \$268,944) of letters of credit were issued and outstanding under this facility for which \$352,636 of investments were pledged as collateral (December 31, 2010: \$325,532). In 2007, the Company entered into a \$100,000 standby letter of credit facility which provides Funds at Lloyd's (the Talbot FAL Facility).

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On November 19, 2009, the Company entered into a Second Amendment to the Talbot FAL Facility to reduce the commitment from \$100,000 to \$25,000. At June 30, 2011, \$25,000 (December 31, 2010: \$25,000) of letters of credit were issued and outstanding under the Talbot FAL Facility for which \$45,204 of investments were pledged as collateral (December 31, 2010: \$45,504). In addition, \$1,993,707 of investments were held in trust at June 30, 2011 (December 31, 2010: \$1,729,631). Of those, \$1,545,533 were held in trust for the benefit of Talbot's cedants and policyholders, and to facilitate the accreditation of Talbot as an alien insurer/reinsurer by certain regulators (December 31, 2010: \$1,489,243).

The Company assumed two letters of credit facilities as part of the acquisition of IPC Holdings, Ltd. (the IPC Acquisition). A Credit Facility between IPC, IPCRe Limited, the Lenders party thereto and Wachovia Bank, National Association (the IPC Syndicated Facility) and a Letters of Credit Master Agreement between Citibank N.A. and IPCRe Limited (the IPC Bi-Lateral Facility). At March 31, 2010, the IPC Syndicated Facility was closed. At June 30, 2011, the IPC Bi-Lateral Facility had \$63,284 (December 31, 2010: \$68,063) letters of credit issued and outstanding for which \$106,216 (December 31, 2010: \$105,310) of investments were held in an associated collateral account.

**(d) Securities lending**

The Company participates in a securities lending program whereby certain securities from its portfolio are loaned to third parties for short periods of time through a lending agent. The Company retains all economic interest in the securities it lends and receives a fee from the borrower for the temporary use of the securities. Collateral in the form of cash, government securities and letters of credit is required at a rate of 102% of the market value of the loaned securities and is held by a third party. As at June 30, 2011, the Company had \$21,604 (December 31, 2010: \$22,566) in securities on loan. During the three months ended June 30, 2011, the Company recorded a \$11 unrealized gain on this collateral on its Statements of Operations (June 30, 2010: unrealized loss \$6). During the six months ended June 30, 2011, the Company recorded a \$41 unrealized gain on this collateral in its Statements of Operations (June 30, 2010: unrealized loss \$1,020).

Securities lending collateral reinvested includes corporate floating rate securities and overnight repo with an average reset period of 1.1 days (December 31, 2010: 17.6 days). As at June 30, 2011, the securities lending collateral reinvested by the Company in connection with its securities lending program was allocated between Levels 1, 2 and 3 as follows:

|                         | <b>Level 1</b> | <b>Level 2</b> | <b>Level 3</b> | <b>Total</b> |
|-------------------------|----------------|----------------|----------------|--------------|
| Corporate               | \$             | \$ 257         | \$             | \$ 257       |
| Asset-backed securities |                |                |                |              |
| Short-term investments  | 20,979         | 173            |                | 21,152       |
| <b>Total</b>            | \$ 20,979      | \$ 430         | \$             | \$ 21,409    |

As at December 31, 2010, the securities lending collateral reinvested by the Company in connection with its securities program was allocated between Levels 1, 2 and 3 as follows:

|                         | <b>Level 1</b> | <b>Level 2</b> | <b>Level 3</b> | <b>Total</b> |
|-------------------------|----------------|----------------|----------------|--------------|
| Corporate               | \$             | \$ 229         | \$             | \$ 229       |
| Asset-backed securities |                | 5,005          |                | 5,005        |
| Short-term investments  | 2,644          | 14,450         |                | 17,094       |
| <b>Total</b>            | \$ 2,644       | \$ 19,684      | \$             | \$ 22,328    |



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The following table sets forth certain information regarding the investment ratings of the Company's securities lending collateral reinvested as at June 30, 2011 and December 31, 2010. Investment ratings are the lower of Moody's or Standard & Poor's rating for each investment security, presented in Standard & Poor's equivalent rating.

For investments where Moody's and Standard & Poor's ratings are not available, Fitch ratings are used and presented in Standard & Poor's equivalent rating.

|                                | June 30, 2011              |               | December 31, 2010          |               |
|--------------------------------|----------------------------|---------------|----------------------------|---------------|
|                                | Estimated<br>Fair<br>Value | % of<br>Total | Estimated<br>Fair<br>Value | % of<br>Total |
| AAA                            | \$ 173                     | 0.8%          | \$ 5,454                   | 24.4%         |
| AA+                            |                            | 0.0%          | 11,003                     | 49.3%         |
| AA                             |                            | 0.0%          |                            | 0.0%          |
| AA-                            |                            | 0.0%          | 2,998                      | 13.5%         |
| A+                             |                            | 0.0%          |                            | 0.0%          |
| A                              |                            | 0.0%          |                            | 0.0%          |
| NR                             | 257                        | 1.2%          | 229                        | 1.0%          |
|                                | 430                        | 2.0%          | 19,684                     | 88.2%         |
| NR- Short-term investments (a) | 20,979                     | 98.0%         | 2,644                      | 11.8%         |
| <b>Total</b>                   | <b>\$ 21,409</b>           | <b>100.0%</b> | <b>\$ 22,328</b>           | <b>100.0%</b> |

(a) This amount relates to short-term investments and is therefore not a rated security.

The amortized cost and estimated fair value amounts for securities lending collateral reinvested by the Company at June 30, 2011 and December 31, 2010 are shown by contractual maturity below. Actual maturity may differ from contractual maturity because certain borrowers may have the right to call or prepay certain obligations with or without call or prepayment penalties.

|                                       | June 30, 2011     |                         | December 31, 2010 |                         |
|---------------------------------------|-------------------|-------------------------|-------------------|-------------------------|
|                                       | Amortized<br>Cost | Estimated Fair<br>Value | Amortized<br>Cost | Estimated Fair<br>Value |
| Due in one year or less               | \$ 21,133         | \$ 21,152               | \$ 17,093         | \$ 17,095               |
| Due after one year through five years | 1,000             | 257                     | 6,000             | 5,233                   |
| <b>Total</b>                          | <b>\$ 22,133</b>  | <b>\$ 21,409</b>        | <b>\$ 23,093</b>  | <b>\$ 22,328</b>        |

**4. Noncontrolling interest**

On May 25, 2011, the Company joined with other investors in capitalizing AlphaCat Re 2011 Ltd. (AlphaCat Re 2011), a new special purpose sidecar reinsurer formed for the purpose of writing collateralized reinsurance and retrocessional reinsurance. Validus Re has an equity interest in AlphaCat Re 2011 and as Validus Re holds a majority of AlphaCat Re 2011's outstanding voting rights, the financial statements of AlphaCat Re 2011 are included in the consolidated financial statements of the Company. The portion of AlphaCat Re 2011's earnings attributable to third party investors for the three months ended June 30, 2011 is recorded in the consolidated statement of operations and comprehensive income as net income attributable to noncontrolling interest.



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The activity in net income attributable to noncontrolling interest is detailed in the table below as at June 30, 2011:

|  | <b>Noncontrolling<br/>interest</b> |
|--|------------------------------------|
| Balance April 1, 2011                              | \$                                 |
| Purchase of shares by noncontrolling interest      | 134,301                            |
| Net Income:  |                                    |
| Net Income attributable to noncontrolling interest | 594                                |
| Balance June 30, 2011                              | \$ 134,895                         |

**5. Derivative instruments used in hedging activities**

The Company enters into derivative instruments for risk management purposes, specifically to economically hedge unmatched foreign currency exposures. During the three months ended June 30, 2011, the Company entered into a foreign currency forward exchange contract to mitigate the risk of foreign currency exposure of unpaid losses denominated in Japanese Yen. During the three months ended March 31, 2011, the Company entered into three foreign currency forward exchange contracts to mitigate the risk of fluctuations in the Euro and Australian dollar to U.S. dollar rates. Two of the contracts were renewed during the three months ended June 30, 2011. During the year ended December 31, 2010, the Company entered into a foreign currency forward contract to mitigate the risk of foreign currency exposure of unpaid losses denominated in Chilean Pesos (CLP). The CLP foreign currency forward contract was renewed during the three months ended June 30, 2011. The following table summarizes information on the location and amount of the derivative fair value on the consolidated balance sheet at June 30, 2011:

| Derivatives designated as<br>hedging instruments: | Notional<br>Amount | Asset Derivatives            |               | Liability Derivatives                             |               |
|---|--------------------|------------------------------|---------------|---|---------------|
|   |                    | Balance<br>Sheet<br>location | Fair<br>value | Balance<br>Sheet<br>location                      | Fair<br>value |
| Foreign exchange contracts                        | \$ 128,613         | Other<br>assets              | \$ 354        | Accounts<br>payable<br>and<br>accrued<br>expenses | \$ 173        |

The following table summarizes information on the location and amount of the derivative fair value on the consolidated balance sheet at December 31, 2010:

| Derivatives designated as<br>hedging instruments: | Notional<br>Amount | Asset Derivatives            |               | Liability Derivatives        |               |
|---|--------------------|------------------------------|---------------|------------------------------|---------------|
|   |                    | Balance<br>Sheet<br>location | Fair<br>value | Balance<br>Sheet<br>location | Fair<br>value |
|   |                    |                              |               | Accounts<br>payable          |               |

|                           |    |        |        |          |       |
|---------------------------|----|--------|--------|----------|-------|
|                           |    |        |        | and      |       |
|                           |    |        |        | accrued  |       |
| Foreign exchange contract | \$ | 75,000 | Other  | \$       | 2,905 |
|                           |    |        | assets | expenses | \$    |

***(a) Classification within the fair value hierarchy***

As described in Note 3 Investments under U.S. GAAP, a company must determine the appropriate level in the fair value hierarchy for each fair value measurement. The assumptions used within the valuation are observable in the marketplace, can be derived from observable data or are supported by observable levels at which transactions are executed in the marketplace. Accordingly, these derivatives were classified within Level 2 of the fair value hierarchy.

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**(b) Derivative instruments designated as a fair value hedge**

The Company designates its derivative instruments as fair value hedges and formally and contemporaneously documents all relationships between the hedging instruments and hedged items and links the hedging derivatives to specific assets and liabilities. The Company assesses the effectiveness of the hedges, both at inception and on an on-going basis and determines whether the hedges are highly effective in offsetting changes in fair value of the linked hedged items.

The following table provides the total impact on earnings relating to the derivative instruments formally designated as fair value hedges along with the impact of the related hedged items for the three and six months ended June 30, 2011:

|                           |                                 | Three Months Ended June 30, 2011           |                                     |                                  |
|---------------------------|---------------------------------|--|-------------------------------------|----------------------------------|
|                           |                                 | Amount of Gain (Loss)                      | Amount of Gain (Loss) Recognized    | Amount of Gain (Loss) Recognized |
| Derivatives designated as | Location of Gain (Loss)         | Amount of Gain (Loss) Recognized in Income | on Hedged Item Recognized in Income | in Income on Derivative          |
| fair value hedges and     | (Loss) Recognized in            | Income                                     | Attributable to Risk                | (Ineffective                     |
| related hedged item:      | Income                          | Derivative                                 | Being Hedged                        | Portion)                         |
| Foreign exchange          | Foreign exchange gains (losses) | \$ 897                                     | \$ (897)                            | \$                               |

|                           |                         | Six Months Ended June 30, 2011             |                                     |                                  |
|---------------------------|-------------------------|--|-------------------------------------|----------------------------------|
|                           |                         | Amount of Gain (Loss)                      | Amount of Gain (Loss) Recognized    | Amount of Gain (Loss) Recognized |
| Derivatives designated as | Location of Gain (Loss) | Amount of Gain (Loss) Recognized in Income | on Hedged Item Recognized in Income | in Income on Derivative          |
| fair value hedges and     | (Loss) Recognized in    | Income                                     | Attributable to Risk                | (Ineffective                     |
| related hedged item:      | Income                  | Derivative                                 | Being Hedged                        | Portion)                         |
| Foreign exchange          | Foreign exchange        | \$ (2,925)                                 | \$ 2,925                            | \$                               |



(losses)  
gains

There was no derivative activity for the three and six months ended June 30, 2010.

**6. Reserve for losses and loss expenses**

Reserves for losses and loss expenses are based in part upon the estimation of case losses reported from brokers, insureds and ceding companies. The Company also uses statistical and actuarial methods to estimate ultimate expected losses and loss expenses. The period of time from the occurrence of a loss, the reporting of a loss to the Company and the settlement of the Company's liability may be several months or years. During this period, additional facts and trends may be revealed. As these factors become apparent, case reserves will be adjusted, sometimes requiring an increase or decrease in the overall reserves of the Company, and at other times requiring a reallocation of incurred but not reported reserves to specific case reserves. These estimates are reviewed regularly, and such adjustments, if any, are reflected in earnings in the period in which they become known. While management believes that it has made a reasonable estimate of ultimate losses, there can be no assurances that ultimate losses and loss expenses will not exceed the total reserves.

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The following table represents an analysis of paid and unpaid losses and loss expenses incurred and a reconciliation of the beginning and ending unpaid loss expenses for the three and six months ended June 30, 2011 and 2010:

|   | <b>Three Months Ended</b> |                          | <b>Six Months Ended</b>  |                          |
|---|---------------------------|--------------------------|--------------------------|--------------------------|
|   | <b>June 30,<br/>2011</b>  | <b>June 30,<br/>2010</b> | <b>June 30,<br/>2011</b> | <b>June 30,<br/>2010</b> |
| Reserve for losses and loss expenses, beginning of period                                       | \$ 2,534,415              | \$ 1,976,889             | \$ 2,035,973             | \$ 1,622,134             |
| Losses and loss expenses recoverable  | (453,701)                 | (198,956)                | (283,134)                | (181,765)                |
| Net reserves for losses and loss expenses, beginning of period                                  | 2,080,714                 | 1,777,933                | 1,752,839                | 1,440,369                |
| Increase (decrease) in net losses and loss expenses incurred in respect of losses occurring in: |                           |                          |                          |                          |
| Current year  | 233,012                   | 244,457                  | 735,726                  | 749,717                  |
| Prior years   | (25,705)                  | (49,563)                 | (52,221)                 | (76,292)                 |
| Total incurred losses and loss expenses   | 207,307                   | 194,894                  | 683,505                  | 673,425                  |
| Total net paid losses   | (121,046)                 | (178,431)                | (284,303)                | (306,084)                |
| Foreign exchange  | 13,580                    | (9,870)                  | 28,514                   | (23,184)                 |
| Net reserve for losses and loss expenses, end of period   | 2,180,555                 | 1,784,526                | 2,180,555                | 1,784,526                |
| Losses and loss expenses recoverable  | 439,805                   | 193,604                  | 439,805                  | 193,604                  |
| Reserve for losses and loss expenses, end of period   | \$ 2,620,360              | \$ 1,978,130             | \$ 2,620,360             | \$ 1,978,130             |

**7. Reinsurance**

The Company enters into reinsurance and retrocession agreements in order to mitigate its accumulation of loss, reduce its liability on individual risks, enable it to underwrite policies with higher limits and increase its aggregate capacity. The cession of insurance and reinsurance does not legally discharge the Company from its primary liability for the full amount of the policies, and the Company is required to pay the loss and bear collection risk if the reinsurer fails to meet its obligations under the reinsurance or retrocession agreement. Amounts recoverable from reinsurers are estimated in a manner consistent with the underlying liabilities.

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**a) Credit risk**

The Company evaluates the financial condition of its reinsurers and monitors concentration of credit risk arising from its exposure to individual reinsurers. The reinsurance program is generally placed with reinsurers whose rating, at the time of placement, was A- or better rated by Standard & Poor's or the equivalent with other rating agencies. Exposure to a single reinsurer is also controlled with restrictions dependent on rating. At June 30, 2011, 99.1% of reinsurance recoverables (which includes loss reserves recoverable and recoverables on paid losses) were from reinsurers rated A- or better and included \$98,321 of IBNR recoverable (December 31, 2010: \$146,519). Reinsurance recoverables by reinsurer are as follows:

|   | June 30, 2011     |               | December 31, 2010 |               |
|---|-------------------|---------------|-------------------|---------------|
|   | Reinsurance       | % of          | Reinsurance       | % of          |
|   | Recoverable       | Total         | Recoverable       | Total         |
| Top 10 reinsurers                       | \$ 340,391        | 72.3%         | \$ 222,420        | 71.5%         |
| Other reinsurers balances > \$1 million | 119,899           | 25.5%         | 80,221            | 25.8%         |
| Other reinsurers balances < \$1 million | 10,369            | 2.2%          | 8,489             | 2.7%          |
| <b>Total</b>                            | <b>\$ 470,659</b> | <b>100.0%</b> | <b>\$ 311,130</b> | <b>100.0%</b> |

|                                 |  | June 30, 2011 |                          |
|---------------------------------|--|---------------|--------------------------|
| Top 10 Reinsurers               |  | Rating        | % of                     |
|                                 |  | Reinsur-      | Total                    |
|                                 |  | ance          |                          |
|                                 |  | Recoverable   |                          |
| Lloyd's Syndicates              |  | A+            | \$ 74,882 22.0%          |
| Allianz                         |  | AA-           | 69,464 20.3%             |
| Hannover Re                     |  | AA-           | 35,757 10.5%             |
| Manulife                        |  | A-            | 35,000 10.3%             |
| Everest Re                      |  | A+            | 29,812 8.8%              |
| Tokio Marine / Tokio Millennium |  | AA-           | 26,106 7.7%              |
| Fully collateralized reinsurers |  | NR            | 20,396 6.0%              |
| Transatlantic Re                |  | A+            | 17,049 5.0%              |
| Odyssey Reinsurance Company     |  | A-            | 16,195 4.8%              |
| Munich Re                       |  | AA-           | 15,730 4.6%              |
| <b>Total</b>                    |  |               | <b>\$ 340,391 100.0%</b> |

|                                 |  | December 31, 2010 |                 |
|---------------------------------|--|-------------------|-----------------|
| Top 10 Reinsurers               |  | Rating            | % of            |
|                                 |  | Reinsur-          | Total           |
|                                 |  | ance              |                 |
|                                 |  | recoverable       |                 |
| Lloyd's Syndicates              |  | A+                | \$ 60,716 27.2% |
| Hannover Re                     |  | AA-               | 32,392 14.6%    |
| Fully collateralized reinsurers |  | NR                | 23,750 10.7%    |
| Montpelier Re                   |  | A-                | 20,000 9.0%     |
| Munich Re                       |  | AA-               | 17,411 7.8%     |
| Everest Re                      |  | A+                | 16,611 7.5%     |

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|                     |    |            |        |
|---------------------|----|------------|--------|
| Allianz             | AA | 14,184     | 6.4%   |
| Transatlantic Re    | A+ | 13,758     | 6.2%   |
| Tokio Millennium Re | AA | 11,980     | 5.4%   |
| Platinum Re         | A  | 11,618     | 5.2%   |
| <b>Total</b>        |    | \$ 222,420 | 100.0% |

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At June 30, 2011 and December 31, 2010, the provision for uncollectible reinsurance relating to losses recoverable was \$6,200 and \$5,652, respectively. To estimate the provision for uncollectible reinsurance recoverable, the reinsurance recoverable is first allocated to applicable reinsurers. This determination is based on a process rather than an estimate, although an element of judgment is applied. As part of this process, ceded IBNR is allocated by reinsurer. Of the \$470,659 reinsurance recoverable at June 30, 2011, \$20,396 was fully collateralized (December 31, 2010: \$23,750).

The Company uses a default analysis to estimate uncollectible reinsurance. The primary components of the default analysis are reinsurance recoverable balances by reinsurer and default factors used to determine the portion of a reinsurer's balance deemed to be uncollectible. Default factors require considerable judgment and are determined using the current rating, or rating equivalent, of each reinsurer as well as other key considerations and assumptions.

**8. Share capital*****a) Authorized and issued***

The Company's authorized share capital is 571,428,571 voting and non-voting shares with a par value of \$0.175 per share. The holders of common voting shares are entitled to receive dividends and are allocated one vote per share, provided that, if the controlled shares of any shareholder or group of related shareholders constitute more than 9.09 percent of the outstanding common shares of the Company, their voting power will be reduced to 9.09 percent.

The Company may from time to time repurchase its securities, including common shares, Junior Subordinated Deferrable Debentures and Senior Notes. In November 2009, the Board of Directors of the Company authorized an initial \$400,000 share repurchase program. On February 17, 2010, the Board of Directors of the Company authorized the Company to return up to \$750,000 to shareholders. This amount was in addition to, and in excess of, the \$135,494 of common shares purchased by the Company through February 17, 2010 under its previously authorized \$400,000 share repurchase program. On May 6, 2010, the Board of Directors authorized a self tender offer pursuant to which the Company repurchased \$300,000 in common shares. On November 4, 2010, the Board of Directors authorized a self tender offer pursuant to which the Company repurchased \$238,362 in common shares. In addition, the Board of Directors authorized separate repurchase agreements with funds affiliated with or managed by each of Aquiline Capital Partners LLC, New Mountain Capital LLC, and Vestar Capital Partners pursuant to which the Company repurchased \$61,638 in common shares. On December 20, 2010, the Board of Directors authorized the Company to return up to an additional \$400,000 to shareholders. This amount is in addition to the \$929,173 of common shares purchased by the Company through December 23, 2010 under its previously authorized share repurchase program.

The Company expects the purchases under its share repurchase program to be made from time to time in the open market or in privately negotiated transactions. The timing, form and amount of the share repurchases under the program will depend on a variety of factors, including market conditions, the Company's capital position relative to internal and rating agency targets, legal requirements and other factors. The repurchase program may be modified, extended or terminated by the Board of Directors at any time.

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The following table is a summary of the common shares issued and outstanding:

|  | <b>Common<br/>Shares</b> |
|--|--------------------------|
| Common shares issued, December 31, 2010                | 132,838,111              |
| Restricted share awards vested, net of shares withheld | 458,933                  |
| Restricted share units vested, net of shares withheld  | 9,496                    |
| Employee seller shares vested                          |                          |
| Options exercised                                      | 455,033                  |
| Warrants exercised                                     | 34,340                   |
| Common shares issued, June 30, 2011                    | 133,795,913              |
| Shares repurchased                                     | (35,031,985)             |
| Common shares outstanding, June 30, 2011               | 98,763,928               |
|  | <b>Common<br/>Shares</b> |
| Common shares issued, December 31, 2009                | 131,616,349              |
| Restricted share awards vested, net of shares withheld | 281,512                  |
| Restricted share units vested, net of shares withheld  | 57,192                   |
| Employee seller shares vested                          |                          |
| Options exercised                                      | 51,534                   |
| Warrants exercised                                     |                          |
| Common shares issued, June 30, 2010                    | 132,006,587              |
| Shares repurchased                                     | (20,598,594)             |
| Common shares outstanding, June 30, 2010               | 111,407,993              |

**b) Warrants**

During the three and six months ended June 30, 2011, 72,598 warrants were exercised which resulted in the issuance of 34,340 common shares. During the three and six months ended June 30, 2010, no warrants were exercised.

**c) Deferred share units**

Under the terms of the Company's Director Stock Compensation Plan, non-management directors may elect to receive their director fees in deferred share units rather than cash. The number of share units distributed in case of election under the plan is equal to the amount of the annual retainer fee otherwise payable to the director on such payment date divided by 100% of the fair market value of a share on such payment date. Additional deferred share units are issued in lieu of dividends that accrue on these deferred share units. The total outstanding deferred share units at June 30, 2011 were 4,802 (December 31, 2010: 4,727).

**d) Dividends**

On February 9, 2011, the Company announced a quarterly cash dividend of \$0.25 (2010: \$0.22) per common share and \$0.25 per common share equivalent for which each outstanding warrant is exercisable. This dividend was paid on March 30, 2011 to holders of record on March 15, 2011.



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On May 4, 2011, the Company announced a quarterly cash dividend of \$0.25 (2010: \$0.22) per common share and \$0.25 per common share equivalent for which each outstanding warrant is exercisable. This dividend was paid on June 30, 2011 to holders of record on June 15, 2011.

**9. Stock plans****a) Long Term Incentive Plan and Short Term Incentive Plan**

The Company's Amended and Restated 2005 Long Term Incentive Plan ( LTIP ) provides for grants to employees of options, stock appreciation rights ( SARs ), restricted shares, restricted share units, performance shares, dividend equivalents or other share-based awards. In addition, the Company may issue restricted share awards or restricted share units in connection with awards issued under its annual Short Term Incentive Plan ( STIP ). The total number of shares reserved for issuance under the LTIP and STIP are 13,126,896 shares of which 4,141,021 shares are remaining. The LTIP and STIP are administered by the Compensation Committee of the Board of Directors. No SARs have been granted to date. Grant prices are established at the fair market value of the Company's common shares at the date of grant.

**i. Options**

Options may be exercised for voting common shares upon vesting. Options have a life of 10 years and vest either ratably or at the end of the required service period from the date of grant. Grant prices are established at the estimated fair value of the Company's common shares at the date of grant using the Black-Scholes option-pricing model. The following weighted average assumptions were used for all grants to date:

| <b>Year</b> | <b>Weighted<br/>average<br/>risk free<br/>interest rate</b> | <b>Weighted<br/>average<br/>dividend<br/>yield</b> | <b>Expected<br/>life<br/>(years)</b> | <b>Expected<br/>volatility</b> |
|-------------|---|--|--------------------------------------|--------------------------------|
| 2008        | 3.5%  | 3.2%   | 7                                    | 30.0%                          |
| 2009        | 3.9%  | 3.7%   | 2                                    | 34.6%                          |
| 2010 (a)    | n/a   | n/a  | n/a                                  | n/a                            |

(a) The Company did not grant any stock option awards during the year ended December 31, 2010 or the six months ended June 30, 2011.

Expected volatility is based on stock price volatility of comparable publicly-traded companies. The Company used the simplified method consistent with U.S. GAAP authoritative guidance on stock compensation expenses to estimate expected lives for options granted during the period as historical exercise data was not available and the options met the requirement as set out in the guidance.

Share compensation expenses of \$179 were recorded for the three months ended June 30, 2011 (2010: \$1,036). Share compensation expenses of \$1,426 were recorded for the six months ended June 30, 2011 (2010: \$2,074). The expenses represent the proportionate accrual of the fair value of each grant based on the remaining vesting period.



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Activity with respect to options for the six months ended June 30, 2011 was as follows:

|  | <b>Options</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Exercise Price</b> |
|--|----------------|---|---|
| Options outstanding, December 31, 2010 | 2,723,684      | \$ 6.74   | \$ 20.19  |
| Options granted                        |                |   |   |
| Options exercised                      | (455,033)      | 6.96  | 20.56   |
| Options forfeited                      | (1,850)        | 10.30   | 20.39   |
| Options outstanding, June 30, 2011     | 2,266,801      | \$ 6.70   | \$ 20.12  |
| Options exercisable at June 30, 2011   | 2,178,828      | \$ 6.62   | \$ 20.02  |

Activity with respect to options for the six months ended June 30, 2010 was as follows:

|  | <b>Options</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Exercise Price</b> |
|--|----------------|---|---|
| Options outstanding, December 31, 2009 | 3,278,015      | \$ 6.83   | \$ 19.88  |
| Options granted                        |                |   |   |
| Options exercised                      | (51,534)       | 5.72  | 22.34   |
| Options forfeited                      | (4,317)        | 10.30   | 20.39   |
| Options outstanding, June 30, 2010     | 3,222,164      | \$ 6.84   | \$ 19.84  |
| Options exercisable at June 30, 2010   | 2,549,805      | \$ 6.05   | \$ 20.10  |

At June 30, 2011, there were \$482 (December 31, 2010: \$851) of total unrecognized share compensation expenses in respect of options that are expected to be recognized over a weighted-average period of 0.7 years (December 31, 2010: 1.2 years).

**ii. Restricted share awards**

Restricted shares granted under the LTIP and STIP vest either ratably or at the end of the required service period and contain certain restrictions during the vesting period, relating to, among other things, forfeiture in the event of termination of employment and transferability. Share compensation expenses of \$5,792 were recorded for the three months ended June 30, 2011 (2010: \$4,735). Share compensation expenses of \$14,948 were recorded for the six months ended June 30, 2011 (2010: \$9,061). The expenses represent the proportionate accrual of the fair value of each grant based on the remaining vesting period.

Activity with respect to unvested restricted share awards for the six months ended June 30, 2011 was as follows:

| <b>Restricted<br/>Share<br/>Awards</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> |
|--|---|
|--|---|

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|  |           |    |       |
|--|-----------|----|-------|
| Restricted share awards outstanding, December 31, 2010 | 3,114,039 | \$ | 24.33 |
| Restricted share awards granted                        | 590,367   |    | 32.16 |
| Restricted share awards vested                         | (553,615) |    | 25.46 |
| Restricted share awards forfeited                      | (13,198)  |    | 27.28 |
| Restricted share awards outstanding, June 30, 2011     | 3,137,593 | \$ | 25.60 |

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Activity with respect to unvested restricted share awards for the six months ended June 30, 2010 was as follows:

|  | <b>Restricted<br/>Share<br/>Awards</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> |
|--|--|---|
| Restricted share awards outstanding, December 31, 2009 | 2,525,958                              | \$ 23.43  |
| Restricted share awards granted                        | 439,114                                | 26.17   |
| Restricted share awards vested                         | (323,520)                              | 23.91   |
| Restricted share awards forfeited                      | (22,609)                               | 23.07   |
| Restricted share awards outstanding, June 30, 2010     | 2,618,943                              | \$ 23.83  |

At June 30, 2011, there were \$50,710 (December 31, 2010: \$44,290) of total unrecognized share compensation expenses in respect of restricted share awards that are expected to be recognized over a weighted-average period of 2.7 years (December 31, 2010: 2.5 years).

**iii. Restricted share units**

Restricted share units under the LTIP and STIP vest either ratably or at the end of the required service period and contain certain restrictions during the vesting period, relating to, among other things, forfeiture in the event of termination of employment and transferability. Share compensation expenses of \$97 were recorded for the three months ended June 30, 2011 (2010: \$61). Share compensation expenses of \$211 were recorded for the six months ended June 30, 2011 (2010: \$234). The expenses represent the proportionate accrual of the fair value of each grant based on the remaining vesting period.

Activity with respect to unvested restricted share units for the six months ended June 30, 2011 was as follows:

|   | <b>Restricted<br/>Share<br/>Units</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> |
|---|---------------------------------------|---|
| Restricted share units outstanding, December 31, 2010 | 47,049                                | \$ 25.04  |
| Restricted share units granted                        | 18,388                                | 32.10   |
| Restricted share units vested                         | (13,340)                              | 24.72   |
| Restricted share units reinvested                     | 296                                   | 25.45   |
| Restricted share units forfeited                      |                                       |   |
| Restricted share units outstanding, June 30, 2011     | 52,393                                | \$ 27.60  |

Activity with respect to unvested restricted share units for the six months ended June 30, 2010 was as follows:

|   | <b>Restricted<br/>Share<br/>Units</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> |
|---|---------------------------------------|---|
| Restricted share units outstanding, December 31, 2009 | 78,591                                | \$ 24.84  |

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|   |          |    |       |
|---|----------|----|-------|
| Restricted share units granted                    | 7,952    |    | 26.07 |
| Restricted share units vested                     | (59,019) |    | 24.76 |
| Restricted share units forfeited                  | (1,094)  |    | 21.49 |
| Restricted share units outstanding, June 30, 2010 | 26,430   | \$ | 25.51 |

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At June 30, 2011, there were \$1,192 (December 31, 2010: \$809) of total unrecognized share compensation expenses in respect of restricted share units that are expected to be recognized over a weighted-average period of 3.0 years (December 31, 2010: 2.7 years).

**iv. Performance share awards**

The Performance Share Awards ( PSAs ) contain a performance based component. The performance component relates to the compounded growth in the Dividend Adjusted Diluted Book Value per Share over a three year period. For PSAs granted during the period, the grant date Diluted Book Value per Share ( DBVPS ) is based on the DBVPS at the end of the most recent financial reporting year. The Dividend Adjusted Performance Period End DBVPS will be the DBVPS three years after the grant date DBVPS. The fair value estimate earns over the requisite attribution period and the estimate will be reassessed at the end of each performance period which will reflect any adjustments in the consolidated statements of income in the period in which they are determined.

Share compensation expenses of \$528 were recorded for the three months ended June 30, 2011 (2010: \$nil). Share compensation expenses of \$872 were recorded for the six months ended June 30, 2011 (2010: \$nil). The expenses represent the proportionate accrual of the fair value of each grant based on the remaining vesting period.

Activity with respect to unvested performance share awards for the six months ended June 30, 2011 was as follows:

|   | <b>Performance<br/>Share<br/>Awards</b> |    | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> |
|---|---|----|---|
| Performance share awards outstanding, December 31, 2010 | 132,401                                 | \$ | 28.70   |
| Performance share awards granted                        | 146,618                                 |    | 32.64   |
| Performance share awards vested                         |   |    |   |
| Performance share awards forfeited                      |   |    |   |
| Performance share awards outstanding, June 30, 2011     | 279,019                                 | \$ | 30.77   |

Activity with respect to unvested performance share awards for the six months ended June 30, 2010 was as follows:

|   | <b>Performance<br/>Share<br/>Awards</b> |    | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> |
|---|---|----|---|
| Performance share awards outstanding, December 31, 2009 |   | \$ |   |
| Performance share awards granted                        |   |    |   |
| Performance share awards vested                         |   |    |   |
| Performance share awards forfeited                      |   |    |   |
| Performance share awards outstanding, June 30, 2010     |   | \$ |   |

At June 30, 2011, there were \$7,071 (December 31, 2010: \$3,375) of total unrecognized share compensation expenses in respect of PSAs that are expected to be recognized over a weighted-average period of 2.6 years

(December 31, 2010: 2.4 years).

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**b) Employee seller shares**

Pursuant to the Share Sale Agreement for the purchase of Talbot Holdings, Ltd. ( Talbot ), the Company issued 1,209,741 restricted shares to Talbot employees (the employee seller shares ). Upon consummation of the acquisition, the employee seller shares were validly issued, fully-paid and non-assessable and entitled to vote and participate in distributions and dividends in accordance with the Company s Bye-laws. However, the employee seller shares are subject to a restricted period during which they are subject to forfeiture (as implemented by repurchase by the Company for a nominal amount). Forfeiture of employee seller shares will generally occur in the event that any such Talbot employee s employment terminates, with certain exceptions, prior to the end of the restricted period. The restricted period ended for 25% of the employee seller shares on each anniversary of the closing date of July 2, 2007 for all Talbot employees other than Talbot s Chairman, such that on July 2, 2011 the potential for forfeiture was completely extinguished.

Share compensation expenses of \$1,032 were recorded for the three months ended June 30, 2011 (2010: \$1,014). Share compensation expenses of \$2,220 were recorded for the six months ended June 30, 2011 (2010: \$2,053).

Activity with respect to unvested employee seller shares for the six months ended June 30, 2011 was as follows:

|   | <b>Employee<br/>Seller<br/>Shares</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> |
|---|---------------------------------------|---|
| Employee seller shares outstanding, December 31, 2010 | 197,879                               | \$ 22.01  |
| Employee seller shares granted                        |                                       |   |
| Employee seller shares vested                         |                                       |   |
| Employee seller shares forfeited                      | (705)                                 | 22.01   |
| Employee seller shares outstanding, June 30, 2011     | 197,174                               | \$ 22.01  |

Activity with respect to unvested employee seller shares for six months ended June 30, 2010 was as follows:

|   | <b>Employee<br/>Seller<br/>Shares</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> |
|---|---------------------------------------|---|
| Employee seller shares outstanding, December 31, 2009 | 410,667                               | \$ 22.01  |
| Employee seller shares granted                        |                                       |   |
| Employee seller shares vested                         |                                       |   |
| Employee seller shares forfeited                      | (3,551)                               | 22.01   |
| Employee seller shares outstanding, June 30, 2010     | 407,116                               | \$ 22.01  |

At June 30, 2011, there were \$71 (December 31, 2010: \$2,141) of total unrecognized share compensation expenses in respect of employee seller shares that are expected to be recognized during the quarter ended September 30, 2011 (December 31, 2010: weighted average period of 0.5 year).

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**c) Total share compensation expenses**

The breakdown of share compensation expenses by award type was as follows:

|                          | <b>Three Months Ended</b> |                      | <b>Six Months Ended</b> |                      |
|--------------------------|---------------------------|----------------------|-------------------------|----------------------|
|                          | <b>June 30, 2011</b>      | <b>June 30, 2010</b> | <b>June 30, 2011</b>    | <b>June 30, 2010</b> |
| Options                  | \$ 179                    | \$ 1,036             | \$ 1,426                | \$ 2,074             |
| Restricted share awards  | 5,792                     | 4,735                | 14,948                  | 9,061                |
| Restricted share units   | 97                        | 61                   | 211                     | 234                  |
| Performance share awards | 528                       |                      | 872                     |                      |
| Employee seller shares   | 1,032                     | 1,014                | 2,220                   | 2,053                |
| <b>Total</b>             | <b>\$ 7,628</b>           | <b>\$ 6,846</b>      | <b>\$ 19,677</b>        | <b>\$ 13,422</b>     |

**10. Debt and financing arrangements****a) Financing structure and finance expenses**

The financing structure at June 30, 2011 was:

|  | <b>Commitment</b>   | <b>Outstanding</b> |                   |
|--|---------------------|--------------------|-------------------|
|  |                     | <b>(a)</b>         | <b>Drawn</b>      |
| 2006 Junior Subordinated Deferrable Debentures           | \$ 150,000          | \$ 150,000         | \$ 150,000        |
| 2007 Junior Subordinated Deferrable Debentures           | 200,000             | 139,800            | 139,800           |
| 2010 Senior Notes due 2040                               | 250,000             | 250,000            | 246,928           |
| \$340,000 syndicated unsecured letter of credit facility | 340,000             |                    |                   |
| \$60,000 bilateral unsecured letter of credit facility   | 60,000              |                    |                   |
| \$500,000 secured letter of credit facility              | 500,000             | 277,679            |                   |
| Talbot FAL Facility (b)                                  | 25,000              | 25,000             |                   |
| IPC Bi-Lateral Facility                                  | 80,000              | 63,284             |                   |
| <b>Total</b>   | <b>\$ 1,605,000</b> | <b>\$ 905,763</b>  | <b>\$ 536,728</b> |

The financing structure at December 31, 2010 was:

|  | <b>Commitment</b>   | <b>Outstanding</b> |                   |
|--|---------------------|--------------------|-------------------|
|  |                     | <b>(a)</b>         | <b>Drawn</b>      |
| 2006 Junior Subordinated Deferrable Debentures           | \$ 150,000          | \$ 150,000         | \$ 150,000        |
| 2007 Junior Subordinated Deferrable Debentures           | 200,000             | 139,800            | 139,800           |
| 2010 Senior Notes due 2040                               | 250,000             | 250,000            | 246,874           |
| \$340,000 syndicated unsecured letter of credit facility | 340,000             |                    |                   |
| \$60,000 bilateral unsecured letter of credit facility   | 60,000              |                    |                   |
| \$500,000 secured letter of credit facility              | 500,000             | 268,944            |                   |
| Talbot FAL Facility (b)                                  | 25,000              | 25,000             |                   |
| IPC Bi-Lateral Facility                                  | 80,000              | 68,063             |                   |
| <b>Total</b>   | <b>\$ 1,605,000</b> | <b>\$ 901,807</b>  | <b>\$ 536,674</b> |



- (a) Indicates utilization of commitment amount, not drawn borrowings.
- (b) Talbot operates in Lloyd's through a corporate member, Talbot 2002 Underwriting Capital Ltd ( T02 ), which is the sole participant in Syndicate 1183. Lloyd's sets T02's required capital annually based on Syndicate 1183's business plan, rating environment, reserving environment together with input arising from Lloyd's discussions with, inter alia, regulatory and rating agencies. Such capital, called Funds at Lloyd's ( FAL ), comprises: cash, investments and undrawn letters of credit provided by various banks.

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Finance expenses consist of interest on our junior subordinated deferrable debentures and senior notes, the amortization of debt offering costs, fees relating to our credit facilities, fees relating to the capitalization of AlphaCat Re 2011 and the costs of FAL as follows:

|  | Three Months Ended  |                  | Six Months Ended    |                  |
|--|---------------------|------------------|---------------------|------------------|
|  | June<br>30,<br>2011 | June 30,<br>2010 | June<br>30,<br>2011 | June 30,<br>2010 |
| 2006 Junior Subordinated Deferrable Debentures | \$ 3,228            | \$ 3,589         | \$ 6,816            | \$ 7,177         |
| 2007 Junior Subordinated Deferrable Debentures | 3,028               | 3,028            | 6,057               | 6,057            |
| 2010 Senior Notes due 2040                     | 5,597               | 5,597            | 11,194              | 9,575            |
| Credit facilities                              | 1,589               | 1,109            | 3,313               | 2,420            |
| AlphaCat Re 2011 fees (a)                      | 2,919               |                  | 2,919               |                  |
| Talbot FAL Facility                            |                     | (89)             | 63                  | 333              |
| Talbot other interest                          |                     | (16)             |                     | 59               |
| Talbot third party FAL facility                |                     |                  |                     | 2,748            |
| <b>Total</b>                                   | <b>\$ 16,361</b>    | <b>\$ 13,218</b> | <b>\$ 30,362</b>    | <b>\$ 28,369</b> |

(a) Includes finance expenses attributable to noncontrolling interest.

**(b) \$250,000 2010 Senior Notes due 2040**

On January 21, 2010, the Company offered and sold \$250,000 of Senior Notes due 2040 (the 2010 Senior Notes) in a registered public offering. The 2010 Senior Notes mature on January 26, 2040, and are redeemable at the Company's option in whole any time or in part from time to time at a make-whole redemption price. The Company may redeem the notes in whole, but not in part, at any time upon the occurrence of certain tax events as described in the notes prospectus supplement. The 2010 Senior Notes bear interest at the rate of 8.875% per annum from January 26, 2010 to maturity or early redemption. Interest on the 2010 Senior Notes is payable semi-annually in arrears on January 26 and July 26 of each year, commencing on July 26, 2010. The net proceeds of \$243,967 from the sale of the 2010 Senior Notes, after the deduction of commissions paid to the underwriters in the transaction and other expenses, was used by the Company for general corporate purposes, which included the repurchase of its outstanding capital stock and payment of dividends to shareholders. Debt issuance costs of \$2,808 were deferred as an asset and amortized over the life of the 2010 Senior Notes.

The 2010 Senior Notes are unsecured and unsubordinated obligations of the Company and rank equally in right of payment with all of the Company's existing and future unsecured and unsubordinated indebtedness. The 2010 Senior Notes will be effectively junior to all of the Company's future secured debt, to the extent of the value of the collateral securing such debt, and will rank senior to all our existing and future subordinated debt. The 2010 Senior Notes will be structurally subordinated to all obligations of the Company's subsidiaries.

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Future expected payments of interest on the 2010 Senior Notes are as follows:

|                                      |                   |
|--------------------------------------|-------------------|
| 2011                                 | \$ 11,094         |
| 2012                                 | 22,188            |
| 2013                                 | 22,188            |
| 2014                                 | 22,188            |
| 2015 and thereafter                  | 565,780           |
| <b>Total minimum future payments</b> | <b>\$ 643,438</b> |

**(c) Junior subordinated deferrable debentures**

On June 15, 2006, the Company participated in a private placement of \$150,000 of junior subordinated deferrable interest debentures due 2036 (the 2006 Junior Subordinated Deferrable Debentures). The 2006 Junior Subordinated Deferrable Debentures mature on June 15, 2036, are redeemable at the Company's option at par beginning June 15, 2011, and require quarterly interest payments by the Company to the holders of the 2006 Junior Subordinated Deferrable Debentures. Interest is payable at 9.069% per annum through June 15, 2011, and thereafter at a floating rate of three-month LIBOR plus 355 basis points, reset quarterly. The proceeds of \$150,000 from the sale of the 2006 Junior Subordinated Deferrable Debentures, after the deduction of commissions paid to the placement agents in the transaction and other expenses, were used by the Company to fund Validus Re segment operations and for general working capital purposes. Debt issuance costs of \$3,750 were deferred as an asset and are amortized to income over the five year optional redemption period.

On June 21, 2007, the Company participated in a private placement of \$200,000 of junior subordinated deferrable interest debentures due 2037 (the 2007 Junior Subordinated Deferrable Debentures). The 2007 Junior Subordinated Deferrable Debentures mature on June 15, 2037, are redeemable at the Company's option at par beginning June 15, 2012, and require quarterly interest payments by the Company to the holders of the 2007 Junior Subordinated Deferrable Debentures. Interest will be payable at 8.480% per annum through June 15, 2012, and thereafter at a floating rate of three-month LIBOR plus 295 basis points, reset quarterly. The proceeds of \$200,000 from the sale of the 2007 Junior Subordinated Deferrable Debentures, after the deduction of commissions paid to the placement agents in the transaction and other expenses, were used by the Company to fund the purchase of Talbot Holdings Ltd. Debt issuance costs of \$2,000 were deferred as an asset and are amortized to income over the five year optional redemption period.

During 2008 and 2009 the Company repurchased from an unaffiliated financial institution \$60,200 principal amount of its 2007 Junior Subordinated Deferrable Debentures due 2037.

Future expected payments of interest and principal on the 2006 and 2007 Junior Subordinated Deferrable Debentures are as follows:

|                                      |                   |
|--------------------------------------|-------------------|
| 2011                                 | \$ 5,928          |
| 2012                                 | 5,928             |
| 2013                                 |                   |
| 2014                                 |                   |
| 2015 and thereafter                  | 289,800           |
| <b>Total minimum future payments</b> | <b>\$ 301,656</b> |

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**(d) Credit facilities****(i) \$340,000 syndicated unsecured letter of credit facility, \$60,000 bilateral unsecured letter of credit facility and \$500,000 secured letter of credit facility**

On March 12, 2010, the Company entered into a three-year \$340,000 syndicated unsecured letter of credit facility and a \$60,000 bilateral unsecured letter of credit facility which provide for letter of credit availability for Validus Re and the Company's other subsidiaries and revolving credit availability for the Company (the Three Year Facilities) (the full \$400,000 of which is available for letters of credit and/or revolving loans).

On March 12, 2007, the Company entered into a \$500,000 five-year secured letter of credit facility, as subsequently amended on October 25, 2007, July 24, 2009, and March 12, 2010, which provides for letter of credit availability for Validus Re and the Company's other subsidiaries (the Five Year Facility and, together with the Three Year Facilities, the Credit Facilities). The Credit Facilities were provided by a syndicate of commercial banks arranged by J.P. Morgan Securities Inc. and Deutsche Bank Securities Inc. On October 25, 2007, the Company entered into the First Amendment to the Credit Facilities to provide for, among other things, additional capacity to incur up to \$100,000 under a new Funds at Lloyd's Letter of Credit Facility (as described below) to support underwriting capacity provided to Talbot 2002 Underwriting Ltd through Syndicate 1183 at Lloyd's of London for the 2008 and 2009 underwriting years of account. The amendment also modified certain provisions in the Credit Facilities in order to permit dividend payments on existing and future preferred and hybrid securities notwithstanding certain events of default.

On September 4, 2009, the Company announced that it had entered into Amendments to its \$500,000 five-year secured letter of credit facility and its then outstanding \$200,000 three-year unsecured facility and \$100,000 Talbot FAL Facility to amend a specific investment restriction clause in order to permit the completion of the IPC Acquisition. The amendment also modified and updated certain pricing and covenant terms.

As amended, the Credit Facilities contain covenants that include, among other things, (i) the requirement that the Company initially maintain a minimum level of consolidated net worth of at least 70% of consolidated net worth (\$2,925,590) and, commencing with the end of the fiscal quarter ending December 31, 2009 to be increased quarterly by an amount equal to 50% of its consolidated net income (if positive) for such quarter plus 50% of any net proceeds received from any issuance of common shares during such quarter, (ii) the requirement that the Company maintain at all times a consolidated total debt to consolidated total capitalization ratio not greater than 0.35:1.00, and (iii) the requirement that Validus Re and any other material insurance subsidiaries maintain a financial strength rating by A.M. Best of not less than B++ (Fair). For purposes of covenant compliance (i) net worth is calculated with investments carried at amortized cost and (ii) consolidated total debt does not include the Company's junior subordinated deferrable debentures. The credit facilities also contain restrictions on our ability to pay dividends and other payments in respect of equity interests at any time that we are otherwise in default with respect to certain provisions under the credit facilities, make investments, incur debt at our subsidiaries, incur liens, sell assets and merge or consolidate with others.

As of June 30, 2011, there was \$277,679 in outstanding letters of credit under the Five Year Facility (December 31, 2010: \$268,944) and \$nil outstanding under the Three Year Facilities (December 31, 2010: \$nil).

As of June 30, 2011, and throughout the reporting periods presented, the Company was in compliance with all covenants and restrictions under the Credit Facilities.

**(ii) Talbot FAL Facility**

On November 28, 2007, Talbot entered into a \$100,000 standby Letter of Credit facility (the Talbot FAL Facility) to provide Funds at Lloyd's for the 2008 and 2009 underwriting years of account; this facility is guaranteed by the Company and is secured against the assets of Validus Re. The Talbot FAL Facility was provided by a syndicate of commercial banks arranged by Lloyds TSB Bank plc and ING Bank N.V., London Branch.

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On November 19, 2009, the Company entered into an Amendment and Restatement of the Talbot FAL Facility to reduce the commitment from \$100,000 to \$25,000, and to extend the support to the 2010 and 2011 underwriting years of account.

As amended, the Talbot FAL Facility contains affirmative covenants that include, among other things, (i) the requirement that we initially maintain a minimum level of consolidated net worth of at least 70% of consolidated net worth (\$2,607,219), and commencing with the end of the fiscal quarter ending September 30, 2009 to be increased quarterly by an amount equal to 50% of our consolidated net income (if positive) for such quarter plus 50% of any net proceeds received from any issuance of common shares during such quarter, and (ii) the requirement that we maintain at all times a consolidated total debt to consolidated total capitalization ratio not greater than 0.35:1.00.

The Talbot FAL Facility also contains restrictions on our ability to incur debt at our subsidiaries, incur liens, sell assets and merge or consolidate with others. Other than in respect of existing and future preferred and hybrid securities, the payment of dividends and other payments in respect of equity interests are not permitted at any time that we are in default with respect to certain provisions under the Credit Facilities. As of June 30, 2011, the Company had \$25,000 in outstanding letters of credit under this facility.

As of June 30, 2011, and throughout the reporting periods presented, the Company was in compliance with all covenants and restrictions under the Talbot FAL Facility.

***(iii) IPC Syndicated Facility and IPC Bi-Lateral Facility***

IPC obtained letters of credit through the IPC Syndicated Facility and the IPC Bi-Lateral Facility (the IPC Facilities). In July, 2009, certain terms of these facilities were amended including suspending IPC's ability to increase existing letters of credit or to issue new letters of credit. Effective March 31, 2010, the IPC Syndicated Facility was closed. As of June 30, 2011, \$63,284 of outstanding letters of credit were issued under the IPC Bi-Lateral Facility (December 31, 2010: \$68,063).

As of June 30, 2011, and throughout the reporting periods presented, the Company was in compliance with all covenants and restrictions under the IPC Bi-Lateral Facility.

**11. Commitments and contingencies*****a) Concentrations of credit risk***

The Company's investments are managed following prudent standards of diversification. The Company attempts to limit its credit exposure by purchasing high quality fixed income investments to maintain an average portfolio credit quality of AA- or higher with mortgage and commercial mortgage-backed issues having an aggregate weighted average credit quality of triple-A. In addition, the Company limits its exposure to any single issuer to 3% or less, excluding treasury and agency securities. With the exception of the Company's bank loan portfolio, the minimum credit rating of any security purchased is Baa3/BBB- and where investments are downgraded, the Company permits a holding of up to 2% in aggregate market value, or 10% with written pre-authorization.

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At June 30, 2011, 1.0% of the portfolio, excluding bank loans, had a split rating below Baa3/BBB- and the Company did not have an aggregate exposure to any single issuer of more than 1.1% of its investment portfolio, other than with respect to government and agency securities.

**b) Funds at Lloyd's**

The amounts provided under the Talbot FAL Facility would become a liability of the Company in the event of Syndicate 1183 declaring a loss at a level which would call on this arrangement.

Talbot operates in Lloyd's through a corporate member, Talbot 2002 Underwriting Capital Ltd ( T02 ), which is the sole participant in Syndicate 1183. Lloyd's sets T02's required capital annually based on syndicate 1183's business plan, rating environment, reserving environment together with input arising from Lloyd's discussions with, inter alia, regulatory and rating agencies. Such capital, called Funds at Lloyd's ( FAL ), comprises: cash, investments and undrawn letters of credit provided by various banks. The amounts of cash, investments and letters of credit at June 30, 2011 amounted to \$441,000 (December 31, 2010: \$441,000) of which \$25,000 is provided under the Talbot FAL Facility (December 31, 2010: \$25,000).

**c) Lloyd's Central Fund**

Whenever a member of Lloyd's is unable to pay its debts to policyholders, such debts may be payable by the Lloyd's Central Fund. If Lloyd's determines that the Central Fund needs to be increased, it has the power to assess premium levies on current Lloyd's members up to 3% of a member's underwriting capacity in any one year. The Company does not believe that any assessment is likely in the foreseeable future and has not provided any allowance for such an assessment. However, based on the Company's 2011 estimated premium income at Lloyd's of £560,000, the June 30, 2011 exchange rate of £1 equals \$1.6018 and assuming the maximum 3% assessment, the Company would be assessed approximately \$26,910.

**12. Related party transactions**

The transactions listed below are classified as related party transactions as each counterparty has either a direct or indirect shareholding in the Company.

a) On December 8, 2005, the Company entered into agreements with Goldman Sachs Asset Management and its affiliates ( GSAM ) under which GSAM provides investment management services for a portion of the Company's investment portfolio. For the three and six months ended June 30, 2010, GSAM was deemed to be a related party due to a combination of GSAM being a shareholder in the Company and having an employee on the Company's Board of Directors during this period. For the three and six months ended June 30, 2011, GSAM was no longer a related party due to the resignation of Sumit Rajpal from the Board of Directors effective February 7, 2011. Investment management fees earned by GSAM for the three and six months ended June 30, 2010 were \$241 and \$733, respectively. Management believes that the fees charged were consistent with those that would have been charged in arm's-length transactions with unrelated third parties.

b) Aquiline Capital Partners, LLC and its related companies ( Aquiline ), which own 6,255,943 shares in the Company, hold warrants to purchase 2,756,088 shares, and have two employees on the Company's Board of Directors who do not receive compensation from the Company, are shareholders of Group Ark Insurance Holdings Ltd. ( Group Ark ). Christopher E. Watson, a director of the Company, also serves as a director of Group Ark. Pursuant to reinsurance agreements with a subsidiary of Group Ark, the Company recognized gross premiums written during the three and six months ended June 30, 2011 of \$900 (2010: \$601) and \$1,411 (2010: \$1,341), respectively, of which \$1,038 was included in premiums receivable at June 30, 2011 (December 31, 2010: \$378). The Company also recognized reinsurance premiums ceded during the three and six months ended June 30, 2011 of \$nil (2010: \$nil) and \$163 (2010: \$606), respectively, of which \$49 was included in reinsurance balances payable at June 30, 2011 (December 31, 2010: \$132). Earned premium adjustments of \$344 (2010: \$213) and \$678 (2010: \$881) were incurred during the three and six months ended June 30, 2011.

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c) Aquiline is also a shareholder of Tiger Risk Partners LLC ( Tiger Risk ). Christopher E. Watson, a director of the Company serves as a director of Tiger Risk. Pursuant to certain reinsurance contracts, the Company recognized brokerage expenses paid to Tiger Risk for the three and six months ended June 30, 2011 of \$628 (2010: \$1,432) and \$1,081 (2010: \$1,469), respectively, of which \$829 was included in accounts payable and accrued expenses at June 30, 2011 (December 31, 2010: \$792).

d) On November 24, 2009, the Company entered into an Investment Management Agreement with Conning, Inc. ( Conning ) to manage a portion of the Company's investment portfolio. Aquiline acquired Conning on June 16, 2009. John J. Hendrickson and Jeffrey W. Greenberg, directors of the Company, each serve as a director of Conning Holdings Corp., the parent company of Conning and Michael Carpenter, the Chairman of Talbot Holdings, Ltd. serves as a director of a subsidiary company of Conning Holdings Corp. Investment management fees earned by Conning for the three and six months ended June 30, 2011 were \$234 (2010: \$100) and \$380 (2010: \$186), respectively, of which \$203 (December 31, 2010: \$97) was included in accounts payable and accrued expenses at June 30, 2011.

**13. Earnings per share**

The following table sets forth the computation of basic and diluted earnings (loss) per share available (attributable) to common shareholders for the three and six months ended June 30, 2011 and 2010:

|  | <b>Three Months Ended</b> |                          | <b>Six Months Ended</b>  |                          |
|--|---------------------------|--------------------------|--------------------------|--------------------------|
|  | <b>June 30,<br/>2011</b>  | <b>June 30,<br/>2010</b> | <b>June 30,<br/>2011</b> | <b>June 30,<br/>2010</b> |
| <b>Basic earnings per share</b>  |                           |                          |                          |                          |
| Income (loss) available (attributable) to Validus                                      | \$ 109,884                | \$ 179,782               | \$ (62,480)              | \$ 61,404                |
| less: Dividends and distributions declared on outstanding warrants                     | (1,966)                   | (1,749)                  | (3,950)                  | (3,498)                  |
| Income (loss) available (attributable) to common shareholders                          | \$ 107,918                | \$ 178,033               | \$ (66,430)              | \$ 57,906                |
| Weighted average number of common shares outstanding                                   | 98,385,924                | 121,009,553              | 98,165,132               | 123,821,415              |
| <b>Basic earnings (loss) per share available (attributable) to common shareholders</b> | <b>\$ 1.10</b>            | <b>\$ 1.47</b>           | <b>\$ (0.68)</b>         | <b>\$ 0.47</b>           |
| <b>Diluted earnings per share</b>  |                           |                          |                          |                          |
| Income (loss) available (attributable) to Validus                                      | \$ 109,884                | \$ 179,782               | \$ (62,480)              | \$ 61,404                |
| less: Dividends and distributions declared on outstanding warrants                     |                           |                          | (3,950)                  | (3,498)                  |
|  | \$ 109,884                | \$ 179,782               | \$ (66,430)              | \$ 57,906                |

Income (loss) available (attributable) to  
common shareholders

|  |                |                |                  |                |
|--|----------------|----------------|------------------|----------------|
| Weighted average number of common<br>shares outstanding  | 98,385,924     | 121,009,553    | 98,165,132       | 123,821,415    |
| Share equivalents:   |                |                |                  |                |
| Warrants   | 3,561,096      | 2,339,922      |                  |                |
| Stock options  | 908,590        | 794,625        |                  | 840,067        |
| Unvested restricted shares   | 1,706,840      | 1,008,200      |                  | 1,000,247      |
| Weighted average number of common<br>shares outstanding  | 104,562,450    | 125,152,300    | 98,165,132       | 125,661,729    |
| <b>Diluted earnings (loss) per share<br/>available (attributable) to common<br/>shareholders</b> | <b>\$ 1.05</b> | <b>\$ 1.44</b> | <b>\$ (0.68)</b> | <b>\$ 0.46</b> |

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**Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (unaudited)

(Expressed in thousands of U.S. dollars, except share and per share information)

Share equivalents that would result in the issuance of common shares of 479,104 (2010: 218,497) and 247,550 (2010: 194,812) were outstanding for the three and six months ended June 30, 2011, but were not included in the computation of diluted earnings per share because the effect would be antidilutive.

**14. Subsequent events**

*Transatlantic Acquisition Proposal*

On June 12, 2011, Transatlantic Holdings, Inc. ( Transatlantic ) and Allied World Assurance Company Holdings, AG ( Allied World ) entered into an Agreement and Plan of Merger (the Transatlantic-Allied World Merger Agreement ).

On July 12, 2011, the Company announced that it had delivered to the Board of Directors of Transatlantic a proposal to merge the businesses of the Company and Transatlantic. Pursuant to the proposal, Transatlantic stockholders would receive 1.5564 Validus voting common shares in the merger and \$8.00 in cash per share pursuant to a one-time special dividend from Transatlantic immediately prior to closing of the merger for each share of Transatlantic common stock they own.

On July 20, 2011, the Company filed a preliminary proxy statement with the SEC in connection with the special meeting of stockholders of Transatlantic, urging the Transatlantic shareholders to vote against the Transatlantic-Allied World Merger Agreement.

On July 25, 2011, the Company commenced an exchange offer for all of the outstanding shares of common stock of Transatlantic. Under the terms of the exchange offer, Transatlantic stockholders would receive 1.5564 Validus voting common shares and \$8.00 in cash for each share of Transatlantic common stock they own. The terms and conditions of the exchange offer are set forth in the offering documents that the Company has filed with the SEC.

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**Validus Holdings, Ltd.**

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*Quarterly Dividend*

On August 3, 2011, the Company announced a quarterly cash dividend of \$0.25 per each common share and \$0.25 per common share equivalent for which each outstanding warrant is exercisable, payable on September 30, 2011 to holders of record on September 15, 2011.

**15. Segment information**

The Company conducts its operations worldwide through two wholly-owned subsidiaries, Validus Reinsurance, Ltd. and Talbot Holdings Ltd. from which two operating segments have been determined under U.S. GAAP segment reporting. The Company's operating segments are strategic business units that offer different products and services. They are managed and have capital allocated separately because each business requires different strategies.

**Validus Re**

The Validus Re segment is focused on short-tail lines of reinsurance. The primary lines in which the segment conducts business are property, marine and specialty which includes agriculture, aerospace and aviation, financial lines of business, nuclear, terrorism, life, accident & health, workers' compensation, crisis management and motor.

**Talbot**

The Talbot segment focuses on a wide range of marine and energy, war, political violence, commercial property, financial institutions, contingency, bloodstock, accident & health and aviation classes of business on an insurance or facultative reinsurance basis and principally property, aerospace and marine classes of business on a treaty reinsurance basis.

**Corporate and other reconciling items**

The Company has a Corporate function, which includes the activities of the parent company, and which carries out certain functions for the group. Corporate includes non-core underwriting expenses, predominantly general and administrative and stock compensation expenses. Corporate also denotes the activities of certain key executives such as the Chief Executive Officer and Chief Financial Officer. For internal reporting purposes, Corporate is reflected separately, however Corporate is not considered an operating segment under these circumstances. Other reconciling items include, but are not limited to, the elimination of intersegment revenues and expenses and unusual items that are not allocated to segments.

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(Expressed in thousands of U.S. dollars, except share and per share information)

The following tables summarize the results of our operating segments and corporate segment:

| <b>Three Months Ended June 30, 2011</b>               | <b>Validus Re</b> | <b>Talbot</b>    | <b>Corporate<br/>&amp;<br/>Eliminations</b> | <b>Total</b>      |
|---|-------------------|------------------|---|-------------------|
| <b>Underwriting income</b>                            |                   |                  |   |                   |
| Gross premiums written                                | \$ 341,651        | \$ 276,886       | \$ (13,150)                                 | \$ 605,387        |
| Reinsurance premiums ceded                            | (98,218)          | (47,278)         | 13,150                                      | (132,346)         |
| Net premiums written                                  | 243,433           | 229,608          |   | 473,041           |
| Change in unearned premiums                           | (10,755)          | (36,646)         |   | (47,401)          |
| <b>Net premiums earned</b>                            | <b>232,678</b>    | <b>192,962</b>   |   | <b>425,640</b>    |
| <b>Underwriting deductions</b>                        |                   |                  |   |                   |
| Losses and loss expenses                              | 94,035            | 113,272          |   | 207,307           |
| Policy acquisition costs                              | 35,769            | 42,307           | 154   | 78,230            |
| General and administrative expenses                   | 15,458            | 34,718           | 10,665                                      | 60,841            |
| Share compensation expenses                           | 1,823             | 2,026            | 3,779                                       | 7,628             |
| <b>Total underwriting deductions</b>                  | <b>147,085</b>    | <b>192,323</b>   | <b>14,598</b>                               | <b>354,006</b>    |
| <b>Underwriting income (loss)</b>                     | <b>\$ 85,593</b>  | <b>\$ 639</b>    | <b>\$ (14,598)</b>                          | <b>\$ 71,634</b>  |
| Net investment income                                 | 22,389            | 6,372            | (2,267)                                     | 26,494            |
| Other income  | 854               | 1,967            | (2,226)                                     | 595               |
| Finance expenses                                      | (4,502)           |                  | (11,859)                                    | (16,361)          |
| <b>Operating income (loss) before taxes</b>           | <b>104,334</b>    | <b>8,978</b>     | <b>(30,950)</b>                             | <b>82,362</b>     |
| Tax (expense) benefit                                 | (4)               | (208)            | 241   | 29                |
| <b>Net operating income (loss)</b>                    | <b>\$ 104,330</b> | <b>\$ 8,770</b>  | <b>\$ (30,709)</b>                          | <b>\$ 82,391</b>  |
| Net realized gains on investments                     | 9,552             | 2,000            |   | 11,552            |
| Net unrealized gains on investments                   | 14,557            | 3,969            |   | 18,526            |
| Foreign exchange (losses) gains                       | (5,337)           | 3,410            | (64)  | (1,991)           |
| <b>Net income (loss)</b>                              | <b>\$ 123,102</b> | <b>\$ 18,149</b> | <b>\$ (30,773)</b>                          | <b>\$ 110,478</b> |
| Net income attributable to noncontrolling interest    | (594)             |                  |   | (594)             |
| <b>Net income available (attributable) to Validus</b> | <b>\$ 122,508</b> | <b>\$ 18,149</b> | <b>\$ (30,773)</b>                          | <b>\$ 109,884</b> |

**Selected ratios:**

|   |                     |                     |                  |                     |
|---|---------------------|---------------------|------------------|---------------------|
| Net premiums written / Gross premiums written | 71.3%               | 82.9%               | 78.1%            |                     |
| Losses and loss expenses                      | 40.4%               | 58.7%               | 48.7%            |                     |
| Policy acquisition costs                      | 15.4%               | 21.9%               | 18.4%            |                     |
| General and administrative expenses (a)       | 7.4%                | 19.0%               | 16.1%            |                     |
| Expense ratio                                 | 22.8%               | 40.9%               | 34.5%            |                     |
| Combined ratio                                | 63.2%               | 99.6%               | 83.2%            |                     |
| <b>Total assets</b>                           | <b>\$ 5,411,663</b> | <b>\$ 2,759,850</b> | <b>\$ 88,275</b> | <b>\$ 8,259,788</b> |

(a) Ratios are based on net premiums earned. The general and administrative expense ratio includes share compensation expenses.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (unaudited)

(Expressed in thousands of U.S. dollars, except share and per share information)

| <b>Three Months Ended June 30, 2010</b>                      | <b>Validus Re</b> | <b>Talbot</b>    | <b>Corporate<br/>&amp;<br/>Eliminations</b> | <b>Total</b>      |
|--|-------------------|------------------|---|-------------------|
| <b>Underwriting income</b>                                   |                   |                  |   |                   |
| Gross premiums written                                       | \$ 284,328        | \$ 253,710       | \$ (21,177)                                 | \$ 516,861        |
| Reinsurance premiums ceded                                   | (41,175)          | (47,728)         | 21,177                                      | (67,726)          |
| Net premiums written   | 243,153           | 205,982          |   | 449,135           |
| Change in unearned premiums                                  | 18,888            | (30,079)         |   | (11,191)          |
| <b>Net premiums earned</b>                                   | <b>262,041</b>    | <b>175,903</b>   |   | <b>437,944</b>    |
| <b>Underwriting deductions</b>                               |                   |                  |   |                   |
| Losses and loss expenses                                     | 123,793           | 71,101           |   | 194,894           |
| Policy acquisition costs                                     | 37,979            | 38,647           | (2,500)                                     | 74,126            |
| General and administrative expenses                          | 10,983            | 24,960           | 16,436                                      | 52,379            |
| Share compensation expenses                                  | 1,749             | 1,468            | 3,629                                       | 6,846             |
| <b>Total underwriting deductions</b>                         | <b>174,504</b>    | <b>136,176</b>   | <b>17,565</b>                               | <b>328,245</b>    |
| <b>Underwriting income (loss)</b>                            | <b>\$ 87,537</b>  | <b>\$ 39,727</b> | <b>\$ (17,565)</b>                          | <b>\$ 109,699</b> |
| Net investment income  | 29,914            | 7,251            | (2,356)                                     | 34,809            |
| Other income   | 1,477             | 3,084            | (1,864)                                     | 2,697             |
| Finance expenses   | (1,107)           | 105              | (12,216)                                    | (13,218)          |
| <b>Operating income (loss) before taxes</b>                  | <b>117,821</b>    | <b>50,167</b>    | <b>(34,001)</b>                             | <b>133,987</b>    |
| Tax (expense) benefit  | (94)              | (4,094)          | 1   | (4,187)           |
| <b>Net operating income (loss)</b>                           | <b>\$ 117,727</b> | <b>\$ 46,073</b> | <b>\$ (34,000)</b>                          | <b>\$ 129,800</b> |
| Net realized gains on investments                            | 10,363            | 2,078            |   | 12,441            |
| Net unrealized gains on investments                          | 35,697            | 5,943            |   | 41,640            |
| Foreign exchange (losses)                                    | (843)             | (3,243)          | (13)  | (4,099)           |
| <b>Net income (loss)</b>                                     | <b>\$ 162,944</b> | <b>\$ 50,851</b> | <b>\$ (34,013)</b>                          | <b>\$ 179,782</b> |
| Net income attributable to noncontrolling interest           |                   |                  |   |                   |
| <b>Net income (loss) available (attributable) to Validus</b> | <b>\$ 162,944</b> | <b>\$ 50,851</b> | <b>\$ (34,013)</b>                          | <b>\$ 179,782</b> |

**Selected ratios:**

|   |                     |                     |                  |                     |
|---|---------------------|---------------------|------------------|---------------------|
| Net premiums written / Gross premiums written | 85.5%               | 81.2%               |                  | 86.9%               |
| Losses and loss expenses                      | 47.2%               | 40.4%               |                  | 44.5%               |
| Policy acquisition costs                      | 14.5%               | 22.0%               |                  | 16.9%               |
| General and administrative expenses (a)       | 4.9%                | 15.0%               |                  | 13.5%               |
| Expense ratio                                 | 19.4%               | 37.0%               |                  | 30.4%               |
| Combined ratio                                | 66.6%               | 77.4%               |                  | 74.9%               |
| <b>Total assets</b>                           | <b>\$ 5,057,693</b> | <b>\$ 2,507,586</b> | <b>\$ 49,344</b> | <b>\$ 7,614,623</b> |

(a) Ratios are based on net premiums earned. The general and administrative expense ratio includes share compensation expenses.

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(Expressed in thousands of U.S. dollars, except share and per share information)

| <b>Six Months Ended June 30, 2011</b>                        | <b>Validus Re</b>  | <b>Talbot</b>      | <b>Corporate<br/>&amp;<br/>Eliminations</b> | <b>Total</b>        |
|--|--------------------|--------------------|---|---------------------|
| <b>Underwriting income</b>                                   |                    |                    |   |                     |
| Gross premiums written                                       | \$ 952,889         | \$ 539,943         | \$ (37,549)                                 | \$ 1,455,283        |
| Reinsurance premiums ceded                                   | (145,023)          | (134,692)          | 37,549                                      | (242,166)           |
| Net premiums written   | 807,866            | 405,251            |   | 1,213,117           |
| Change in unearned premiums                                  | (322,879)          | (35,065)           |   | (357,944)           |
| <b>Net premiums earned</b>                                   | <b>484,987</b>     | <b>370,186</b>     |   | <b>855,173</b>      |
| <b>Underwriting deductions</b>                               |                    |                    |   |                     |
| Losses and loss expenses                                     | 404,579            | 278,926            |   | 683,505             |
| Policy acquisition costs                                     | 75,835             | 79,523             | 168   | 155,526             |
| General and administrative expenses                          | 26,115             | 63,440             | 19,763                                      | 109,318             |
| Share compensation expenses                                  | 4,928              | 4,745              | 10,004                                      | 19,677              |
| <b>Total underwriting deductions</b>                         | <b>511,457</b>     | <b>426,634</b>     | <b>29,935</b>                               | <b>968,026</b>      |
| <b>Underwriting (loss)</b>                                   | <b>\$ (26,470)</b> | <b>\$ (56,448)</b> | <b>\$ (29,935)</b>                          | <b>\$ (112,853)</b> |
| Net investment income  | 48,040             | 12,962             | (4,533)                                     | 56,469              |
| Other income   | 2,287              | 4,984              | (5,070)                                     | 2,201               |
| Finance expenses   | (6,215)            | (63)               | (24,084)                                    | (30,362)            |
| <b>Operating income (loss) before taxes</b>                  | <b>17,642</b>      | <b>(38,565)</b>    | <b>(63,622)</b>                             | <b>(84,545)</b>     |
| Tax (expense) benefit  | (6)                | 1,585              | (91)  | 1,488               |
| <b>Net operating income (loss)</b>                           | <b>\$ 17,636</b>   | <b>\$ (36,980)</b> | <b>\$ (63,713)</b>                          | <b>\$ (83,057)</b>  |
| Net realized gains on investments                            | 13,471             | 4,460              |   | 17,931              |
| Net unrealized gains (losses) on investments                 | 6,042              | (344)              |   | 5,698               |
| Foreign exchange (losses) gains                              | (9,697)            | 7,311              | (72)  | (2,458)             |
| <b>Net income (loss)</b>                                     | <b>\$ 27,452</b>   | <b>\$ (25,553)</b> | <b>\$ (63,785)</b>                          | <b>\$ (61,886)</b>  |
| Net income attributable to noncontrolling interest           | (594)              |                    |   | (594)               |
| <b>Net income (loss) available (attributable) to Validus</b> | <b>\$ 26,858</b>   | <b>\$ (25,553)</b> | <b>\$ (63,785)</b>                          | <b>\$ (62,480)</b>  |

**Selected ratios:**

|   |                     |                     |                  |                     |
|---|---------------------|---------------------|------------------|---------------------|
| Net premiums written / Gross premiums written | 84.8%               | 75.1%               |                  | 83.4%               |
| Losses and loss expenses                      | 83.4%               | 75.3%               |                  | 79.9%               |
| Policy acquisition costs                      | 15.6%               | 21.5%               |                  | 18.2%               |
| General and administrative expenses (a)       | 6.4%                | 18.4%               |                  | 15.1%               |
| Expense ratio                                 | 22.0%               | 39.9%               |                  | 33.3%               |
| Combined ratio                                | 105.4%              | 115.2%              |                  | 113.2%              |
| <b>Total assets</b>                           | <b>\$ 5,411,663</b> | <b>\$ 2,759,850</b> | <b>\$ 88,275</b> | <b>\$ 8,259,788</b> |

(a) Ratios are based on net premiums earned. The general and administrative expense ratio includes share compensation expenses.



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(Expressed in thousands of U.S. dollars, except share and per share information)

| <b>Six Months Ended June 30, 2010</b>                        | <b>Validus Re</b>  | <b>Talbot</b>    | <b>Corporate<br/>&amp;<br/>Eliminations</b> | <b>Total</b>       |
|--|--------------------|------------------|---|--------------------|
| <b>Underwriting income</b>                                   |                    |                  |   |                    |
| Gross premiums written                                       | \$ 924,623         | \$ 524,251       | \$ (61,079)                                 | \$ 1,387,795       |
| Reinsurance premiums ceded                                   | (54,285)           | (165,259)        | 61,079                                      | (158,465)          |
| Net premiums written   | 870,338            | 358,992          |   | 1,229,330          |
| Change in unearned premiums                                  | (324,376)          | (9,316)          |   | (333,692)          |
| <b>Net premiums earned</b>                                   | <b>545,962</b>     | <b>349,676</b>   |   | <b>895,638</b>     |
| <b>Underwriting deductions</b>                               |                    |                  |   |                    |
| Losses and loss expenses                                     | 472,713            | 200,712          |   | 673,425            |
| Policy acquisition costs                                     | 81,482             | 73,592           | (4,772)                                     | 150,302            |
| General and administrative expenses                          | 27,295             | 50,508           | 28,145                                      | 105,948            |
| Share compensation expenses                                  | 3,378              | 3,027            | 7,017                                       | 13,422             |
| <b>Total underwriting deductions</b>                         | <b>584,868</b>     | <b>327,839</b>   | <b>30,390</b>                               | <b>943,097</b>     |
| <b>Underwriting (loss) income</b>                            | <b>\$ (38,906)</b> | <b>\$ 21,837</b> | <b>\$ (30,390)</b>                          | <b>\$ (47,459)</b> |
| Net investment income  | 59,159             | 14,571           | (4,622)                                     | 69,108             |
| Other income   | 2,555              | 5,059            | (4,029)                                     | 3,585              |
| Finance expenses   | (2,400)            | (3,140)          | (22,829)                                    | (28,369)           |
| <b>Operating income (loss) before taxes</b>                  | <b>20,408</b>      | <b>38,327</b>    | <b>(61,870)</b>                             | <b>(3,135)</b>     |
| Tax (expense)  | (185)              | (3,299)          | (6)   | (3,490)            |
| <b>Net operating income (loss)</b>                           | <b>\$ 20,223</b>   | <b>\$ 35,028</b> | <b>\$ (61,876)</b>                          | <b>\$ (6,625)</b>  |
| Net realized gains on investments                            | 20,142             | 3,697            |   | 23,839             |
| Net unrealized gains (losses) on investments                 | 47,892             | 9,161            |   | 57,053             |
| Foreign exchange (losses)                                    | (5,982)            | (6,842)          | (39)  | (12,863)           |
| <b>Net income (loss)</b>                                     | <b>\$ 82,275</b>   | <b>\$ 41,044</b> | <b>\$ (61,915)</b>                          | <b>\$ 61,404</b>   |
| Net income attributable to noncontrolling interest           |                    |                  |   |                    |
| <b>Net income (loss) available (attributable) to Validus</b> | <b>\$ 82,275</b>   | <b>\$ 41,044</b> | <b>\$ (61,915)</b>                          | <b>\$ 61,404</b>   |

**Selected ratios:**

|   |        |       |        |
|---|--------|-------|--------|
| Net premiums written / Gross premiums written | 94.1%  | 68.5% | 88.6%  |
| Losses and loss expenses                      | 86.6%  | 57.4% | 75.2%  |
| Policy acquisition costs                      | 14.9%  | 21.0% | 16.8%  |
| General and administrative expenses (a)       | 5.6%   | 15.3% | 13.3%  |
| Expense ratio                                 | 20.5%  | 36.3% | 30.1%  |
| Combined ratio                                | 107.1% | 93.7% | 105.3% |

|                     |                     |                     |                  |                     |
|---------------------|---------------------|---------------------|------------------|---------------------|
| <b>Total assets</b> | <b>\$ 5,057,693</b> | <b>\$ 2,507,586</b> | <b>\$ 49,344</b> | <b>\$ 7,614,623</b> |
|---------------------|---------------------|---------------------|------------------|---------------------|

(a) Ratios are based on net premiums earned. The general and administrative expense ratio includes share compensation expenses.

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(Expressed in thousands of U.S. dollars, except share and per share information)

The Company's exposures are generally diversified across geographic zones. The following tables set forth the gross premiums written allocated to the territory of coverage exposure for the periods indicated:

**Three Months Ended June 30, 2011****Gross premiums written**

|                                       | <b>Validus<br/>Re</b> | <b>Talbot</b>     | <b>Eliminations</b> | <b>Total</b>      | <b>%</b>      |
|---------------------------------------|-----------------------|-------------------|---------------------|-------------------|---------------|
| United States                         | \$ 261,364            | \$ 34,181         | \$ (2,307)          | \$ 293,238        | 48.5%         |
| Worldwide excluding United States     |                       |                   |                     |                   |               |
| (a)                                   | 2,580                 | 57,204            | (257)               | 59,527            | 9.8%          |
| Europe                                | 10,729                | 18,935            | (59)                | 29,605            | 4.9%          |
| Latin America and Caribbean           | 11,432                | 22,265            | (8,942)             | 24,755            | 4.1%          |
| Japan                                 | 23,871                | 2,216             |                     | 26,087            | 4.3%          |
| Canada                                | 10                    | 2,443             | (10)                | 2,443             | 0.4%          |
| Rest of the world (b)                 | 8,939                 |                   |                     | 8,939             | 1.5%          |
| Sub-total, non United States          | 57,561                | 103,063           | (9,268)             | 151,356           | 25.0%         |
| Worldwide including United States (a) | 12,584                | 15,506            | (40)                | 28,050            | 4.6%          |
| Marine and Aerospace (c)              | 10,142                | 124,136           | (1,535)             | 132,743           | 21.9%         |
| <b>Total</b>                          | <b>\$ 341,651</b>     | <b>\$ 276,886</b> | <b>\$ (13,150)</b>  | <b>\$ 605,387</b> | <b>100.0%</b> |

**Three Months Ended June 30, 2010****Gross premiums written**

|                                       | <b>Validus<br/>Re</b> | <b>Talbot</b>     | <b>Eliminations</b> | <b>Total</b>      | <b>%</b>      |
|---------------------------------------|-----------------------|-------------------|---------------------|-------------------|---------------|
| United States                         | \$ 186,653            | \$ 29,691         | \$ (2,020)          | \$ 214,324        | 41.5%         |
| Worldwide excluding United States     |                       |                   |                     |                   |               |
| (a)                                   | 4,830                 | 58,806            | (2,086)             | 61,550            | 11.9%         |
| Europe                                | 10,757                | 12,832            | (504)               | 23,085            | 4.4%          |
| Latin America and Caribbean           | 15,036                | 29,368            | (12,766)            | 31,638            | 6.1%          |
| Japan                                 | 19,250                | 2,901             | (72)                | 22,079            | 4.3%          |
| Canada                                | 72                    | 3,367             | (72)                | 3,367             | 0.7%          |
| Rest of the world (b)                 | 25,168                |                   |                     | 25,168            | 4.9%          |
| Sub-total, non United States          | 75,113                | 107,274           | (15,500)            | 166,887           | 32.3%         |
| Worldwide including United States (a) | 2,032                 | 15,911            | (504)               | 17,439            | 3.3%          |
| Marine and Aerospace (c)              | 20,530                | 100,834           | (3,153)             | 118,211           | 22.9%         |
| <b>Total</b>                          | <b>\$ 284,328</b>     | <b>\$ 253,710</b> | <b>\$ (21,177)</b>  | <b>\$ 516,861</b> | <b>100.0%</b> |

(a) Represents risks in two or more geographic zones.

(b) Represents risks in one geographic zone.

- (c) Not classified as geographic area as marine and aerospace risks can span multiple geographic areas and are not fixed locations in some instances.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (unaudited)

(Expressed in thousands of U.S. dollars, except share and per share information)

The Company's exposures are generally diversified across geographic zones. The following tables set forth the gross premiums written allocated to the territory of coverage exposure for the periods indicated:

**Six Months Ended June 30, 2011****Gross premiums written**

|                                   | <b>Validus<br/>Re</b> | <b>Talbot</b>     | <b>Eliminations</b> | <b>Total</b>        | <b>%</b>      |
|-----------------------------------|-----------------------|-------------------|---------------------|---------------------|---------------|
| United States                     | \$ 453,729            | \$ 62,012         | \$ (4,204)          | \$ 511,537          | 35.2%         |
| Worldwide excluding United States |                       |                   |                     |                     |               |
| (a)                               | 29,558                | 125,171           | (2,969)             | 151,760             | 10.4%         |
| Europe                            | 69,695                | 34,944            | (561)               | 104,078             | 7.2%          |
| Latin America and Caribbean       | 36,551                | 40,533            | (22,571)            | 54,513              | 3.7%          |
| Japan                             | 34,069                | 2,756             | (100)               | 36,725              | 2.5%          |
| Canada                            | 110                   | 6,251             | (110)               | 6,251               | 0.4%          |
| Rest of the world (b)             | 44,996                |                   |                     | 44,996              | 3.1%          |
| Sub-total, non United States      | 214,979               | 209,655           | (26,311)            | 398,323             | 27.3%         |
| Worldwide including United States |                       |                   |                     |                     |               |
| (a)                               | 80,780                | 26,036            | (542)               | 106,274             | 7.3%          |
| Marine and Aerospace (c)          | 203,401               | 242,240           | (6,492)             | 439,149             | 30.2%         |
| <b>Total</b>                      | <b>\$ 952,889</b>     | <b>\$ 539,943</b> | <b>\$ (37,549)</b>  | <b>\$ 1,455,283</b> | <b>100.0%</b> |

**Six Months Ended June 30, 2010****Gross premiums written**

|                                   | <b>Validus<br/>Re</b> | <b>Talbot</b>     | <b>Eliminations</b> | <b>Total</b>        | <b>%</b>      |
|-----------------------------------|-----------------------|-------------------|---------------------|---------------------|---------------|
| United States                     | \$ 420,220            | \$ 54,974         | \$ (5,491)          | \$ 469,703          | 33.8%         |
| Worldwide excluding United States |                       |                   |                     |                     |               |
| (a)                               | 44,594                | 134,824           | (5,918)             | 173,500             | 12.5%         |
| Europe                            | 91,233                | 28,370            | (961)               | 118,642             | 8.5%          |
| Latin America and Caribbean       | 43,775                | 46,595            | (28,553)            | 61,817              | 4.5%          |
| Japan                             | 19,900                | 3,609             | (137)               | 23,372              | 1.7%          |
| Canada                            | 137                   | 7,003             | (137)               | 7,003               | 0.5%          |
| Rest of the world (b)             | 25,168                |                   |                     | 25,168              | 1.8%          |
| Sub-total, non United States      | 224,807               | 220,401           | (35,706)            | 409,502             | 29.5%         |
| Worldwide including United States |                       |                   |                     |                     |               |
| (a)                               | 78,267                | 28,687            | (2,234)             | 104,720             | 7.6%          |
| Marine and Aerospace (c)          | 201,329               | 220,189           | (17,648)            | 403,870             | 29.1%         |
| <b>Total</b>                      | <b>\$ 924,623</b>     | <b>\$ 524,251</b> | <b>\$ (61,079)</b>  | <b>\$ 1,387,795</b> | <b>100.0%</b> |

(a) Represents risks in two or more geographic zones.

- (b) Represents risks in one geographic zone.
- (c) Not classified as geographic area as marine and aerospace risks can span multiple geographic areas and are not fixed locations in some instances.

**Table of Contents****ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following is a discussion and analysis of the Company's consolidated results of operations for the three and six months ended June 30, 2011 and 2010 and the Company's consolidated financial condition, liquidity and capital resources at June 30, 2011 and December 31, 2010. This discussion and analysis should be read in conjunction with the audited consolidated financial statements and related notes for the fiscal year ended December 31, 2010, the discussions of critical accounting policies and the qualitative and quantitative disclosure about market risk contained in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2010.

For a variety of reasons, the Company's historical financial results may not accurately indicate future performance. See Cautionary Note Regarding Forward-Looking Statements. The Risk Factors set forth in Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2010 present a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained herein.

**Executive Overview**

The Company underwrites from two distinct global operating segments, Validus Reinsurance, Ltd. ( Validus Re ) and Talbot Holdings Ltd. ( Talbot ). Validus Re, the Company's principal reinsurance operating segment, operates as a Bermuda-based provider of short-tail reinsurance products on a global basis. Talbot, the Company's principal insurance operating segment, operates through its two underwriting platforms: Talbot Underwriting Ltd, which manages Syndicate 1183 at Lloyd's of London ( Lloyd's ) and which writes short-tail insurance products on a worldwide basis, and Underwriting Risk Services Ltd, which is an underwriting agency writing primarily yacht and onshore energy business on behalf of the Talbot syndicate and others.

The Company's strategy has been to concentrate primarily on short-tail risks, which has been an area where management believes current prices and terms provide an attractive risk adjusted return and the management team has proven expertise. The Company's profitability in any given period is based upon premium and investment revenues, less net losses and loss expenses, acquisition expenses and operating expenses. Financial results in the insurance and reinsurance industry are influenced by the frequency and/or severity of claims and losses, including as a result of catastrophic events, changes in interest rates, financial markets and general economic conditions, the supply of insurance and reinsurance capacity and changes in legal, regulatory and judicial environments.

On September 4, 2009, the Company acquired all of the outstanding shares of IPC (the IPC Acquisition ) in exchange for common shares and cash. IPC's operations focused on short-tail lines of reinsurance. The primary lines in which IPC conducted business were property catastrophe reinsurance and, to a limited extent, property-per-risk excess, aviation (including satellite) and other short-tail reinsurance on a worldwide basis. The IPC Acquisition was undertaken to increase the Company's capital base and gain a strategic advantage in the then current reinsurance market. This acquisition created a leading Bermuda carrier in the short-tail reinsurance market that facilitates stronger relationships with major reinsurance intermediaries.

On May 25, 2011, the Company joined with other investors in capitalizing AlphaCat Re 2011, a new special purpose sidecar reinsurer formed for the purpose of writing collateralized reinsurance and retrocessional reinsurance. Validus Re has an equity interest in AlphaCat Re 2011 and as Validus Re holds a majority of AlphaCat Re 2011's outstanding voting rights, the financial statements of AlphaCat Re 2011 are included in the consolidated financial statements of the Company. The portion of AlphaCat Re 2011's earnings attributable to third party investors for the three months ended June 30, 2011 is recorded in the consolidated statement of operations and comprehensive income as net income attributable to noncontrolling interest.

**Business Outlook and Trends**

We underwrite global specialty property insurance and reinsurance and have large aggregate exposures to natural and man-made disasters. The occurrence of claims from catastrophic events results in substantial volatility, and can have material adverse effects on the Company's financial condition and results and ability to write new business.

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This volatility affects results for the period in which the loss occurs because U.S. accounting principles do not permit reinsurers to reserve for such catastrophic events until they occur. Catastrophic events of significant magnitude historically have been relatively infrequent, although management believes the property catastrophe reinsurance market has experienced a higher level of worldwide catastrophic losses in terms of both frequency and severity in the period from 1992 to the present. We also expect that increases in the values and concentrations of insured property will increase the severity of such occurrences in the future. The Company seeks to reflect these trends when pricing contracts.

Property and other reinsurance premiums have historically risen in the aftermath of significant catastrophic losses. As loss reserves are established, industry surplus is depleted and the industry's capacity to write new business diminishes. At the same time, management believes that there is a heightened awareness of exposure to natural catastrophes on the part of cedants, rating agencies and catastrophe modeling firms, resulting in an increase in the demand for reinsurance protection.

The global property and casualty insurance and reinsurance industry has historically been highly cyclical. The Company was formed in October 2005 in response to the supply/demand imbalance resulting from the large industry losses in 2004 and 2005. In the aggregate, the Company observed substantial increases in premium rates in 2006 compared to 2005 levels. During the years ended December 31, 2007 and 2008, the Company experienced increased competition in most lines of business. Capital provided by new entrants or by the commitment of additional capital by existing insurers and reinsurers increased the supply of insurance and reinsurance which resulted in a softening of rates in most lines. However, during 2008, the insurance and reinsurance industry incurred material losses and capital declines due to Hurricanes Ike and Gustav and the global financial crisis. In the wake of these events, the January 2009 renewal season saw decreased competition and increased premium rates due to relatively scarce capital and increased demand. During 2009, the Company observed reinsurance demand stabilization and industry capital recovery from investment portfolio gains. In 2009, there were few notable large losses affecting the worldwide (re)insurance industry and no major hurricanes making landfall in the United States. During 2010, the Company continued to see increased competition and decreased premium rates in most classes of business with the exception of offshore energy, Latin America, financial institutions and political risk lines. During 2010 there was an increased level of catastrophe activity, principally the Chilean earthquake and the Deepwater Horizon events.

During the January 2011 renewal season, Validus Re increased gross premiums written on the U.S. Cat XOL lines and decreased gross premiums written in the proportional lines. In addition, Validus Re decreased gross premiums written in the International Property lines as market conditions dictated. In the aftermath of 2010's Deepwater Horizon loss, Validus Re saw additional opportunities and rate increases in the marine lines. Within its specialty lines, Validus Re increased gross premiums written in the terrorism lines among other sub-classes. During the first quarter of 2011, premiums in Talbot have been relatively stable with rate increases occurring on renewals that have suffered losses but rate reductions continuing elsewhere, as a result of good experience and excess capacity in the market. Talbot is receiving improved pricing in the energy, property and political risk lines as a result of recent loss events. The significant worldwide elevated loss activity since the beginning of 2010, in conjunction with changes to certain commercial vendors' catastrophe models, is resulting in improved pricing and demand for catastrophe reinsurance. Rate levels in both the U.S. and International property catastrophe business continued to improve for mid-year 2011 renewals due to the magnitude of the worldwide loss activity.

**Financial Measures**

The Company believes the following financial indicators are important in evaluating performance and measuring the overall growth in value generated for shareholders:

*Annualized return on average equity* represents the level of net income available to shareholders generated from the average shareholders' equity during the period. Annualized return on average equity is calculated by dividing the net income for the period by the average shareholders' equity during the period. Average shareholders' equity is the average of the beginning, ending and intervening quarter end shareholders' equity balances. Percentages for the quarter and interim periods are annualized. The Company's objective is to generate superior returns on capital that appropriately reward shareholders for the risks assumed and to grow premiums written only when returns meet or exceed internal requirements. Details of annualized return on average equity are provided below.





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|                                     | <b>Three Months Ended</b> |                      | <b>Year Ended</b>        |
|-------------------------------------|---------------------------|----------------------|--------------------------|
|                                     | <b>June 30, 2011</b>      | <b>June 30, 2010</b> | <b>December 31, 2010</b> |
| Annualized return on average equity | 13.1%                     | 19.5%                | 10.8%                    |

The decrease in annualized return on average equity for the three months ended June 30, 2011 was driven primarily by a reduction in net income. Net income available to Validus for the three months ended June 30, 2011 decreased by \$69.9 million, or 38.9% compared to the three months ended June 30, 2010. This unfavorable movement was primarily due to large loss events coupled with an unfavorable movement in unrealized gains on investments.

*Diluted book value per common share* is considered by management to be an appropriate measure of our returns to common shareholders, as we believe growth in our book value on a diluted basis ultimately translates into growth of our stock price. Diluted book value per common share decreased by \$1.07, or 3.2%, from \$32.98 at December 31, 2010 to \$31.91 at June 30, 2011. The decrease was due to the loss generated in the six months ended June 30, 2011. Diluted book value per common share is a Non-GAAP financial measure. The most comparable U.S. GAAP financial measure is book value per common share. Diluted book value per common share is calculated based on total shareholders' equity plus the assumed proceeds from the exercise of outstanding options and warrants, divided by the sum of common shares, unvested restricted shares, options and warrants outstanding (assuming their exercise). A reconciliation of diluted book value per common share to book value per common share is presented below in the section entitled *Non-GAAP Financial Measures*.

*Cash dividends per common share* are an integral part of the value created for shareholders. On August 3, 2011, the Company announced a quarterly cash dividend of \$0.25 per each common share and \$0.25 per common share equivalent for which each outstanding warrant is exercisable, payable on September 30, 2011 to holders of record on September 15, 2011.

*Underwriting income (loss)* measures the performance of the Company's core underwriting function, excluding revenues and expenses such as net investment income (loss), other income, finance expenses, net realized and unrealized gains (losses) on investments and foreign exchange gains (losses). The Company believes the reporting of underwriting income enhances the understanding of our results by highlighting the underlying profitability of the Company's core insurance and reinsurance operations. Underwriting income for the three months ended June 30, 2011 and 2010 was \$71.6 million and \$109.7 million, respectively. Underwriting income (loss) is a Non-GAAP financial measure as described in detail and reconciled in the section below entitled *Underwriting Income*.

**Critical Accounting Policies and Estimates**

There are certain accounting policies that the Company considers to be critical due to the judgment and uncertainty inherent in the application of those policies. In calculating financial statement estimates, the use of different assumptions could produce materially different estimates. The Company believes the following critical accounting policies affect significant estimates used in the preparation of our consolidated financial statements:

Reserve for losses and loss expenses;

Premiums;

Reinsurance premiums ceded and reinsurance recoverable; and

Investment valuation.

Critical accounting policies and estimates are discussed further in Item 7, Management's Discussion and Analysis of Results of Operations and Financial Condition in the Company's Annual Report on Form 10-K for the year ended December 31, 2010.



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**Segment Reporting**

Management has determined that the Company operates in two reportable segments. The two significant operating segments are Validus Re and Talbot.

**Results of Operations**

Validus Re commenced operations on December 16, 2005. The Company's fiscal year ends on December 31. Financial statements are prepared in accordance with generally accepted accounting principles in the United States of America ( U.S. GAAP ) for interim financial information.

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The following table presents results of operations for the three and six months ended June 30, 2011 and 2010:

| <b>(Dollars in thousands)</b>                                | <b>Three Months Ended June</b> |                   | <b>Six Months Ended June 30,</b> |                  |
|--|--------------------------------|-------------------|----------------------------------|------------------|
|  | <b>2011</b>                    | <b>2010</b>       | <b>2011</b>                      | <b>2010</b>      |
| Gross premiums written                                       | \$ 605,387                     | \$ 516,861        | \$ 1,455,283                     | \$ 1,387,795     |
| Reinsurance premiums ceded                                   | (132,346)                      | (67,726)          | (242,166)                        | (158,465)        |
| Net premiums written   | 473,041                        | 449,135           | 1,213,117                        | 1,229,330        |
| Change in unearned premiums                                  | (47,401)                       | (11,191)          | (357,944)                        | (333,692)        |
| <b>Net premiums earned</b>                                   | <b>425,640</b>                 | <b>437,944</b>    | <b>855,173</b>                   | <b>895,638</b>   |
| Losses and loss expenses                                     | 207,307                        | 194,894           | 683,505                          | 673,425          |
| Policy acquisition costs                                     | 78,230                         | 74,126            | 155,526                          | 150,302          |
| General and administrative expenses                          | 60,841                         | 52,379            | 109,318                          | 105,948          |
| Share compensation expenses                                  | 7,628                          | 6,846             | 19,677                           | 13,422           |
| <b>Total underwriting deductions</b>                         | <b>354,006</b>                 | <b>328,245</b>    | <b>968,026</b>                   | <b>943,097</b>   |
| <b>Underwriting income (loss) (a)</b>                        | <b>71,634</b>                  | <b>109,699</b>    | <b>(112,853)</b>                 | <b>(47,459)</b>  |
| Net investment income  | 26,494                         | 34,809            | 56,469                           | 69,108           |
| Other income   | 595                            | 2,697             | 2,201                            | 3,585            |
| Finance expenses   | (16,361)                       | (13,218)          | (30,362)                         | (28,369)         |
| <b>Operating income (loss) before taxes</b>                  | <b>82,362</b>                  | <b>133,987</b>    | <b>(84,545)</b>                  | <b>(3,135)</b>   |
| Tax benefit (expense)  | 29                             | (4,187)           | 1,488                            | (3,490)          |
| <b>Net operating income (loss) (a)</b>                       | <b>82,391</b>                  | <b>129,800</b>    | <b>(83,057)</b>                  | <b>(6,625)</b>   |
| Net realized gains on investments                            | 11,552                         | 12,441            | 17,931                           | 23,839           |
| Net unrealized gains on investments                          | 18,526                         | 41,640            | 5,698                            | 57,053           |
| Foreign exchange (losses)                                    | (1,991)                        | (4,099)           | (2,458)                          | (12,863)         |
| <b>Net income (loss)</b>                                     | <b>110,478</b>                 | <b>179,782</b>    | <b>(61,886)</b>                  | <b>61,404</b>    |
| Net income attributable to noncontrolling interest           | (594)                          |                   | (594)                            |                  |
| <b>Net income (loss) available (attributable) to Validus</b> | <b>\$ 109,884</b>              | <b>\$ 179,782</b> | <b>\$ (62,480)</b>               | <b>\$ 61,404</b> |
| <b>Selected ratios:</b>                                      |                                |                   |                                  |                  |
| Net premiums written / Gross premiums written                | 78.1%                          | 86.9%             | 83.4%                            | 88.6%            |

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|   |       |       |        |        |
|---|-------|-------|--------|--------|
| Losses and loss expenses                | 48.7% | 44.5% | 79.9%  | 75.2%  |
| Policy acquisition costs                | 18.4% | 16.9% | 18.2%  | 16.8%  |
| General and administrative expenses (b) | 16.1% | 13.5% | 15.1%  | 13.3%  |
| Expense ratio                           | 34.5% | 30.4% | 33.3%  | 30.1%  |
| Combined ratio                          | 83.2% | 74.9% | 113.2% | 105.3% |

- a) Non-GAAP Financial Measures: In presenting the Company's results, management has included and discussed underwriting income and operating income that are not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. A reconciliation of underwriting income to net income, the most comparable U.S. GAAP financial measure, is presented in the section below entitled Underwriting Income.
- b) The general and administrative ratio includes share compensation expenses.

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|                                       | <b>Three Months Ended June</b> |                | <b>Six Months Ended June</b> |                 |
|---------------------------------------|--------------------------------|----------------|------------------------------|-----------------|
|                                       | <b>30,</b>                     |                | <b>30,</b>                   |                 |
|                                       | <b>2011</b>                    | <b>2010</b>    | <b>2011</b>                  | <b>2010</b>     |
| <b>Validus Re</b>                     |                                |                |                              |                 |
| Gross premiums written                | \$ 341,651                     | \$ 284,328     | \$ 952,889                   | \$ 924,623      |
| Reinsurance premiums ceded            | (98,218)                       | (41,175)       | (145,023)                    | (54,285)        |
| Net premiums written                  | 243,433                        | 243,153        | 807,866                      | 870,338         |
| Change in unearned premiums           | (10,755)                       | 18,888         | (322,879)                    | (324,376)       |
| <b>Net premiums earned</b>            | <b>232,678</b>                 | <b>262,041</b> | <b>484,987</b>               | <b>545,962</b>  |
| Losses and loss expenses              | 94,035                         | 123,793        | 404,579                      | 472,713         |
| Policy acquisition costs              | 35,769                         | 37,979         | 75,835                       | 81,482          |
| General and administrative expenses   | 15,458                         | 10,983         | 26,115                       | 27,295          |
| Share compensation expenses           | 1,823                          | 1,749          | 4,928                        | 3,378           |
| <b>Total underwriting deductions</b>  | <b>147,085</b>                 | <b>174,504</b> | <b>511,457</b>               | <b>584,868</b>  |
| <b>Underwriting income (loss) (a)</b> | <b>85,593</b>                  | <b>87,537</b>  | <b>(26,470)</b>              | <b>(38,906)</b> |
| <b>Talbot</b>                         |                                |                |                              |                 |
| Gross premiums written                | \$ 276,886                     | \$ 253,710     | \$ 539,943                   | \$ 524,251      |
| Reinsurance premiums ceded            | (47,278)                       | (47,728)       | (134,692)                    | (165,259)       |
| Net premiums written                  | 229,608                        | 205,982        | 405,251                      | 358,992         |
| Change in unearned premiums           | (36,646)                       | (30,079)       | (35,065)                     | (9,316)         |
| <b>Net premiums earned</b>            | <b>192,962</b>                 | <b>175,903</b> | <b>370,186</b>               | <b>349,676</b>  |
| Losses and loss expenses              | 113,272                        | 71,101         | 278,926                      | 200,712         |
| Policy acquisition costs              | 42,307                         | 38,647         | 79,523                       | 73,592          |
| General and administrative expenses   | 34,718                         | 24,960         | 63,440                       | 50,508          |
| Share compensation expenses           | 2,026                          | 1,468          | 4,745                        | 3,027           |
| <b>Total underwriting deductions</b>  | <b>192,323</b>                 | <b>136,176</b> | <b>426,634</b>               | <b>327,839</b>  |
| <b>Underwriting income (loss) (a)</b> | <b>639</b>                     | <b>39,727</b>  | <b>(56,448)</b>              | <b>21,837</b>   |
| <b>Corporate &amp; Eliminations</b>   |                                |                |                              |                 |
| Gross premiums written                | \$ (13,150)                    | \$ (21,177)    | \$ (37,549)                  | \$ (61,079)     |
| Reinsurance premiums ceded            | 13,150                         | 21,177         | 37,549                       | 61,079          |
| Net premiums written                  |                                |                |                              |                 |

Change in unearned premiums

**Net premiums earned**

Losses and loss expenses

|                                     |        |         |        |         |
|-------------------------------------|--------|---------|--------|---------|
| Policy acquisition costs            | 154    | (2,500) | 168    | (4,772) |
| General and administrative expenses | 10,665 | 16,436  | 19,763 | 28,145  |
| Share compensation expenses         | 3,779  | 3,629   | 10,004 | 7,017   |

|                                      |        |        |        |        |
|--------------------------------------|--------|--------|--------|--------|
| <b>Total underwriting deductions</b> | 14,598 | 17,565 | 29,935 | 30,390 |
|--------------------------------------|--------|--------|--------|--------|

|                                |          |          |          |          |
|--------------------------------|----------|----------|----------|----------|
| <b>Underwriting (loss) (a)</b> | (14,598) | (17,565) | (29,935) | (30,390) |
|--------------------------------|----------|----------|----------|----------|

|   |           |            |              |             |
|---|-----------|------------|--------------|-------------|
| <b>Total underwriting income (loss) (a)</b> | \$ 71,634 | \$ 109,699 | \$ (112,853) | \$ (47,459) |
|---|-----------|------------|--------------|-------------|

- a) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income that is not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. A reconciliation of this measure to net income, the most comparable U.S. GAAP financial measure, is presented in the section below entitled Underwriting Income.



**Table of Contents****Three Months Ended June 30, 2011 compared to Three Months Ended June 30, 2010**

Net income available to Validus for the three months ended June 30, 2011 was \$109.9 million compared to \$179.8 million for the three months ended June 30, 2010, a decrease of \$69.9 million or 38.9%. The primary factors driving the decrease in net income were:

Decrease in underwriting income of \$38.1 million due to:

A \$12.3 million decrease in net premiums earned.

A \$13.3 million increase in other underwriting deductions including policy acquisition costs, general and administrative expenses and share compensation expenses.

A \$12.4 million increase in loss and loss expenses due to increased catastrophe losses.

An unfavorable movement of \$23.1 million in net unrealized (losses) gains on investments.

Decrease in net investment income of \$8.3 million.

The change in net income available to Validus for the three months ended June 30, 2011 of \$69.9 million as compared to the three months ended June 30, 2010 is described in the following table:

|  | <b>Three Months Ended June 30, 2011</b>                              |                 |                     |                 |
|--|--|-----------------|---------------------|-----------------|
|  | <b>Increase (Decrease) Over the Three Months Ended June 30, 2010</b> |                 |                     |                 |
|  | <b>Corporate and</b>   |                 |                     |                 |
|  | <b>Validus</b>   |                 | <b>Eliminations</b> | <b>Total</b>    |
| <b>(Dollars in thousands)</b>  | <b>Re</b>  | <b>Talbot</b>   |                     |                 |
| Notable losses (increase) decrease in net loss and loss expenses (a)       | \$ (2,852)   | \$ (16,952)     | \$                  | \$ (19,804)     |
| Less: Notable losses (decrease) increase in net reinstatement premiums (a) | (1,452)  | 5,087           |                     | 3,635           |
| Other underwriting income (loss)   | 2,360  | (27,223)        | 2,967               | (21,896)        |
| Underwriting (loss) income (b)   | (1,944)  | (39,088)        | 2,967               | (38,065)        |
| Net investment income  | (7,525)  | (879)           | 89                  | (8,315)         |
| Other income   | (623)  | (1,117)         | (362)               | (2,102)         |
| Finance expenses   | (3,395)  | (105)           | 357                 | (3,143)         |
|  | (13,487)   | (41,189)        | 3,051               | (51,625)        |
| Taxes  | 90   | 3,886           | 240                 | 4,216           |
|  | (13,397)   | (37,303)        | 3,291               | (47,409)        |
| Net realized (losses) on investments                                       | (811)  | (78)            |                     | (889)           |
| Net unrealized (losses) on investments                                     | (21,140)   | (1,974)         |                     | (23,114)        |
| Net foreign exchange (losses) gains  | (4,494)  | 6,653           | (51)                | 2,108           |
| <b>Net (loss) income</b>   | <b>(39,842)</b>  | <b>(32,702)</b> | <b>3,240</b>        | <b>(69,304)</b> |
|  | (594)  |                 |                     | (594)           |

Net income attributable to noncontrolling interest

**Net (loss) income (attributable) available to Validus**

|             |             |          |             |
|-------------|-------------|----------|-------------|
| \$ (40,436) | \$ (32,702) | \$ 3,240 | \$ (69,898) |
|-------------|-------------|----------|-------------|

(a) Notable losses for the three months ended June 30, 2011 include: Cat 46, Cat 48 and Jupiter 1. Notable losses for the three months ended June 30, 2010 include Deepwater Horizon, Aban Pearl, Bangkok riots and Perth hailstorm. Excludes the reserve for potential development on 2010 and 2011 notable loss events.

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(b) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income (loss) that is not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. A reconciliation of this measure to net income, the most comparable U.S. GAAP financial measure, is presented in the section below entitled Underwriting Income.

**Gross Premiums Written**

Gross premiums written for the three months ended June 30, 2011 were \$605.4 million compared to \$516.9 million for the three months ended June 30, 2010, an increase of \$88.5 million or 17.1%. Gross premiums written on the property lines increased by \$68.5 million, while the marine and specialty lines increased by \$4.9 million and \$15.2 million, respectively. Details of gross premiums written by line of business are provided below.

|                               | Three Months Ended<br>June 30, 2011 |                                     | Three Months Ended<br>June 30, 2010 |                                     | %<br>Change  |
|-------------------------------|-------------------------------------|-------------------------------------|-------------------------------------|-------------------------------------|--------------|
|                               | Gross<br>Premiums<br>Written        | Gross<br>Premiums<br>Written<br>(%) | Gross<br>Premiums<br>Written        | Gross<br>Premiums<br>Written<br>(%) |              |
| <b>(Dollars in thousands)</b> |                                     |                                     |                                     |                                     |              |
| Property                      | \$ 408,785                          | 67.5%                               | \$ 340,290                          | 65.8%                               | 20.1%        |
| Marine                        | 97,243                              | 16.1%                               | 92,380                              | 17.9%                               | 5.3%         |
| Specialty                     | 99,359                              | 16.4%                               | 84,191                              | 16.3%                               | 18.0%        |
| <b>Total</b>                  | <b>\$ 605,387</b>                   | <b>100.0%</b>                       | <b>\$ 516,861</b>                   | <b>100.0%</b>                       | <b>17.1%</b> |

*Validus Re.* Validus Re gross premiums written for the three months ended June 30, 2011 were \$341.7 million compared to \$284.3 million for the three months ended June 30, 2010, an increase of \$57.3 million or 20.2%. Details of Validus Re gross premiums written by line of business are provided below.

|                               | Three Months Ended<br>June 30, 2011 |                                     | Three Months Ended<br>June 30, 2010 |                                     | %<br>Change  |
|-------------------------------|-------------------------------------|-------------------------------------|-------------------------------------|-------------------------------------|--------------|
|                               | Gross<br>Premiums<br>Written        | Gross<br>Premiums<br>Written<br>(%) | Gross<br>Premiums<br>Written        | Gross<br>Premiums<br>Written<br>(%) |              |
| <b>(Dollars in thousands)</b> |                                     |                                     |                                     |                                     |              |
| Property                      | \$ 323,108                          | 94.6%                               | \$ 261,568                          | 92.0%                               | 23.5%        |
| Marine                        | 4,846                               | 1.4%                                | 15,410                              | 5.4%                                | (68.6)%      |
| Specialty                     | 13,697                              | 4.0%                                | 7,350                               | 2.6%                                | 86.4%        |
| <b>Total</b>                  | <b>\$ 341,651</b>                   | <b>100.0%</b>                       | <b>\$ 284,328</b>                   | <b>100.0%</b>                       | <b>20.2%</b> |

The increase in gross premiums written in the property lines of \$61.5 million was due primarily to \$42.6 million of gross premiums written by AlphaCat Re 2011 and a \$23.8 million increase in catastrophe excess of loss gross premiums written. The increase in catastrophe excess of loss premiums written was due primarily to an improving US property rate environment increasing premiums on existing business and providing attractive opportunities that resulted in growth. The decrease in gross premiums written of \$10.6 million in the marine lines was due primarily to a \$5.1 million decrease in estimated premium income adjustments and a \$5.8 million decrease in reinstatement premiums due to higher losses in 2010 attributable to the Deepwater Horizon loss. The increase in gross premiums written in the specialty lines of \$6.3 million was primarily due to a \$6.2 million increase in gross premiums written on a proportional basis.

Gross premiums written under the quota share, surplus treaty and excess of loss contracts between Validus Re and Talbot for three months ended June 30, 2011 decreased by \$8.0 million as compared to the three months ended June 30, 2010. The decrease in premiums written was due to a \$6.7 million decrease in the property lines and a \$1.3 million decrease in the marine lines. These reinsurance agreements with Talbot are eliminated upon consolidation.

*Talbot.* Talbot gross premiums written for the three months ended June 30, 2011 were \$276.9 million compared to \$253.7 million for the three months ended June 30, 2010, an increase of \$23.2 million or 9.1%. The \$276.9 million of gross premiums written translated at 2010 rates of exchange would have been \$273.9 million during the three months ended June 30, 2011, giving an effective increase of \$20.2 million or 8.0%. Details of Talbot gross premiums written by line of business are provided below.

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| (Dollars in thousands) | Three Months Ended<br>June 30, 2011 |                                     | Three Months Ended<br>June 30, 2010 |                                     | %<br>Change |
|------------------------|-------------------------------------|-------------------------------------|-------------------------------------|-------------------------------------|-------------|
|                        | Gross<br>Premiums<br>Written        | Gross<br>Premiums<br>Written<br>(%) | Gross<br>Premiums<br>Written        | Gross<br>Premiums<br>Written<br>(%) |             |
|                        |                                     |                                     |                                     |                                     |             |
| Property               | \$ 97,732                           | 35.3%                               | \$ 97,529                           | 38.4%                               | 0.2%        |
| Marine                 | 93,492                              | 33.8%                               | 79,355                              | 31.3%                               | 17.8%       |
| Specialty              | 85,662                              | 30.9%                               | 76,826                              | 30.3%                               | 11.5%       |
| <b>Total</b>           | <b>\$ 276,886</b>                   | <b>100.0%</b>                       | <b>\$ 253,710</b>                   | <b>100.0%</b>                       | <b>9.1%</b> |

The increase in gross premiums written in the marine lines of \$14.1 million was due primarily to a \$9.8 million increase in premiums written in the marine liability lines and a \$5.2 million increase in premiums written in the cargo lines. The increase in gross premiums written in the specialty lines of \$8.8 million was primarily due to a \$6.3 million increase in premiums written in the political violence lines.

**Reinsurance Premiums Ceded**

Reinsurance premiums ceded for the three months ended June 30, 2011 were \$132.3 million compared to \$67.7 million for the three months ended June 30, 2010, an increase of \$64.6 million or 95.4%. Details of reinsurance premiums ceded by line of business are provided below.

| (Dollars in thousands) | Three Months Ended<br>June 30, 2011 |   | Three Months Ended<br>June 30, 2010 |   | %<br>Change  |
|------------------------|-------------------------------------|---|-------------------------------------|---|--------------|
|                        | Reinsurance<br>Premiums<br>Ceded    | Reinsurance<br>Premiums<br>Ceded<br>(%) | Reinsurance<br>Premiums<br>Ceded    | Reinsurance<br>Premiums<br>Ceded<br>(%) |              |
|                        |                                     |   |                                     |   |              |
| Property               | \$ 112,299                          | 84.9%                                   | \$ 53,828                           | 79.5%                                   | 108.6%       |
| Marine                 | 16,034                              | 12.1%                                   | 10,923                              | 16.1%                                   | 46.8%        |
| Specialty              | 4,013                               | 3.0%                                    | 2,975                               | 4.4%                                    | 34.9%        |
| <b>Total</b>           | <b>\$ 132,346</b>                   | <b>100.0%</b>                           | <b>\$ 67,726</b>                    | <b>100.0%</b>                           | <b>95.4%</b> |

*Validus Re.* Validus Re reinsurance premiums ceded for the three months ended June 30, 2011 were \$98.2 million compared to \$41.2 million for the three months ended June 30, 2010, an increase of \$57.0 million or 138.5%. Details of Validus Re reinsurance premiums ceded by line of business are provided below.

| (Dollars in thousands) | Three Months Ended<br>June 30, 2011 |   | Three Months Ended<br>June 30, 2010 |   | %<br>Change   |
|------------------------|-------------------------------------|---|-------------------------------------|---|---------------|
|                        | Reinsurance<br>Premiums<br>Ceded    | Reinsurance<br>Premiums<br>Ceded<br>(%) | Reinsurance<br>Premiums<br>Ceded    | Reinsurance<br>Premiums<br>Ceded<br>(%) |               |
|                        |                                     |   |                                     |   |               |
| Property               | \$ 85,389                           | 86.9%                                   | \$ 33,933                           | 82.4%                                   | 151.6%        |
| Marine                 | 12,829                              | 13.1%                                   | 7,242                               | 17.6%                                   | 77.1%         |
| <b>Total</b>           | <b>\$ 98,218</b>                    | <b>100.0%</b>                           | <b>\$ 41,175</b>                    | <b>100.0%</b>                           | <b>138.5%</b> |

Reinsurance premiums ceded in the property lines increased by \$51.5 million, due primarily to the purchase of \$60.4 million of additional retrocessional coverage on the U.S. catastrophe portfolio, partially offset by a \$4.8 million decrease in non-proportional retrocessional coverage on the worldwide catastrophe portfolio. The additional U.S. retrocessional coverage was purchased to ensure that the Company would be well positioned to take advantage of opportunities in a post loss environment.

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Reinsurance premiums ceded in the marine lines increased by \$5.6 million, due primarily to \$5.1 million of additional retrocessional coverage purchased in the three months ended June 30, 2011.

*Talbot.* Talbot reinsurance premiums ceded for the three months ended June 30, 2011 were \$47.3 million compared to \$47.7 million for the three months ended June 30, 2010, a decrease of \$0.5 million or 0.9%. Details of Talbot reinsurance premiums ceded by line of business are provided below.

|                               | Three Months Ended<br>June 30, 2011 |                                      | Three Months Ended<br>June 30, 2010 |                                      | %<br>Change   |
|-------------------------------|-------------------------------------|--------------------------------------|-------------------------------------|--------------------------------------|---------------|
|                               | Reinsurance<br>Premiums<br>Ceded    | Reinsurance<br>Premiums<br>Ceded (%) | Reinsurance<br>Premiums<br>Ceded    | Reinsurance<br>Premiums<br>Ceded (%) |               |
| <b>(Dollars in thousands)</b> |                                     |                                      |                                     |                                      |               |
| Property                      | \$ 38,965                           | 82.4%                                | \$ 38,702                           | 81.1%                                | 0.7%          |
| Marine                        | 4,300                               | 9.1%                                 | 6,066                               | 12.7%                                | (29.1)%       |
| Specialty                     | 4,013                               | 8.5%                                 | 2,960                               | 6.2%                                 | 35.6%         |
| <b>Total</b>                  | <b>\$ 47,278</b>                    | <b>100.0%</b>                        | <b>\$ 47,728</b>                    | <b>100.0%</b>                        | <b>(0.9)%</b> |

Reinsurance premiums ceded across the property, marine and specialty lines are generally consistent with the three months ended June 30, 2010. There was a reduction in reinsurance premiums ceded to Validus Re, which is described above. This reduction was offset by an increase of \$7.6 million in reinsurance premiums ceded to third parties.

**Net Premiums Written**

Net premiums written for the three months ended June 30, 2011 were \$473.0 million compared to \$449.1 million for the three months ended June 30, 2010, an increase of \$23.9 million, or 5.3%. The ratios of net premiums written to gross premiums written for the three months ended June 30, 2011 and 2010 were 78.1% and 86.9%, respectively. Details of net premiums written by line of business are provided below.

|                               | Three Months Ended<br>June 30, 2011 |                                | Three Months Ended<br>June 30, 2010 |                                | %<br>Change |
|-------------------------------|-------------------------------------|--------------------------------|-------------------------------------|--------------------------------|-------------|
|                               | Net<br>Premiums<br>Written          | Net<br>Premiums<br>Written (%) | Net<br>Premiums<br>Written          | Net<br>Premiums<br>Written (%) |             |
| <b>(Dollars in thousands)</b> |                                     |                                |                                     |                                |             |
| Property                      | \$ 296,486                          | 62.7%                          | \$ 286,463                          | 63.8%                          | 3.5%        |
| Marine                        | 81,209                              | 17.2%                          | 81,455                              | 18.1%                          | (0.3)%      |
| Specialty                     | 95,346                              | 20.1%                          | 81,217                              | 18.1%                          | 17.4%       |
| <b>Total</b>                  | <b>\$ 473,041</b>                   | <b>100.0%</b>                  | <b>\$ 449,135</b>                   | <b>100.0%</b>                  | <b>5.3%</b> |

*Validus Re.* Validus Re net premiums written for the three months ended June 30, 2011 were \$243.4 million compared to \$243.2 million for the three months ended June 30, 2010, an increase of \$0.3 million or 0.1%. Details of Validus Re net premiums written by line of business are provided below.

|                               | Three Months Ended<br>June 30, 2011 |                            | Three Months Ended<br>June 30, 2010 |                            |
|-------------------------------|-------------------------------------|----------------------------|-------------------------------------|----------------------------|
|                               | Net<br>Premiums<br>Written          | Net<br>Premiums<br>Written | Net<br>Premiums<br>Written          | Net<br>Premiums<br>Written |
| <b>(Dollars in thousands)</b> |                                     |                            |                                     |                            |

|              |            | <b>Written</b><br><b>(%)</b> |            | <b>Written</b><br><b>(%)</b> | <b>%</b><br><b>Change</b> |
|--------------|------------|------------------------------|------------|------------------------------|---------------------------|
| Property     | \$ 237,719 | 97.7%                        | \$ 227,635 | 93.6%                        | 4.4%                      |
| Marine       | (7,983)    | (3.3)%                       | 8,168      | 3.4%                         | (197.7)%                  |
| Specialty    | 13,697     | 5.6%                         | 7,350      | 3.0%                         | 86.4%                     |
| <b>Total</b> | \$ 243,433 | 100.0%                       | \$ 243,153 | 100.0%                       | 0.1%                      |



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The increase in Validus Re net premiums written was driven by the factors highlighted above in respect of gross premiums written and reinsurance premiums ceded. Negative net written premiums in the marine lines is the result of premium adjustments on gross premiums written and the timing of purchases of retrocessional coverage. The ratios of net premiums written to gross premiums written were 71.3% and 85.5% for the three months ended June 30, 2011 and 2010, respectively, reflecting the increase in reinsurance premiums ceded as a result of the purchase of additional retrocessional coverage described above.

*Talbot.* Talbot net premiums written for the three months ended June 30, 2011 were \$229.6 million compared to \$206.0 million for the three months ended June 30, 2010, an increase of \$23.6 million or 11.5%. Details of Talbot net premiums written by line of business are provided below.

|                               | Three Months Ended<br>June 30, 2011 |                                   | Three Months Ended<br>June 30, 2010 |                                   | %<br>Change  |
|-------------------------------|-------------------------------------|-----------------------------------|-------------------------------------|-----------------------------------|--------------|
|                               | Net<br>Premiums<br>Written          | Net<br>Premiums<br>Written<br>(%) | Net<br>Premiums<br>Written          | Net<br>Premiums<br>Written<br>(%) |              |
| <b>(Dollars in thousands)</b> |                                     |                                   |                                     |                                   |              |
| Property                      | \$ 58,767                           | 25.6%                             | \$ 58,827                           | 28.5%                             | (0.1)%       |
| Marine                        | 89,192                              | 38.8%                             | 73,289                              | 35.6%                             | 21.7%        |
| Specialty                     | 81,649                              | 35.6%                             | 73,866                              | 35.9%                             | 10.5%        |
| <b>Total</b>                  | <b>\$ 229,608</b>                   | <b>100.0%</b>                     | <b>\$ 205,982</b>                   | <b>100.0%</b>                     | <b>11.5%</b> |

The increase in net premiums written was driven by the factors highlighted above in respect of gross premiums written and reinsurance premiums ceded. The ratios of net premiums written to gross premiums written for the three months ended June 30, 2011 and 2010 were 82.9% and 81.2%, respectively.

**Change in Unearned Premiums**

Net change in unearned premiums for the three months ended June 30, 2011 was (\$47.4) million compared to (\$11.2) million for the three months ended June 30, 2010, a change of \$36.2 million or 323.6%.

|                                       | Three Months<br>Ended<br>June 30, 2011 | Three Months<br>Ended<br>June 30, 2010 | %<br>Change   |
|---------------------------------------|--|--|---------------|
|                                       | Change in<br>Unearned<br>Premiums      | Change in<br>Unearned<br>Premiums      |               |
| <b>(Dollars in thousands)</b>         |  |  |               |
| Change in gross unearned premium      | \$ (109,608)                           | \$ (93,012)                            | 17.8%         |
| Change in prepaid reinsurance premium | 62,207                                 | 81,821                                 | (24.0)%       |
| <b>Net change in unearned premium</b> | <b>\$ (47,401)</b>                     | <b>\$ (11,191)</b>                     | <b>323.6%</b> |

*Validus Re.* Validus Re's net change in unearned premiums for the three months ended June 30, 2011 were (\$10.8) million compared to \$18.9 million for the three months ended June 30, 2010, a change of \$29.6 million or 156.9%.

| Three Months<br>Ended<br>June 30, 2011 | Three Months<br>Ended<br>June 30, 2010 |
|--|--|
| Change in<br>Unearned                  | Change in<br>Unearned                  |

| <b>(Dollars in thousands)</b>         |                    |                  | <b>%</b>        |
|---------------------------------------|--------------------|------------------|-----------------|
|                                       | <b>Premiums</b>    | <b>Premiums</b>  | <b>Change</b>   |
| Change in gross unearned premium      | \$ (83,079)        | \$ (75,680)      | 9.8%            |
| Change in prepaid reinsurance premium | 72,324             | 94,568           | (23.5)%         |
| <b>Net change in unearned premium</b> | <b>\$ (10,755)</b> | <b>\$ 18,888</b> | <b>(156.9)%</b> |

The Validus Re net change in unearned premium has decreased for the three months ended June 30, 2011 due primarily to the timing differences in purchases of retrocessional coverage during the three months ended June 30, 2011 compared to the three months ended June 30, 2010.

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*Talbot.* The Talbot net change in unearned premiums for the three months ended June 30, 2011 was (\$36.6) million compared to (\$30.1) million for the three months ended June 30, 2010, a change of \$6.6 million or 21.8%.

|                                       | Three Months Ended<br>June 30, 2011 |                       | Three Months Ended<br>June 30, 2010 |                       | %<br>Change |
|---------------------------------------|-------------------------------------|-----------------------|-------------------------------------|-----------------------|-------------|
|                                       | Premiums                            | Change in<br>Unearned | Premiums                            | Change in<br>Unearned |             |
| <b>(Dollars in thousands)</b>         |                                     |                       |                                     |                       |             |
| Change in gross unearned premium      | \$                                  | (26,529)              | \$                                  | (17,332)              | 53.1%       |
| Change in prepaid reinsurance premium |                                     | (10,117)              |                                     | (12,747)              | (20.6)%     |
| <b>Net change in unearned premium</b> | \$                                  | (36,646)              | \$                                  | (30,079)              | 21.8%       |

The Talbot net change in unearned premium is generally consistent for the three months ended June 30, 2011 compared to the three months ended June 30, 2010.

**Net Premiums Earned**

Net premiums earned for the three months ended June 30, 2011 were \$425.6 million compared to \$437.9 million for the three months ended June 30, 2010, a decrease of \$12.3 million or 2.8%. The decrease in net premiums earned was driven by a decrease in net premiums earned of \$29.4 million in the Validus Re segment, partially offset by an increase of \$17.1 million in the Talbot segment. Details of net premiums earned by line of business are provided below.

|                               | Three Months Ended<br>June 30, 2011 |                                  | Three Months Ended<br>June 30, 2010 |                                  | %<br>Change |
|-------------------------------|-------------------------------------|----------------------------------|-------------------------------------|----------------------------------|-------------|
|                               | Net<br>Premiums<br>Earned           | Net<br>Premiums<br>Earned<br>(%) | Net<br>Premiums<br>Earned           | Net<br>Premiums<br>Earned<br>(%) |             |
| <b>(Dollars in thousands)</b> |                                     |                                  |                                     |                                  |             |
| Property                      | \$ 204,624                          | 48.1%                            | \$ 223,596                          | 51.0%                            | (8.5)%      |
| Marine                        | 125,496                             | 29.5%                            | 111,567                             | 25.5%                            | 12.5%       |
| Specialty                     | 95,520                              | 22.4%                            | 102,781                             | 23.5%                            | (7.1)%      |
| <b>Total</b>                  | \$ 425,640                          | 100.0%                           | \$ 437,944                          | 100.0%                           | (2.8)%      |

*Validus Re.* Validus Re net premiums earned for the three months ended June 30, 2011 were \$232.7 million compared to \$262.0 million for the three months ended June 30, 2010, a decrease of \$29.4 million or 11.2%. Details of Validus Re net premiums earned by line of business are provided below.

|                               | Three Months Ended<br>June 30, 2011 |                                  | Three Months Ended<br>June 30, 2010 |                                  | %<br>Change |
|-------------------------------|-------------------------------------|----------------------------------|-------------------------------------|----------------------------------|-------------|
|                               | Net<br>Premiums<br>Earned           | Net<br>Premiums<br>Earned<br>(%) | Net<br>Premiums<br>Earned           | Net<br>Premiums<br>Earned<br>(%) |             |
| <b>(Dollars in thousands)</b> |                                     |                                  |                                     |                                  |             |
| Property                      | \$ 166,779                          | 71.7%                            | \$ 186,444                          | 71.1%                            | (10.5)%     |
| Marine                        | 46,549                              | 20.0%                            | 48,154                              | 18.4%                            | (3.3)%      |
| Specialty                     | 19,350                              | 8.3%                             | 27,443                              | 10.5%                            | (29.5)%     |

|              |            |        |            |        |         |
|--------------|------------|--------|------------|--------|---------|
| <b>Total</b> | \$ 232,678 | 100.0% | \$ 262,041 | 100.0% | (11.2)% |
|--------------|------------|--------|------------|--------|---------|

The decrease in net premiums earned is consistent with the relevant patterns of net written premiums influencing the earned premiums for the three months ended June 30, 2011 compared to the three months ended June 30, 2010. *Talbot*. Talbot net premiums earned for the three months ended June 30, 2011 were \$193.0 million compared to \$175.9 million for the three months ended June 30, 2010, an increase of \$17.1 million or 9.7%. Details of Talbot net premiums earned by line of business are provided below.

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|                               | Three Months Ended<br>June 30, 2011 |                                  | Three Months Ended<br>June 30, 2010 |                                  | %<br>Change |
|-------------------------------|-------------------------------------|----------------------------------|-------------------------------------|----------------------------------|-------------|
|                               | Net<br>Premiums<br>Earned           | Net<br>Premiums<br>Earned<br>(%) | Net<br>Premiums<br>Earned           | Net<br>Premiums<br>Earned<br>(%) |             |
| <b>(Dollars in thousands)</b> |                                     |                                  |                                     |                                  |             |
| Property                      | \$ 37,845                           | 19.6%                            | \$ 37,152                           | 21.1%                            | 1.9%        |
| Marine                        | 78,947                              | 40.9%                            | 63,413                              | 36.1%                            | 24.5%       |
| Specialty                     | 76,170                              | 39.5%                            | 75,338                              | 42.8%                            | 1.1%        |
| <b>Total</b>                  | <b>\$ 192,962</b>                   | <b>100.0%</b>                    | <b>\$ 175,903</b>                   | <b>100.0%</b>                    | <b>9.7%</b> |

The increase in net premiums earned is consistent with the relevant patterns of net written premiums influencing the earned premium for the three months ended June 30, 2011, as compared to the three months ended June 30, 2010, as discussed above.

**Losses and Loss Expenses**

Losses and loss expenses for the three months ended June 30, 2011 were \$207.3 million compared to \$194.9 million for the three months ended June 30, 2010, an increase of \$12.4 million or 6.4%. The loss ratios, defined as losses and loss expenses divided by net premiums earned, for the three months ended June 30, 2011 and 2010 were 48.7% and 44.5%, respectively. Details of loss ratios by line of business are provided below.

|                  | Three Months<br>Ended | Three Months<br>Ended | Percentage<br>Point<br>Change |
|------------------|-----------------------|-----------------------|-------------------------------|
|                  | June 30, 2011         | June 30, 2010         |                               |
| Property         | 52.8%                 | 31.3%                 | 21.5                          |
| Marine           | 59.5%                 | 76.0%                 | (16.5)                        |
| Specialty        | 25.8%                 | 38.9%                 | (13.1)                        |
| <b>All lines</b> | <b>48.7%</b>          | <b>44.5%</b>          | <b>4.2</b>                    |

For the three months ended June 30, 2011, the Company incurred \$90.3 million from notable loss events, which represented 21.2 percentage points of the loss ratio as described below. Net of \$6.9 million of reinstatement premiums, the effect of these events on net income was \$83.4 million. For the three months ended June 30, 2010, the Company incurred \$70.5 million from notable loss events, which represented 16.1 percentage points of the loss ratio, excluding reserve for development on notable loss events, as described below. Net of \$3.3 million of reinstatement premiums, the effect of these events on net income was \$67.2 million. The Company's loss ratio, excluding prior year development and notable loss events for the three months ended June 30, 2011 and 2010 was 33.5% and 39.7%, respectively.

| Second Quarter 2011 Notable Loss Events (a) | Three months ended June 30, 2011<br>(Dollars in thousands) |                  |   |             |   |             |
|---|--|------------------|---|-------------|---|-------------|
|   | Validus Re   |                  | Talbot  |             | Total   |             |
| Description                                 | Net<br>Losses<br>and<br>Loss<br>Expenses<br>(b)            | % of<br>NPE      | Net<br>Losses<br>and<br>Loss<br>Expenses<br>(b) | % of<br>NPE | Net<br>Losses<br>and<br>Loss<br>Expenses<br>(b) | % of<br>NPE |
|   | Cat 46   | Tornado\$ 36,584 | 15.7%   | \$ 7,222    | 3.7%  | \$ 43,806   |

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|              |          |           |       |           |       |           |       |
|--------------|----------|-----------|-------|-----------|-------|-----------|-------|
| Cat 48       | Tornado  | 20,869    | 9.0%  | 10,612    | 5.5%  | 31,481    | 7.4%  |
|              | Platform |           |       |           |       |           |       |
| Jupiter 1    | failure  | 4,970     | 2.1%  | 10,038    | 5.2%  | 15,008    | 3.5%  |
| <b>Total</b> |          | \$ 62,423 | 26.8% | \$ 27,872 | 14.4% | \$ 90,295 | 21.2% |

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| <b>Three months ended June 30, 2010</b><br><b>(Dollars in thousands)</b> |                   |              |                  |             |                  |              |
|--|-------------------|--------------|------------------|-------------|------------------|--------------|
| <b>Second Quarter 2010 Notable Loss Events (a)</b>                       | <b>Validus Re</b> |              | <b>Talbot</b>    |             | <b>Total</b>     |              |
| <b>Description</b>   | <b>Net</b>        |              | <b>Net</b>       |             | <b>Net</b>       |              |
|  | <b>Losses</b>     |              | <b>Losses</b>    |             | <b>Losses</b>    |              |
|  | <b>and</b>        |              | <b>and</b>       |             | <b>and</b>       |              |
|  | <b>Loss</b>       |              | <b>Loss</b>      |             | <b>Loss</b>      |              |
|  | <b>Expenses</b>   | <b>% of</b>  | <b>Expenses</b>  | <b>% of</b> | <b>Expenses</b>  | <b>% of</b>  |
|  | <b>(b)</b>        | <b>NPE</b>   | <b>(b)</b>       | <b>NPE</b>  | <b>(b)</b>       | <b>NPE</b>   |
| Oil rig and Deepwater Horizon  | \$ 33,681         | 12.9%        | \$ 10,420        | 5.9%        | \$ 44,101        | 10.1%        |
| Aban Pearl   | 10,000            | 3.8%         | 500              | 0.3%        | 10,500           | 2.4%         |
| Bangkok riots  | 7,500             | 2.9%         |                  |             | 7,500            | 1.7%         |
| Perth hailstorm  | 8,390             | 3.1%         |                  |             | 8,390            | 1.9%         |
| <b>Total</b>   | <b>\$ 59,571</b>  | <b>22.7%</b> | <b>\$ 10,920</b> | <b>6.2%</b> | <b>\$ 70,491</b> | <b>16.1%</b> |

- (a) These notable loss event amounts exclude the reserve for potential development on 2010 and 2011 notable loss events and are based on management's estimates following a review of the Company's potential exposure and discussions with certain clients and brokers. Given the magnitude and recent occurrence of these events, and other uncertainties inherent in loss estimation, meaningful uncertainty remains regarding losses from these events and the Company's actual ultimate net losses from these events may vary materially from these estimates.
- (b) Net of reinsurance but not net of reinstatement premiums. Total reinstatement premiums were \$6.9 million for the three months ended June 30, 2011 and \$3.3 million for the three months ended June 30, 2010.

|           |                                |                          | <b>Three Months Ended June 30,</b> |             |                   |
|-----------|--------------------------------|--------------------------|------------------------------------|-------------|-------------------|
|           |                                |                          |                                    |             | <b>Percentage</b> |
|           |                                |                          |                                    |             | <b>Point</b>      |
|           |                                |                          |                                    |             | <b>Change</b>     |
|           |                                |                          | <b>2011</b>                        | <b>2010</b> |                   |
| Property  | current period                 | excluding notable losses | 21.9%                              | 38.0%       | (16.1)            |
| Property  | current period                 | notable losses           | 33.7%                              | 3.8%        | 29.9              |
| Property  | change in prior accident years |                          | (2.8)%                             | (10.5)%     | 7.7               |
| Property  | loss ratio                     |                          | 52.8%                              | 31.3%       | 21.5              |
| Marine    | current period                 | excluding notable losses | 50.9%                              | 40.1%       | 10.8              |
| Marine    | current period                 | notable losses           | 16.5%                              | 48.9%       | (32.4)            |
| Marine    | change in prior accident years |                          | (7.9)%                             | (13.0)%     | 5.1               |
| Marine    | loss ratio                     |                          | 59.5%                              | 76.0%       | (16.5)            |
| Specialty | current period                 | excluding notable losses | 35.8%                              | 43.0%       | (7.2)             |
| Specialty | current period                 | notable losses           | 0.6%                               | 7.3%        | (6.7)             |

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|                  |   |         |         |        |
|------------------|---|---------|---------|--------|
| Specialty        | change in prior accident years          | (10.6)% | (11.3)% | 0.7    |
| Specialty        | loss ratio                              | 25.8%   | 38.9%   | (13.2) |
| All lines        | current period excluding notable losses | 33.5%   | 39.7%   | (6.2)  |
| All lines        | current period notable losses           | 21.2%   | 16.1%   | 5.1    |
| All lines        | change in prior accident years          | (6.0)%  | (11.3)% | 5.3    |
| <b>All lines</b> | <b>loss ratio</b>                       | 48.7%   | 44.5%   | 4.2    |

*Validus Re.* Validus Re losses and loss expenses for the three months ended June 30, 2011 were \$94.0 million compared to \$123.8 million for the three months ended June 30, 2010, a decrease of \$29.8 million or 24.0%. The loss ratio, defined as losses and loss expenses divided by net premiums earned, was 40.4% and 47.2% for the three months ended June 30, 2011 and 2010, respectively. For the three months ended June 30, 2011, favorable loss development on prior years totaled \$12.3 million and benefited the Validus Re loss ratio by 5.3 percentage points. For the three months ended June 30, 2010, favorable loss development on prior years totaled \$17.9 million and benefited the Validus Re loss ratio by 6.9 percentage points.



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For the three months ended June 30, 2011, Validus Re incurred notable loss events as identified above of \$62.4 million, which represented 26.8 percentage points of the loss ratio. Net of reinstatement premiums of \$6.3 million, the effect of these events on Validus Re segment income was \$56.1 million. For the three months ended June 30, 2010, Validus Re incurred notable loss events as identified above of \$59.6 million, which represented 22.7 percentage points of the loss ratio, excluding the reserve for potential development on notable loss events. Net of reinstatement premiums of \$7.7 million, the effect of these events on Validus Re segment income was \$51.9 million. Validus Re segment loss ratios, excluding prior year development and notable loss events identified above, for the three months ended June 30, 2011 and 2010 were 18.9% and 31.4%, respectively. Details of loss ratios by line of business and period of occurrence are provided below.

|                  |   | <b>Three Months Ended June 30,</b> |              |              |
|------------------|---|------------------------------------|--------------|--------------|
|                  |   | <b>Percentage</b>                  |              |              |
|                  |   | <b>Point</b>                       |              |              |
|                  |   | <b>Change</b>                      |              |              |
|                  |   | <b>2011</b>                        | <b>2010</b>  |              |
| Property         | current period excluding notable losses | 13.4%                              | 36.1%        | (22.7)       |
| Property         | current period notable losses           | 34.4%                              | 4.5%         | 29.9         |
| Property         | change in prior accident years          | (3.9)%                             | (7.3)%       | 3.4          |
| Property         | loss ratio                              | 43.9%                              | 33.3%        | 10.6         |
| Marine           | current period excluding notable losses | 41.7%                              | 26.8%        | 14.9         |
| Marine           | current period notable losses           | 10.7%                              | 90.7%        | (80.0)       |
| Marine           | change in prior accident years          | (9.7)%                             | (7.5)%       | (2.2)        |
| Marine           | loss ratio                              | 42.7%                              | 110.0%       | (67.3)       |
| Specialty        | current period excluding notable losses | 11.3%                              | 7.0%         | 4.3          |
| Specialty        | current period notable losses           | 0.0%                               | 27.3%        | (27.3)       |
| Specialty        | change in prior accident years          | (6.6)%                             | (2.3)%       | (4.3)        |
| Specialty        | loss ratio                              | 4.7%                               | 32.0%        | (27.3)       |
| All lines        | current period excluding notable losses | 18.9%                              | 31.4%        | (12.5)       |
| All lines        | current period notable losses           | 26.8%                              | 22.7%        | 4.1          |
| All lines        | change in prior accident years          | (5.3)%                             | (6.9)%       | 1.6          |
| <b>All lines</b> | <b>loss ratio</b>                       | <b>40.4%</b>                       | <b>47.2%</b> | <b>(6.8)</b> |

For the three months ended June 30, 2011, Validus Re property lines losses and loss expenses include \$79.8 million related to current year losses and \$6.5 million of favorable development relating to prior accident years. This favorable development is attributable to lower than expected claims development. For the three months ended June 30, 2010, Validus Re property lines losses and loss expenses included \$75.7 million related to current year losses and \$13.6 million of favorable development relating to prior accident years. This favorable development is attributable to reduced loss estimates for the U.K. flood loss and windstorm Kyrill, as well as lower than expected claim development elsewhere.

For the three months ended June 30, 2011, Validus Re's property lines incurred \$57.4 million of notable losses, which represented 34.4 percentage points of the property lines loss ratio. For the three months ended June 30, 2010, Validus Re's property lines incurred \$8.4 million of notable losses, which represented 4.5 percentage points of the property lines loss ratio, excluding reserve for potential development on notable loss events. Validus Re property lines loss ratios, excluding prior year development and notable loss events identified above, for the three months ended

June 30, 2011 and 2010 were 13.4% and 36.1%, respectively.

For the three months ended June 30, 2011, Validus Re marine lines losses and loss expenses include \$24.4 million related to current year losses and \$4.5 million of favorable development relating to prior accident years. For the three months ended June 30, 2010, Validus Re marine lines losses and loss expenses included \$56.6 million related to current year losses and \$3.7 million of favorable development relating to prior accident years.

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For the three months ended June 30, 2011, Validus Re s marine lines incurred \$5.0 million of notable losses which represented 10.7 percentage points of the marine lines loss ratio. For the three months ended June 30, 2010, Validus Re s marine lines incurred \$43.7 million of notable losses, which represented 90.7 percentage points of the marine lines loss ratio, excluding the reserve for potential development on notable loss events. Validus Re marine lines loss ratios, excluding prior year development and notable loss events identified above, for the three months ended June 30, 2011 and 2010 were 41.7% and 26.8%, respectively.

For the three months ended June 30, 2011, Validus Re specialty lines losses and loss expenses include \$2.1 million related to current year losses and \$1.3 million of favorable development relating to prior accident years. For the three months ended June 30, 2010, Validus Re specialty lines losses and loss expenses included \$9.4 million related to current year losses and \$0.6 million of favorable development relating to prior accident years.

For the three months ended June 30, 2011, Validus Re s specialty lines did not incur any notable losses. For the three months ended June 30, 2010, Validus Re s specialty lines incurred \$7.5 million of notable losses, which represented 27.3 percentage points of the specialty lines loss ratio. Validus Re specialty lines loss ratios, excluding prior year development, for the three months ended June 30, 2011 and 2010 were 11.3% and 7.0%, respectively. *Talbot*. Talbot losses and loss expenses for the three months ended June 30, 2011 were \$113.3 million compared to \$71.1 million for the three months ended June 30, 2010, an increase of \$42.2 million or 59.3%. The Talbot loss ratio was 58.7% and 40.4% for the three months ended June 30, 2011 and 2010, respectively. For the three months ended June 30, 2011, Talbot incurred losses of \$126.7 million related to current year losses and \$13.4 million in favorable development relating to prior accident years. For the three months ended June 30, 2010, Talbot incurred losses of \$102.8 million related to current year losses and \$31.7 million in favorable development relating to prior accident years.

For the three months ended June 30, 2011, Talbot incurred \$27.9 million of notable losses, which represented 14.4 percentage points of the loss ratio. Net of reinstatement premiums of \$0.7 million, the effect of these events on Talbot segment income is \$27.2 million. For the three months ended June 30, 2010, Talbot incurred \$10.9 million of notable losses, which represented 6.2 percentage points of the Talbot loss ratio. Net of reinstatement premiums of (\$4.4) million, the effect of these events on Talbot segment income was \$15.3 million. Talbot loss ratios, excluding prior year loss development and notable loss events identified above, for the three months ended June 30, 2011 and 2010 were 51.2% and 52.2%, respectively. Details of loss ratios by line of business and period of occurrence are provided below.

|           |   | <b>Three Months Ended June 30,</b> |             |                   |
|-----------|---|------------------------------------|-------------|-------------------|
|           |   |                                    |             | <b>Percentage</b> |
|           |   |                                    |             | <b>Point</b>      |
|           |   |                                    |             | <b>Change</b>     |
|           |   | <b>2011</b>                        | <b>2010</b> |                   |
| Property  | current period excluding notable losses | 58.9%                              | 48.0%       | 10.9              |
| Property  | current period notable losses           | 30.5%                              | 0.0%        | 30.5              |
| Property  | change in prior accident years          | 2.3%                               | (26.5)%     | 28.8              |
| Property  | loss ratio                              | 91.7%                              | 21.5%       | 70.2              |
| Marine    | current period excluding notable losses | 56.3%                              | 50.1%       | 6.2               |
| Marine    | current period notable losses           | 20.0%                              | 17.2%       | 2.8               |
| Marine    | change in prior accident years          | (6.8)%                             | (17.0)%     | 10.2              |
| Marine    | loss ratio                              | 69.5%                              | 50.3%       | 19.2              |
| Specialty | current period excluding notable losses | 42.0%                              | 56.1%       | (14.1)            |
| Specialty | current period notable losses           | 0.7%                               | 0.0%        | 0.7               |
| Specialty | change in prior accident years          | (11.6)%                            | (14.7)%     | 3.1               |

|                  |   |              |              |             |
|------------------|---|--------------|--------------|-------------|
| Specialty        | loss ratio                              | 31.1%        | 41.4%        | (10.3)      |
| All lines        | current period excluding notable losses | 51.2%        | 52.2%        | (1.0)       |
| All lines        | current period notable losses           | 14.4%        | 6.2%         | 8.2         |
| All lines        | change in prior accident years          | (6.9)%       | (18.0)%      | 11.1        |
| <b>All lines</b> | <b>loss ratio</b>                       | <b>58.7%</b> | <b>40.4%</b> | <b>18.3</b> |

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For the three months ended June 30, 2011, Talbot property lines losses and loss expenses include \$33.8 million related to current year losses and \$0.9 million of adverse development relating to prior accident years. The prior year adverse development is attributable to higher than expected claims development on the onshore energy lines, largely offset by lower than expected claims on the property treaty and property facultative lines. For the three months ended June 30, 2010, Talbot property lines losses and loss expenses included \$17.8 million related to current year losses and \$9.8 million of favorable development relating to prior accident years. The prior year favorable development was attributable to lower than expected claim development on the property facultative and binder accounts, together with favorable development on hurricanes Katrina and Ike.

For the three months ended June 30, 2011, Talbot's property lines incurred \$11.5 million of notable losses, which represented 30.5 percentage points of the property lines loss ratio. For the three months ended June 30, 2010, Talbot's property lines did not incur any notable losses. Talbot property line loss ratio, excluding prior year development and notable loss events identified above for the three months ended June 30, 2011 and 2010 were 58.9% and 48.0%, respectively.

For the three months ended June 30, 2011, Talbot marine lines losses and loss expenses include \$60.3 million related to current year losses and \$5.4 million of favorable development relating to prior accident years. The prior year favorable development is due primarily to lower than expected claims development across most lines of business, partially offset by adverse claims development on the offshore energy lines. For the three months ended June 30, 2010, Talbot marine lines losses and loss expenses included \$42.7 million related to current year losses and \$10.8 million of favorable development relating to prior accident years. The prior year favorable development was primarily due to lower than expected loss development on the Hull lines.

For the three months ended June 30, 2011, Talbot's marine lines incurred \$15.8 million of notable losses, which represented 20.0 percentage points of the marine lines loss ratio. For the three months ended June 30, 2010, Talbot's marine lines incurred \$10.9 million of notable losses, which represented 17.2 percentage points of the marine lines loss ratio. Talbot marine lines loss ratios, excluding prior year development and notable loss events identified above, for the three months ended June 30, 2011 and 2010 were 56.3% and 50.1%, respectively.

For the three months ended June 30, 2011, Talbot specialty lines losses and loss expenses include \$32.6 million relating to current year losses and \$8.9 million of favorable development relating to prior accident years. The prior year favorable development is due primarily to lower than expected claims development across most lines of business, partially offset by adverse claims development on the financial institutions lines. For the three months ended June 30, 2010, Talbot specialty lines losses and loss expenses included \$42.3 million relating to current year losses and \$11.0 million of favorable development relating to prior accident years. The prior year favorable development was primarily due to lower than expected claims across most specialty sub classes.

For the three months ended June 30, 2011, Talbot's specialty lines incurred \$0.6 million of notable losses, which represented 0.7 percentage points of the specialty lines loss ratio. For the three months ended June 30, 2010, Talbot's specialty lines did not incur any notable losses. Talbot specialty lines loss ratios, excluding prior year development and notable loss events identified above for the three months ended June 30, 2011 and 2010 were 42.0% and 56.1%, respectively.

At June 30, 2011 and 2010, gross and net reserves for losses and loss expenses were estimated using the methodology as outlined in the critical accounting policies and estimates as discussed in Item 7, Management's Discussion and Analysis of Results of Operations and Financial Condition in the Company's Annual Report on Form 10-K for the year ended December 31, 2010. The Company did not make any significant changes in the assumptions or methodology used in its reserving process for the three months ended June 30, 2011.

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| <b>(Dollars in thousands)</b> | <b>As at June 30, 2011</b> |                     |   |
|-------------------------------|----------------------------|---------------------|---|
|                               | <b>Gross Case Reserves</b> | <b>Gross IBNR</b>   | <b>Total Gross Reserve for Losses and Loss Expenses</b> |
| Property                      | \$ 757,858                 | \$ 556,685          | \$ 1,314,543  |
| Marine                        | 404,886                    | 372,778             | 777,664   |
| Specialty                     | 236,659                    | 291,494             | 528,153   |
| <b>Total</b>                  | <b>\$ 1,399,403</b>        | <b>\$ 1,220,957</b> | <b>\$ 2,620,360</b>                                     |

| <b>(Dollars in thousands)</b> | <b>As at June 30, 2011</b> |                     |   |
|-------------------------------|----------------------------|---------------------|---|
|                               | <b>Net Case Reserves</b>   | <b>Net IBNR</b>     | <b>Total Net Reserve for Losses and Loss Expenses</b> |
| Property                      | \$ 544,165                 | \$ 522,391          | \$ 1,066,556  |
| Marine                        | 328,987                    | 356,046             | 685,033   |
| Specialty                     | 184,767                    | 244,199             | 428,966   |
| <b>Total</b>                  | <b>\$ 1,057,919</b>        | <b>\$ 1,122,636</b> | <b>\$ 2,180,555</b>                                   |

The following table sets forth a reconciliation of gross and net reserves for losses and loss expenses by segment for the three months ended June 30, 2011:

| <b>(Dollars in thousands)</b>      | <b>Three Months Ended June 30, 2011</b> |               |                     |              |
|------------------------------------|---|---------------|---------------------|--------------|
|                                    | <b>Validus Re</b>                       | <b>Talbot</b> | <b>Eliminations</b> | <b>Total</b> |
| Gross reserves at period beginning | \$ 1,340,418                            | \$ 1,324,967  | \$ (130,970)        | \$ 2,534,415 |
| Losses recoverable                 | (216,300)                               | (368,371)     | 130,970             | (453,701)    |
| Net reserves at period beginning   | 1,124,118                               | 956,596       |                     | 2,080,714    |
| Incurred losses- current year      | 106,347                                 | 126,665       |                     | 233,012      |
| Change in prior accident years     | (12,312)                                | (13,393)      |                     | (25,705)     |
| Incurred losses                    | 94,035                                  | 113,272       |                     | 207,307      |
| Foreign exchange                   | 14,050                                  | (470)         |                     | 13,580       |
| Paid losses                        | (38,070)                                | (82,976)      |                     | (121,046)    |
| Net reserves at period end         | 1,194,133                               | 986,422       |                     | 2,180,555    |
| Losses recoverable                 | 182,306                                 | 384,268       | (126,769)           | 439,805      |

|                              |              |              |              |              |
|------------------------------|--------------|--------------|--------------|--------------|
| Gross reserves at period end | \$ 1,376,439 | \$ 1,370,690 | \$ (126,769) | \$ 2,620,360 |
|------------------------------|--------------|--------------|--------------|--------------|

The amount of recorded reserves represents management's best estimate of expected losses and loss expenses on premiums earned. For the three months ended June 30, 2011, favorable loss reserve development on prior years totaled \$25.7 million. Of this \$12.3 million of the favorable loss reserve development related to the Validus Re segment and \$13.4 million related to the Talbot segment. Favorable loss reserve development benefited the Company's loss ratio by 6.0 percentage points for the three months ended June 30, 2011. For the three months ended June 30, 2010, favorable loss reserve development on prior years totaled \$49.6 million. Of this \$17.9 million related to the Validus Re segment and \$31.7 million related to the Talbot segment. Favorable loss reserve development benefited the Company's loss ratio by 11.3 percentage points for the three months ended June 30, 2010.

Management of insurance and reinsurance companies use significant judgment in the estimation of reserves for losses and loss expenses. Given the magnitude of recent loss events and other uncertainties inherent in loss estimation, meaningful uncertainty remains regarding the estimation for recent notable loss events. The Company's actual ultimate net loss may vary materially from these estimates. Validus Re ultimate losses for notable loss events are estimated through detailed review of contracts which are identified by the Company as potentially exposed to the specific notable loss event.

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However, there can be no assurance that the ultimate loss amount estimated for a specific contract will be accurate, or that all contracts with exposure to a specific notable loss event will be identified in a timely manner. Potential losses in excess of the estimated ultimate loss assigned to a contract on the basis of a specific review, or loss amounts from contracts not specifically included in the detailed review are reserved for in the reserve for potential development on notable loss events. As at March 31, 2011, the total reserve for development on both 2010 and 2011 events was \$83.4 million. During the three months ended June 30, 2011 \$8.9 million, \$20.1 million and \$20.2 million of the reserve for potential development on 2010 and 2011 notable loss events was allocated to the Deepwater Horizon loss, the Tohoku earthquake and the Christchurch earthquake, respectively. Therefore as at June 30, 2011 the total reserve for potential development on both 2010 and 2011 events was \$34.2 million.

**Policy Acquisition Costs**

Policy acquisition costs for the three months ended June 30, 2011 were \$78.2 million compared to \$74.1 million for the three months ended June 30, 2010, an increase of \$4.1 million or 5.5%. Policy acquisition costs as a percent of net premiums earned for the three months ended June 30, 2011 and 2010 were 18.4% and 16.9%, respectively. The changes in policy acquisition costs are due to the factors provided below.

|                               | Three Months Ended<br>June 30, 2011 |                                       |  | Three Months Ended<br>June 30, 2010 |                                       |  | %<br>Change |
|-------------------------------|-------------------------------------|---------------------------------------|--|-------------------------------------|---------------------------------------|--|-------------|
|                               | Policy<br>Acquisition<br>Costs      | Policy<br>Acquisition<br>Costs<br>(%) | Policy<br>Acquisition<br>Cost<br>Ratio | Policy<br>Acquisition<br>Costs      | Policy<br>Acquisition<br>Costs<br>(%) | Policy<br>Acquisition<br>Cost<br>Ratio |             |
| <b>(Dollars in thousands)</b> | <b>Costs</b>                        | <b>(%)</b>                            | <b>Ratio</b>                           | <b>Costs</b>                        | <b>(%)</b>                            | <b>Ratio</b>                           |             |
| Property                      | \$ 30,032                           | 38.4%                                 | 14.7%                                  | \$ 30,614                           | 41.3%                                 | 13.7%                                  | (1.9)%      |
| Marine                        | 26,977                              | 34.5%                                 | 21.5%                                  | 22,982                              | 31.0%                                 | 20.6%                                  | 17.4%       |
| Specialty                     | 21,221                              | 27.1%                                 | 22.2%                                  | 20,530                              | 27.7%                                 | 20.0%                                  | 3.4%        |
| <b>Total</b>                  | <b>\$ 78,230</b>                    | <b>100.0%</b>                         | <b>18.4%</b>                           | <b>\$ 74,126</b>                    | <b>100.0%</b>                         | <b>16.9%</b>                           | <b>5.5%</b> |

*Validus Re.* Validus Re policy acquisition costs for the three months ended June 30, 2011 were \$35.8 million compared to \$38.0 million for the three months ended June 30, 2010, a decrease of \$2.2 million or 5.8%.

|                               | Three Months Ended<br>June 30, 2011 |                                       |  | Three Months Ended<br>June 30, 2010 |                                       |  | %<br>Change   |
|-------------------------------|-------------------------------------|---------------------------------------|--|-------------------------------------|---------------------------------------|--|---------------|
|                               | Policy<br>Acquisition<br>Costs      | Policy<br>Acquisition<br>Costs<br>(%) | Policy<br>Acquisition<br>Cost<br>Ratio | Policy<br>Acquisition<br>Costs      | Policy<br>Acquisition<br>Costs<br>(%) | Policy<br>Acquisition<br>Cost<br>Ratio |               |
| <b>(Dollars in thousands)</b> | <b>Costs</b>                        | <b>(%)</b>                            | <b>Ratio</b>                           | <b>Costs</b>                        | <b>(%)</b>                            | <b>Ratio</b>                           |               |
| Property                      | \$ 22,546                           | 63.0%                                 | 13.5%                                  | \$ 27,182                           | 71.6%                                 | 14.6%                                  | (17.1)%       |
| Marine                        | 10,147                              | 28.4%                                 | 21.8%                                  | 7,707                               | 20.3%                                 | 16.0%                                  | 31.7%         |
| Specialty                     | 3,076                               | 8.6%                                  | 15.9%                                  | 3,090                               | 8.1%                                  | 11.3%                                  | (0.5)%        |
| <b>Total</b>                  | <b>\$ 35,769</b>                    | <b>100.0%</b>                         | <b>15.4%</b>                           | <b>\$ 37,979</b>                    | <b>100.0%</b>                         | <b>14.5%</b>                           | <b>(5.8)%</b> |

Policy acquisition costs include brokerage, commission and excise tax, are generally driven by contract terms and are normally a set percentage of premiums and are also net of ceding commission income on retrocessions. Items such as ceded premium, earned premium adjustments and reinstatement premiums that are recognized in the period have an effect on policy acquisition costs. Validus Re policy acquisition costs as a percent of net premiums earned for the three months ended June 30, 2011 and 2010 were 15.4% and 14.5%, respectively. The policy acquisition cost ratio in the marine lines increased by 5.8 percentage points due primarily to the three months ended June 30, 2010 containing substantially more reinstatement premiums, which have no associated policy acquisition costs. The policy acquisition



cost ratio in the specialty line has increased by 4.6 percentage points due primarily to negative earned premium adjustments in the three months ended June 30, 2011.

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*Talbot.* Talbot policy acquisition costs for the three months ended June 30, 2011 were \$42.3 million compared to \$38.6 million for the three months ended June 30, 2010, an increase of \$3.7 million or 9.5%.

|                               | Three Months Ended<br>June 30, 2011   |                                       |                              | Three Months Ended<br>June 30, 2010   |                                       |                              | %<br>Change |
|-------------------------------|---------------------------------------|---------------------------------------|------------------------------|---------------------------------------|---------------------------------------|------------------------------|-------------|
|                               | Policy<br>Acquisition<br>Costs<br>(%) | Policy<br>Acquisition<br>Costs<br>(%) | Acquisition<br>Cost<br>Ratio | Policy<br>Acquisition<br>Costs<br>(%) | Policy<br>Acquisition<br>Costs<br>(%) | Acquisition<br>Cost<br>Ratio |             |
| <b>(Dollars in thousands)</b> | <b>Costs</b>                          | <b>(%)</b>                            | <b>Ratio</b>                 | <b>Costs</b>                          | <b>(%)</b>                            | <b>Ratio</b>                 |             |
| Property                      | \$ 7,217                              | 17.0%                                 | 19.1%                        | \$ 5,824                              | 15.1%                                 | 15.7%                        | 23.9%       |
| Marine                        | 16,834                                | 39.8%                                 | 21.3%                        | 15,314                                | 39.6%                                 | 24.1%                        | 9.9%        |
| Specialty                     | 18,256                                | 43.2%                                 | 24.0%                        | 17,509                                | 45.3%                                 | 23.2%                        | 4.3%        |
| <b>Total</b>                  | <b>\$ 42,307</b>                      | <b>100.0%</b>                         | <b>21.9%</b>                 | <b>\$ 38,647</b>                      | <b>100.0%</b>                         | <b>22.0%</b>                 | <b>9.5%</b> |

Policy acquisition costs as a percent of net premiums earned for the three months ended June 30, 2011 and 2010 were 21.9% and 22.0%, respectively. The policy acquisition cost ratio in the Talbot property lines increased due to increased syndicate acquisition cost rates and a reduction in intercompany ceded premiums and the associated ceding commissions.

**General and Administrative Expenses**

General and administrative expenses for the three months ended June 30, 2011 were \$60.8 million compared to \$52.4 million for the three months ended June 30, 2010, an increase of \$8.5 million or 16.2%. The increase was a result of increased expenses in the Validus Re and Talbot segments, offset by a decrease in the Corporate segment.

|                               | Three Months Ended<br>June 30, 2011                 |   | Three Months Ended<br>June 30, 2010                 |   | %<br>Change  |
|-------------------------------|---|---|---|---|--------------|
|                               | General<br>and<br>Administrative<br>Expenses<br>(%) | General<br>and<br>Administrative<br>Expenses<br>(%) | General<br>and<br>Administrative<br>Expenses<br>(%) | General<br>and<br>Administrative<br>Expenses<br>(%) |              |
| <b>(Dollars in thousands)</b> | <b>Expenses</b>                                     | <b>(%)</b>  | <b>Expenses</b>                                     | <b>(%)</b>  |              |
| Validus Re                    | \$ 15,458   | 25.4%   | \$ 10,983   | 21.0%   | 40.7%        |
| Talbot                        | 34,718  | 57.1%   | 24,960  | 47.6%   | 39.1%        |
| Corporate & Eliminations      | 10,665  | 17.5%   | 16,436  | 31.4%   | (35.1)%      |
| <b>Total</b>                  | <b>\$ 60,841</b>                                    | <b>100.0%</b>                                       | <b>\$ 52,379</b>                                    | <b>100.0%</b>                                       | <b>16.2%</b> |

General and administrative expenses of \$60.8 million in the three months ended June 30, 2011 represents 14.3 percentage points of the expense ratio. Share compensation expense is discussed in the following section. *Validus Re.* Validus Re general and administrative expenses for the three months ended June 30, 2011 were \$15.5 million compared to \$11.0 million for the three months ended June 30, 2010, an increase of \$4.5 million or 40.7%. General and administrative expenses have increased due primarily to a \$1.8 million increase in salaries and benefits driven by increased staff numbers and a \$1.5 million increase in professional fees. General and administrative expenses include salaries and benefits, professional fees, rent and office expenses. Validus Re's general and administrative expenses as a percent of net premiums earned for the three months ended June 30, 2011 and 2010 were 6.6% and 4.2%, respectively.

*Talbot.* Talbot general and administrative expenses for the three months ended June 30, 2011 were \$34.7 million compared to \$25.0 million for the three months ended June 30, 2010, an increase of \$9.8 million or 39.1%. To better align the Company's operating and reporting structure with its current strategy, there was an internal reallocation of

\$2.1 million relating to the New York operations from the Corporate segment to the Talbot segment. Other factors contributing to the increase in general and administrative expenses are a \$2.6 million increase in staff costs due to a higher staff count, a \$2.5 million increase in bonus expense and a \$1.4 million increase in syndicate costs. Talbot's general and administrative expenses as a percent of net premiums earned for the three months ended June 30, 2011 and 2010 were 18.0% and 14.2%, respectively.

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*Corporate & Eliminations.* Corporate general and administrative expenses for the three months ended June 30, 2011 were \$10.7 million compared to \$16.4 million for the three months ended June 30, 2010, a decrease of \$5.8 million or 35.1%. To better align the Company's operating and reporting structure with its current strategy, there was an internal reallocation of \$2.1 million relating to the New York operations from the Corporate segment to the Talbot segment. There was also an allocation of corporate expenses of \$2.2 million to the operating segments relating to group wide costs. Corporate general and administrative expenses are comprised of executive and board expenses, internal and external audit expenses and other costs relating to the Company as a whole.

**Share Compensation Expenses**

Share compensation expenses for the three months ended June 30, 2011 were \$7.6 million compared to \$6.8 million for the three months ended June 30, 2010, an increase of \$0.8 million or 11.4%. This expense is non-cash and has no net effect on total shareholders' equity, as it is balanced by an increase in additional paid-in capital.

|                               | Three Months Ended<br>June 30, 2011 |  | Three Months Ended<br>June 30, 2010 |  | %<br>Change  |
|-------------------------------|-------------------------------------|--|-------------------------------------|--|--------------|
|                               | Share<br>Compensation<br>Expenses   | Share<br>Compensation<br>Expenses<br>(%) | Share<br>Compensation<br>Expenses   | Share<br>Compensation<br>Expenses<br>(%) |              |
| <b>(Dollars in thousands)</b> |                                     |  |                                     |  |              |
| Validus Re                    | \$ 1,823                            | 23.9%                                    | \$ 1,749                            | 25.6%                                    | 4.2%         |
| Talbot                        | 2,026                               | 26.6%                                    | 1,468                               | 21.4%                                    | 38.0%        |
| Corporate & Eliminations      | 3,779                               | 49.5%                                    | 3,629                               | 53.0%                                    | 4.1%         |
| <b>Total</b>                  | <b>\$ 7,628</b>                     | <b>100.0%</b>                            | <b>\$ 6,846</b>                     | <b>100.0%</b>                            | <b>11.4%</b> |

Share compensation expenses of \$7.6 million in the three months ended June 30, 2011 represents 1.8 percentage points of the general and administrative expense ratio.

*Validus Re.* Validus Re share compensation expenses for the three months ended June 30, 2011 were \$1.8 million compared to \$1.7 million for the three months ended June 30, 2010 an increase of \$0.1 million or 4.2%. Share compensation expense as a percent of net premiums earned for the three months ended June 30, 2011 and 2010 were 0.8% and 0.7%, respectively.

*Talbot.* Talbot share compensation expenses for the three months ended June 30, 2011 was \$2.0 million compared to \$1.5 million for the three months ended June 30, 2010 an increase of \$0.6 million or 38.0%. This increase was due primarily to an increase in restricted share awards as a part of the executive and non-executive long term incentive plan. Share compensation expense as a percent of net premiums earned for the three months ended June 30, 2011 and 2010 were 1.0% and 0.8%, respectively.

*Corporate & Eliminations.* Corporate share compensation expenses for the three months ended June 30, 2011 were \$3.8 million compared to \$3.6 million for the three months ended June 30, 2010, an increase of \$0.2 million or 4.1%. This increase was due primarily to an increase in restricted share awards as a part of the executive and non-executive long term incentive plan.

**Selected Ratios**

The underwriting results of an insurance or reinsurance company are often measured by reference to its combined ratio, which is the sum of the loss ratio and the expense ratio. The net loss ratio is calculated by dividing losses and loss expenses incurred (including estimates for incurred but not reported losses) by net premiums earned. The expense ratio is calculated by dividing acquisition costs combined with general and administrative expenses (including share compensation expenses) by net premiums earned. The following table presents the losses and loss expenses ratio, policy acquisition cost ratio, general and administrative expense ratio, expense ratio and combined ratio for the three months ended June 30, 2011 and 2010.

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|  | <b>Three Months<br/>Ended</b> | <b>Three Months<br/>Ended</b> | <b>Percentage<br/>Point<br/>Change</b> |
|--|-------------------------------|-------------------------------|--|
|  | <b>June 30, 2011</b>          | <b>June 30, 2010</b>          |  |
| Losses and loss expense ratio                | 48.7%                         | 44.5%                         | 4.2                                    |
| Policy acquisition cost ratio                | 18.4%                         | 16.9%                         | 1.5                                    |
| General and administrative expense ratio (a) | 16.1%                         | 13.5%                         | 2.6                                    |
| <b>Expense ratio</b>                         | <b>34.5%</b>                  | <b>30.4%</b>                  | <b>4.1</b>                             |
| <b>Combined ratio</b>                        | <b>83.2%</b>                  | <b>74.9%</b>                  | <b>8.3</b>                             |

|  | <b>Three Months<br/>Ended</b> | <b>Three Months<br/>Ended</b> | <b>Percentage<br/>Point<br/>Change</b> |
|--|-------------------------------|-------------------------------|--|
|  | <b>June 30, 2011</b>          | <b>June 30, 2010</b>          |  |
| <i>Validus Re</i>                            |                               |                               |  |
| Losses and loss expense ratio                | 40.4%                         | 47.2%                         | (6.8)                                  |
| Policy acquisition cost ratio                | 15.4%                         | 14.5%                         | 0.9                                    |
| General and administrative expense ratio (a) | 7.4%                          | 4.9%                          | 2.5                                    |
| <b>Expense ratio</b>                         | <b>22.8%</b>                  | <b>19.4%</b>                  | <b>3.4</b>                             |
| <b>Combined ratio</b>                        | <b>63.2%</b>                  | <b>66.6%</b>                  | <b>(3.4)</b>                           |

|  | <b>Three Months<br/>Ended</b> | <b>Three Months<br/>Ended</b> | <b>Percentage<br/>Point<br/>Change</b> |
|--|-------------------------------|-------------------------------|--|
|  | <b>June 30, 2011</b>          | <b>June 30, 2010</b>          |  |
| <i>Talbot</i>                                |                               |                               |  |
| Losses and loss expense ratio                | 58.7%                         | 40.4%                         | 18.3                                   |
| Policy acquisition cost ratio                | 21.9%                         | 22.0%                         | (0.1)                                  |
| General and administrative expense ratio (a) | 19.0%                         | 15.0%                         | 4.0                                    |
| <b>Expense ratio</b>                         | <b>40.9%</b>                  | <b>37.0%</b>                  | <b>3.9</b>                             |
| <b>Combined ratio</b>                        | <b>99.6%</b>                  | <b>77.4%</b>                  | <b>22.2</b>                            |

(a) Includes general and administrative expenses and share compensation expenses.

General and administrative expense ratios for the three months ended June 30, 2011 and 2010 were 16.1% and 13.5%, respectively. General and administrative expense ratio is the sum of general and administrative expenses and share compensation expense divided by net premiums earned.

| <b>Three Months Ended<br/>June 30, 2011</b> | <b>Three Months Ended<br/>June 30, 2010</b> |
|---|---|
| <b>Expenses as<br/>% of</b>                 | <b>Expenses as<br/>% of</b>                 |

| <b>(Dollars in thousands)</b>       | <b>Expenses</b>  | <b>Net Earned<br/>Premiums</b> | <b>Expenses</b>  | <b>Net Earned<br/>Premiums</b> |
|-------------------------------------|------------------|--------------------------------|------------------|--------------------------------|
| General and administrative expenses | \$ 60,841        | 14.3%                          | \$ 52,379        | 12.0%                          |
| Share compensation expenses         | 7,628            | 1.8%                           | 6,846            | 1.5%                           |
| <b>Total</b>                        | <b>\$ 68,469</b> | <b>16.1%</b>                   | <b>\$ 59,225</b> | <b>13.5%</b>                   |

**Underwriting Income**

Underwriting income for the three months ended June 30, 2011 was \$71.6 million compared to underwriting income of \$109.7 million for the three months ended June 30, 2010, a decrease of \$38.1 million, or 34.7%.

| <b>(Dollars in thousands)</b> | <b>Three<br/>Months<br/>Ended June<br/>30,<br/>2011</b> | <b>% of<br/>sub-total</b> | <b>Three<br/>Months<br/>Ended June<br/>30,<br/>2010</b> | <b>% of<br/>sub-total</b> | <b>%<br/>Change</b> |
|-------------------------------|---|---------------------------|---|---------------------------|---------------------|
| Validus Re                    | \$ 85,593   | 99.3%                     | \$ 87,537   | 68.8%                     | (2.2)%              |
| Talbot                        | 639   | 0.7%                      | 39,727  | 31.2%                     | (98.4)%             |
| Sub-total                     | 86,232  | 100.0%                    | 127,264   | 100.0%                    | (32.2)%             |
| Corporate & Eliminations      | (14,598)  |                           | (17,565)  |                           | (16.9)%             |
| <b>Total</b>                  | <b>\$ 71,634</b>  |                           | <b>\$ 109,699</b>                                       |                           | <b>(34.7)%</b>      |

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The underwriting results of an insurance or reinsurance company are also often measured by reference to its underwriting income, which is a non-GAAP financial measure. Underwriting income, as set out in the table below, is reconciled to net income (the most directly comparable GAAP financial measure) by the addition or subtraction of certain Consolidated Statement of Operations and Comprehensive Income (Loss) line items, as illustrated below.

| <b>(Dollars in thousands)</b>       | <b>Three Months<br/>Ended<br/>June 30, 2011</b> | <b>Three Months<br/>Ended<br/>June 30, 2010</b> |
|-------------------------------------|---|---|
| Underwriting income                 | \$ 71,634                                       | \$ 109,699                                      |
| Net investment income               | 26,494  | 34,809  |
| Other income                        | 595   | 2,697   |
| Finance expenses                    | (16,361)  | (13,218)  |
| Net realized gains on investments   | 11,552  | 12,441  |
| Net unrealized gains on investments | 18,526  | 41,640  |
| Foreign exchange (losses)           | (1,991)   | (4,099)   |
| <b>Net income before tax</b>        | <b>\$ 110,449</b>                               | <b>\$ 183,969</b>                               |

Underwriting income indicates the performance of the Company's core underwriting function, excluding revenues and expenses such as the reconciling items in the table above. The Company believes the reporting of underwriting income enhances the understanding of our results by highlighting the underlying profitability of the Company's core insurance and reinsurance business. Underwriting profitability is influenced significantly by earned premium growth, adequacy of the Company's pricing and loss frequency and severity. Underwriting profitability over time is also influenced by the Company's underwriting discipline, which seeks to manage exposure to loss through favorable risk selection and diversification, its management of claims, its use of reinsurance and its ability to manage its expense ratio, which it accomplishes through its management of acquisition costs and other underwriting expenses. The Company believes that underwriting income provides investors with a valuable measure of profitability derived from underwriting activities.

The Company excludes the U.S. GAAP income statement line items noted above, from its calculation of underwriting income. Net realized and unrealized gains (losses) on investments are excluded because the amount of these gains and losses is heavily influenced by, and fluctuates in part, according to availability of investment market opportunities. The Company believes the other line items excluded are largely independent of its underwriting business and including them distorts the analysis of trends in its operations. In addition to presenting net income determined in accordance with U.S. GAAP, the Company believes that showing underwriting income enables investors, analysts, rating agencies and other users of its financial information to more easily analyze the Company's results of operations in a manner similar to how management analyzes the Company's underlying business performance. The Company uses underwriting income as a primary measure of underwriting results in its analysis of historical financial information and when performing its budgeting and forecasting processes. Analysts, investors and rating agencies who follow the Company request this non-GAAP financial information on a regular basis. In addition, underwriting income is one of the factors considered by the compensation committee of our Board of Directors in determining the bonus component of the total annual incentive compensation.

Underwriting income should not be viewed as a substitute for U.S. GAAP net income as there are inherent material limitations associated with the use of underwriting income as compared to using net income, which is the most directly comparable U.S. GAAP financial measure. The most significant limitation is the ability of users of the financial information to make comparable assessments of underwriting income with other companies, particularly as underwriting income may be defined or calculated differently by other companies. Therefore, the Company provides more prominence in this filing to the use of the most comparable U.S. GAAP financial measure, net income, which includes the reconciling items in the table above. The Company compensates for these limitations by providing both clear and transparent disclosure of net income and reconciliation of underwriting income to net income.





**Table of Contents****Net Investment Income**

Net investment income for the three months ended June 30, 2011 was \$26.5 million compared to \$34.8 million for the three months ended June 30, 2010, a decrease of \$8.3 million or 23.9%. Net investment income decreased due to falling yields on fixed maturity investments. Net investment is comprised of accretion of premium or discount on fixed maturities, interest on coupon-paying bonds, short-term investments and cash and cash equivalents, partially offset by investment management fees. The components of net investment income for the three months ended June 30, 2011 and 2010 are as provided below.

| (Dollars in thousands)                      | Three Months<br>Ended | Three Months<br>Ended | %<br>Change |
|---|-----------------------|-----------------------|-------------|
|   | June 30, 2011         | June 30, 2010         |             |
| Fixed maturities and short-term investments | \$ 27,535             | \$ 36,346             | (24.2)%     |
| Cash and cash equivalents                   | 687                   | 311                   | 120.9%      |
| Securities lending income                   | 8                     | 49                    | (83.7)%     |
| Total gross investment income               | 28,230                | 36,706                | (23.1)%     |
| Investment expenses                         | (1,736)               | (1,897)               | 8.5%        |
| Net investment income                       | \$ 26,494             | \$ 34,809             | (23.9)%     |

Annualized effective investment yield is based on the weighted average investments held calculated on a simple period average and excludes net unrealized gains (losses), realized gains (losses) on investments, foreign exchange gains (losses) on investments and the foreign exchange effect of insurance balances. The Company's annualized effective investment yield was 1.76% and 2.37% for the three months ended June 30, 2011 and 2010, respectively, and the average duration of the portfolio at June 30, 2011 was 1.57 years (December 31, 2010 - 2.27 years).

**Other Income**

Other income for the three months ended June 30, 2011 was \$0.6 million compared to \$2.7 million for the three months ended June 30, 2010, a decrease of \$2.1 million or 77.9%.

**Finance Expenses**

Finance expenses for the three months ended June 30, 2011 were \$16.4 million compared to \$13.2 million for the three months ended June 30, 2010, an increase of \$3.1 million or 23.8%. Finance expenses also include the amortization of debt offering costs and discounts, and fees related to our credit facilities.

| (Dollars in thousands)                         | Three Months Ended June<br>30, |                  | %<br>Change  |
|--|--------------------------------|------------------|--------------|
|  | 2011                           | 2010             |              |
| 2006 Junior Subordinated Deferrable Debentures | \$ 3,228                       | \$ 3,589         | (10.1)%      |
| 2007 Junior Subordinated Deferrable Debentures | 3,028                          | 3,028            | 0.0%         |
| 2010 Senior Notes due 2040                     | 5,597                          | 5,597            | 0.0%         |
| Credit facilities                              | 1,589                          | 1,109            | 43.3%        |
| AlphaCat Re 2011 fees (a)                      | 2,919                          |                  | NM           |
| Talbot FAL Facility                            |                                | (89)             | NM           |
| Talbot other interest                          |                                | (16)             | NM           |
| <b>Finance expenses</b>                        | <b>\$ 16,361</b>               | <b>\$ 13,218</b> | <b>23.8%</b> |

(a) Includes finance expenses attributable to noncontrolling interest.

NM: Not Meaningful

Capital in Lloyd's entities, whether personal or corporate, is required to be set annually for the prospective year and held by Lloyd's in trust ( Funds at Lloyd's or FAL ). For underwriting years up to and including 2007, Talbot's FAL has been provided both by Talbot and by third parties, thereafter Talbot's FAL has been provided exclusively by the Company.

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As all of the underwriting years up to and including 2007 are closed with effect from December 31, 2009, the FAL relating to these years has been returned to the third party providers. There were some costs paid in 2010, which are the final amounts payable under the Talbot third party FAL facility.

**Tax Benefit (Expense)**

Tax expense for the three months ended June 30, 2011 was \$0.0 million compared to an expense of (\$4.2) million for the three months ended June 30, 2010, a decrease of \$4.2 million or 100.7%. The decrease is primarily due to adjustments to deferred tax balances in the Talbot segment following the reduction in the effective U.K. tax rate from 28.0% to 26.5% together with a reduction in U.K. taxable profits.

**Net Realized Gains on Investments**

Net realized gains on investments for the three months ended June 30, 2011 were \$11.6 million compared to \$12.4 million for the three months ended June 30, 2010, a decrease of \$0.9 million or 7.1%.

**Net Unrealized Gains on Investments**

Net unrealized gains on investments for the three months ended June 30, 2011 were \$18.5 million compared to \$41.6 million for the three months ended June 30, 2010 a decrease of \$23.1 million or 55.5%. The net unrealized gains in the three months ended June 30, 2011 were a result of a significant downward shift in rates as the two-year Treasury rate fell from 0.82% to 0.46% (36 bps) and the five-year rate decreased from 2.28% to 1.76% (52 bps) in the period.

Net unrealized gains on investments are recorded as a component of net income. The Company has adopted all authoritative guidance on U.S. GAAP fair value measurements in effect as of the balance sheet date. Consistent with these standards, certain market conditions allow for fair value measurements that incorporate unobservable inputs where active market transaction based measurements are unavailable. Certain non-Agency RMBS securities were previously identified as trading in inactive markets.

**Foreign Exchange (Losses)**

Foreign exchange losses for the three months ended June 30, 2011 were (\$2.0) million compared to (\$4.1) million for the three months ended June 30, 2010, a favorable movement of \$2.1 million or 51.4%. The favorable movement in foreign exchange was due primarily to the increased value of assets denominated in foreign currencies relative to the U.S. dollar reporting currency for the three months ended June 30, 2011, as compared to the three months ended June 30, 2010. For the three months ended June 30, 2011, Validus Re recognized foreign exchange losses of (\$5.3) million, Talbot recognized foreign exchange gains of \$3.4 million. The Euro to U.S. dollar exchange rates were 1.41 and 1.44 at March 31, 2011 and June 30, 2011, respectively. The British pound sterling to U.S. dollar exchange rates were 1.60 and 1.60 at March 31, 2011 and June 30, 2011, respectively. During the quarter, the Euro appreciated by 2.1%, while the British pound remained stable.

For the three months ended June 30, 2011, Validus Re segment foreign exchange losses were (\$5.3) million compared to losses of (\$0.8) million for the three months ended June 30, 2010, an unfavorable movement of \$4.5 million or 533.1%. The unfavorable movement in Validus Re foreign exchange losses was due primarily to losses incurred as a result of the Company having liabilities in both New Zealand dollars and Japanese Yen during a period when both of these currencies strengthened against the U.S. dollar.

For the three months ended June 30, 2011, Talbot segment foreign exchange gains were \$3.4 million compared to losses of (\$3.2) million for the three months ended June 30, 2010, a favorable movement of \$6.7 million or 205.1%. The favorable movement in Talbot segment foreign exchange was due primarily to the valuation of funds held in Euros given the appreciation of the British pound sterling against the Euro during the three months ended June 30, 2011. Certain premiums receivable and liabilities for losses incurred in currencies other than the U.S. dollar are exposed to the risk of changes in value resulting from fluctuations in foreign exchange rates and may affect financial results in the future.

At June 30, 2011, Talbot's balance sheet includes net unearned premiums and deferred acquisition costs denominated in foreign currencies of approximately \$103.7 million and \$21.6 million, respectively. These balances consisted of British pound sterling and Canadian dollars of \$73.0 million and \$9.1 million, respectively.

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Net unearned premiums and deferred acquisition costs are classified as non-monetary items and are translated at historic exchange rates. All of Talbot's other balance sheet items are classified as monetary items and are translated at period end exchange rates. Additional foreign exchange gains (losses) may be incurred on the translation of net unearned premiums and deferred acquisition costs arising from insurance and reinsurance premiums written in future periods.

**Net Income Attributable to Noncontrolling Interest**

On May 25, 2011, the Company joined with other investors in capitalizing AlphaCat Re 2011, a new special purpose sidecar reinsurer formed for the purpose of writing collateralized reinsurance and retrocessional reinsurance. Validus Re has an equity interest in AlphaCat Re 2011 and as Validus Re holds a majority of AlphaCat Re 2011's outstanding voting rights, the financial statements of AlphaCat Re 2011 are included in the consolidated financial statements of the Company. The portion of AlphaCat Re 2011's earnings attributable to third party investors for the three months ended June 30, 2011 is recorded in the consolidated statement of operations and comprehensive income as net income attributable to noncontrolling interest.

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The following table presents results of operations for the three and six months ended June 30, 2011 and 2010:

| <b>(Dollars in thousands)</b>                                | <b>Three Months Ended June</b> |                   | <b>Six Months Ended June 30,</b> |                  |
|--|--------------------------------|-------------------|----------------------------------|------------------|
|  | <b>2011</b>                    | <b>2010</b>       | <b>2011</b>                      | <b>2010</b>      |
| Gross premiums written                                       | \$ 605,387                     | \$ 516,861        | \$ 1,455,283                     | \$ 1,387,795     |
| Reinsurance premiums ceded                                   | (132,346)                      | (67,726)          | (242,166)                        | (158,465)        |
| Net premiums written   | 473,041                        | 449,135           | 1,213,117                        | 1,229,330        |
| Change in unearned premiums                                  | (47,401)                       | (11,191)          | (357,944)                        | (333,692)        |
| <b>Net premiums earned</b>                                   | <b>425,640</b>                 | <b>437,944</b>    | <b>855,173</b>                   | <b>895,638</b>   |
| Losses and loss expenses                                     | 207,307                        | 194,894           | 683,505                          | 673,425          |
| Policy acquisition costs                                     | 78,230                         | 74,126            | 155,526                          | 150,302          |
| General and administrative expenses                          | 60,841                         | 52,379            | 109,318                          | 105,948          |
| Share compensation expenses                                  | 7,628                          | 6,846             | 19,677                           | 13,422           |
| <b>Total underwriting deductions</b>                         | <b>354,006</b>                 | <b>328,245</b>    | <b>968,026</b>                   | <b>943,097</b>   |
| <b>Underwriting income (loss) (a)</b>                        | <b>71,634</b>                  | <b>109,699</b>    | <b>(112,853)</b>                 | <b>(47,459)</b>  |
| Net investment income  | 26,494                         | 34,809            | 56,469                           | 69,108           |
| Other income   | 595                            | 2,697             | 2,201                            | 3,585            |
| Finance expenses   | (16,361)                       | (13,218)          | (30,362)                         | (28,369)         |
| <b>Operating income (loss) before taxes</b>                  | <b>82,362</b>                  | <b>133,987</b>    | <b>(84,545)</b>                  | <b>(3,135)</b>   |
| Tax benefit (expense)  | 29                             | (4,187)           | 1,488                            | (3,490)          |
| <b>Net operating income (loss) (a)</b>                       | <b>82,391</b>                  | <b>129,800</b>    | <b>(83,057)</b>                  | <b>(6,625)</b>   |
| Net realized gains on investments                            | 11,552                         | 12,441            | 17,931                           | 23,839           |
| Net unrealized gains on investments                          | 18,526                         | 41,640            | 5,698                            | 57,053           |
| Foreign exchange (losses)                                    | (1,991)                        | (4,099)           | (2,458)                          | (12,863)         |
| <b>Net income (loss)</b>                                     | <b>110,478</b>                 | <b>179,782</b>    | <b>(61,886)</b>                  | <b>61,404</b>    |
| Net income attributable to noncontrolling interest           | (594)                          |                   | (594)                            |                  |
| <b>Net income (loss) available (attributable) to Validus</b> | <b>\$ 109,884</b>              | <b>\$ 179,782</b> | <b>\$ (62,480)</b>               | <b>\$ 61,404</b> |
| <b>Selected ratios:</b>                                      |                                |                   |                                  |                  |
| Net premiums written / Gross premiums written                | 78.1%                          | 86.9%             | 83.4%                            | 88.6%            |

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|   |       |       |        |        |
|---|-------|-------|--------|--------|
| Losses and loss expenses                | 48.7% | 44.5% | 79.9%  | 75.2%  |
| Policy acquisition costs                | 18.4% | 16.9% | 18.2%  | 16.8%  |
| General and administrative expenses (b) | 16.1% | 13.5% | 15.1%  | 13.3%  |
| Expense ratio                           | 34.5% | 30.4% | 33.3%  | 30.1%  |
| Combined ratio                          | 83.2% | 74.9% | 113.2% | 105.3% |

- a) Non-GAAP Financial Measures: In presenting the Company's results, management has included and discussed underwriting income and operating income that are not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. A reconciliation of underwriting income to net income, the most comparable U.S. GAAP financial measure, is presented in the section below entitled Underwriting Income.
- b) The general and administrative ratio includes share compensation expenses.

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|                                       | <b>Three Months Ended June</b> |                | <b>Six Months Ended June</b> |                 |
|---------------------------------------|--------------------------------|----------------|------------------------------|-----------------|
|                                       | <b>30,</b>                     |                | <b>30,</b>                   |                 |
|                                       | <b>2011</b>                    | <b>2010</b>    | <b>2011</b>                  | <b>2010</b>     |
| <b>Validus Re</b>                     |                                |                |                              |                 |
| Gross premiums written                | \$ 341,651                     | \$ 284,328     | \$ 952,889                   | \$ 924,623      |
| Reinsurance premiums ceded            | (98,218)                       | (41,175)       | (145,023)                    | (54,285)        |
| Net premiums written                  | 243,433                        | 243,153        | 807,866                      | 870,338         |
| Change in unearned premiums           | (10,755)                       | 18,888         | (322,879)                    | (324,376)       |
| <b>Net premiums earned</b>            | <b>232,678</b>                 | <b>262,041</b> | <b>484,987</b>               | <b>545,962</b>  |
| Losses and loss expenses              | 94,035                         | 123,793        | 404,579                      | 472,713         |
| Policy acquisition costs              | 35,769                         | 37,979         | 75,835                       | 81,482          |
| General and administrative expenses   | 15,458                         | 10,983         | 26,115                       | 27,295          |
| Share compensation expenses           | 1,823                          | 1,749          | 4,928                        | 3,378           |
| <b>Total underwriting deductions</b>  | <b>147,085</b>                 | <b>174,504</b> | <b>511,457</b>               | <b>584,868</b>  |
| <b>Underwriting income (loss) (a)</b> | <b>85,593</b>                  | <b>87,537</b>  | <b>(26,470)</b>              | <b>(38,906)</b> |
| <b>Talbot</b>                         |                                |                |                              |                 |
| Gross premiums written                | \$ 276,886                     | \$ 253,710     | \$ 539,943                   | \$ 524,251      |
| Reinsurance premiums ceded            | (47,278)                       | (47,728)       | (134,692)                    | (165,259)       |
| Net premiums written                  | 229,608                        | 205,982        | 405,251                      | 358,992         |
| Change in unearned premiums           | (36,646)                       | (30,079)       | (35,065)                     | (9,316)         |
| <b>Net premiums earned</b>            | <b>192,962</b>                 | <b>175,903</b> | <b>370,186</b>               | <b>349,676</b>  |
| Losses and loss expenses              | 113,272                        | 71,101         | 278,926                      | 200,712         |
| Policy acquisition costs              | 42,307                         | 38,647         | 79,523                       | 73,592          |
| General and administrative expenses   | 34,718                         | 24,960         | 63,440                       | 50,508          |
| Share compensation expenses           | 2,026                          | 1,468          | 4,745                        | 3,027           |
| <b>Total underwriting deductions</b>  | <b>192,323</b>                 | <b>136,176</b> | <b>426,634</b>               | <b>327,839</b>  |
| <b>Underwriting income (loss) (a)</b> | <b>639</b>                     | <b>39,727</b>  | <b>(56,448)</b>              | <b>21,837</b>   |
| <b>Corporate &amp; Eliminations</b>   |                                |                |                              |                 |
| Gross premiums written                | \$ (13,150)                    | \$ (21,177)    | \$ (37,549)                  | \$ (61,079)     |
| Reinsurance premiums ceded            | 13,150                         | 21,177         | 37,549                       | 61,079          |
| Net premiums written                  |                                |                |                              |                 |

Change in unearned premiums

**Net premiums earned**

Losses and loss expenses

|                                     |        |         |        |         |
|-------------------------------------|--------|---------|--------|---------|
| Policy acquisition costs            | 154    | (2,500) | 168    | (4,772) |
| General and administrative expenses | 10,665 | 16,436  | 19,763 | 28,145  |
| Share compensation expenses         | 3,779  | 3,629   | 10,004 | 7,017   |

|                                      |        |        |        |        |
|--------------------------------------|--------|--------|--------|--------|
| <b>Total underwriting deductions</b> | 14,598 | 17,565 | 29,935 | 30,390 |
|--------------------------------------|--------|--------|--------|--------|

|                                |          |          |          |          |
|--------------------------------|----------|----------|----------|----------|
| <b>Underwriting (loss) (a)</b> | (14,598) | (17,565) | (29,935) | (30,390) |
|--------------------------------|----------|----------|----------|----------|

|   |           |            |              |             |
|---|-----------|------------|--------------|-------------|
| <b>Total underwriting income (loss) (a)</b> | \$ 71,634 | \$ 109,699 | \$ (112,853) | \$ (47,459) |
|---|-----------|------------|--------------|-------------|

- a) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income that is not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. A reconciliation of this measure to net income, the most comparable U.S. GAAP financial measure, is presented in the section below entitled Underwriting Income.



**Table of Contents****Six Months Ended June 30, 2011 compared to Six Months Ended June 30, 2010**

Net loss attributable to Validus for the six months ended June 30, 2011 was (\$62.5) million compared to net income available to Validus of \$61.4 million for the six months ended June 30, 2010, a decrease of \$123.9 million or 201.8%. The primary factors driving the decrease in net income were:

Decrease in underwriting loss of \$65.4 million due primarily to a \$40.5 million decrease in net premiums earned, due primarily to increased reinsurance premiums ceded. Loss and loss expenses and other underwriting deductions also increased by \$10.1 million and \$14.8 million, respectively;

Decrease in net unrealized gains on investments of \$51.4 million;

The change in net income available to Validus for the six months ended June 30, 2011 of \$123.9 million as compared to the six months ended June 30, 2010, is described in the following table:

|  | <b>Six Months Ended June 30,<br/>2011</b>                              |               |  |              |
|--|--|---------------|--|--------------|
|  | <b>(Decrease) increase over the Six Months Ended June 30,<br/>2011</b> |               |  |              |
|  | <b>Validus</b>   |               | <b>Corporate<br/>and other<br/>reconciling</b> |              |
| <b>(Dollars in thousands)</b>  | <b>Re</b>  | <b>Talbot</b> | <b>items</b>                                   | <b>Total</b> |
| Notable losses decrease (increase) in net loss and loss expenses (a)       | \$ 40,039  | \$ (47,264)   | \$   | \$ (7,225)   |
| Less: Notable losses increase (decrease) in net reinstatement premiums (a) | 10,539   | (2,732)       |  | 7,807        |
| Other underwriting (loss) income   | (38,142)   | (28,289)      | 455  | (65,976)     |
| Underwriting income (loss) (b)   | 12,436   | (78,285)      | 455  | (65,394)     |
| Net investment income  | (11,119)   | (1,609)       | 89   | (12,639)     |
| Other income   | (268)  | (75)          | (1,041)  | (1,384)      |
| Finance expenses   | (3,815)  | 3,077         | (1,255)  | (1,993)      |
|  | (2,766)  | (76,892)      | (1,752)  | (81,410)     |
| Taxes  | 179  | 4,884         | (85)   | 4,978        |
|  | (2,587)  | (72,008)      | (1,837)  | (76,432)     |
| Net realized (losses) gains on investments                                 | (6,671)  | 763           |  | (5,908)      |
| Net unrealized (losses) on investments                                     | (41,850)   | (9,505)       |  | (51,355)     |
| Foreign exchange (losses) gains  | (3,715)  | 14,153        | (33)   | 10,405       |
| <b>Net (loss)</b>  | (54,823)   | (66,597)      | (1,870)  | (123,290)    |
| Net income attributable to noncontrolling interest                         | (594)  |               |  | (594)        |
| <b>Net (loss) attributable to Validus</b>                                  | \$ (55,417)  | \$ (66,597)   | \$ (1,870)                                     | \$ (123,884) |

- (a) Notable losses for the six months ended June 30, 2011 include: Tohoku earthquake, Gryphon Alpha, Christchurch earthquake, Brisbane floods, CNRL Horizon, Cat 46, Cat 48 and Jupiter 1. Notable losses for the six months ended June 30, 2010 include: the Chilean earthquake, Melbourne hailstorm, windstorm Xynthia, Deepwater Horizon, Aban Pearl, Bangkok riots and the Perth hailstorm. Excludes reserve for potential development on 2010 and 2011 notable loss events.

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(b) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income (loss) that is not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. A reconciliation of this measure to net income, the most comparable U.S. GAAP financial measure, is presented in the section below entitled Underwriting Income.

**Gross Premiums Written**

Gross premiums written for the six months ended June 30, 2011 were \$1,455.3 million compared to \$1,387.8 million for the six months ended June 30, 2010, an increase of \$67.5 million or 4.9%. The property, marine and specialty lines increased by \$10.5 million, \$32.0 million and \$25.0 million, respectively. Details of gross premiums written by line of business are provided below.

|                               | Six Months Ended<br>June 30, 2011 |                                     | Six Months Ended<br>June 30, 2010 |                                     | %<br>Change |
|-------------------------------|-----------------------------------|-------------------------------------|-----------------------------------|-------------------------------------|-------------|
|                               | Gross<br>Premiums<br>Written      | Gross<br>Premiums<br>Written<br>(%) | Gross<br>Premiums<br>Written      | Gross<br>Premiums<br>Written<br>(%) |             |
| <b>(Dollars in thousands)</b> |                                   |                                     |                                   |                                     |             |
| Property                      | \$ 827,908                        | 56.8%                               | \$ 817,428                        | 58.9%                               | 1.3%        |
| Marine                        | 384,991                           | 26.5%                               | 353,004                           | 25.4%                               | 9.1%        |
| Specialty                     | 242,384                           | 16.7%                               | 217,363                           | 15.7%                               | 11.5%       |
| <b>Total</b>                  | <b>\$ 1,455,283</b>               | <b>100.0%</b>                       | <b>\$ 1,387,795</b>               | <b>100.0%</b>                       | <b>4.9%</b> |

*Validus Re.* Validus Re gross premiums written for the six months ended June 30, 2011 were \$952.9 million compared to \$924.6 million for the six months ended June 30, 2010, an increase of \$28.3 million or 3.1%. Details of Validus Re gross premiums written by line of business are provided below.

|                               | Six Months Ended<br>June 30, 2011 |                                     | Six Months Ended<br>June 30, 2010 |                                     | %<br>Change |
|-------------------------------|-----------------------------------|-------------------------------------|-----------------------------------|-------------------------------------|-------------|
|                               | Gross<br>Premiums<br>Written      | Gross<br>Premiums<br>Written<br>(%) | Gross<br>Premiums<br>Written      | Gross<br>Premiums<br>Written<br>(%) |             |
| <b>(Dollars in thousands)</b> |                                   |                                     |                                   |                                     |             |
| Property                      | \$ 688,376                        | 72.3%                               | \$ 673,976                        | 72.9%                               | 2.1%        |
| Marine                        | 189,879                           | 19.9%                               | 185,396                           | 20.0%                               | 2.4%        |
| Specialty                     | 74,634                            | 7.8%                                | 65,251                            | 7.1%                                | 14.4%       |
| <b>Total</b>                  | <b>\$ 952,889</b>                 | <b>100.0%</b>                       | <b>\$ 924,623</b>                 | <b>100.0%</b>                       | <b>3.1%</b> |

The increase in the Validus Re property lines of \$14.4 million was due primarily to a \$42.6 million increase in premiums written by AlphaCat Re 2011 and a \$21.8 million increase in reinstatement premiums following the Tohoku earthquake, the Christchurch earthquake, Cat 46 and Cat 48. This was partially offset by a \$35.0 million decrease in new and renewing premiums written on a proportional basis and an \$11.0 million decrease in intercompany premiums written with Talbot. The increase in gross premiums written in the Validus Re marine lines of \$4.5 million was due primarily to a \$27.4 million increase in new and renewing business due to growth in proportional lines within the marine lines, offset by an \$11.7 million decrease in premium adjustments and an \$11.3 million decrease in intercompany business written with Talbot. The increase in gross premiums written in the Validus Re specialty lines of \$9.4 million was due primarily to a \$4.8 million increase in new and renewing business including a \$2.0 million

increase in new business generated by Validus Re Singapore and \$3.2 million increase in premium adjustments.

Gross premiums written under the quota share, surplus treaty and excess of loss contracts between Validus Re and Talbot for the six months ended June 30, 2011 decreased by \$23.5 million as compared to the six months ended June 30, 2010. The decrease in premiums written was due to an \$11.0 million decrease in the property lines, an \$11.3 million decrease in the marine lines and a \$1.2 million decrease in the specialty lines. These reinsurance agreements with Talbot are eliminated upon consolidation.

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*Talbot.* Talbot gross premiums written for the six months ended June 30, 2011 were \$539.9 million compared to \$524.3 million for the six months ended June 30, 2010, an increase of \$15.7 million or 3.0%. The \$539.9 million of gross premiums written translated at second quarter 2010 rates of exchange would have been \$532.8 million for the six months ended June 30, 2011, giving an effective increase of \$8.5 million or 1.6%. Details of Talbot gross premiums written by line of business are provided below.

|                               | Six Months Ended<br>June 30, 2011 |                                     | Six Months Ended<br>June 30, 2010 |                                     | %<br>Change |
|-------------------------------|-----------------------------------|-------------------------------------|-----------------------------------|-------------------------------------|-------------|
|                               | Gross<br>Premiums<br>Written      | Gross<br>Premiums<br>Written<br>(%) | Gross<br>Premiums<br>Written      | Gross<br>Premiums<br>Written<br>(%) |             |
| <b>(Dollars in thousands)</b> |                                   |                                     |                                   |                                     |             |
| Property                      | \$ 168,461                        | 31.2%                               | \$ 183,404                        | 34.9%                               | (8.1)%      |
| Marine                        | 198,427                           | 36.7%                               | 182,227                           | 34.8%                               | 8.9%        |
| Specialty                     | 173,055                           | 32.1%                               | 158,620                           | 30.3%                               | 9.1%        |
| <b>Total</b>                  | <b>\$ 539,943</b>                 | <b>100.0%</b>                       | <b>\$ 524,251</b>                 | <b>100.0%</b>                       | <b>3.0%</b> |

Talbot gross premiums written decreased across the property lines by \$14.9 million and increased across the marine and specialty lines by, \$16.2 million and \$14.4 million, respectively. The decrease in the property lines is due primarily to a \$10.6 million decrease in premiums written by the onshore energy team and a \$4.7 million decrease in reinstatement premiums in the property treaty lines. The increase in the marine lines is due primarily to a \$17.3 million increase in gross premiums written across the offshore energy, marine liability and hull lines. The increase in the specialty lines is due primarily to a \$14.2 million increase in the war, political risk and violence lines.

**Reinsurance Premiums Ceded**

Reinsurance premiums ceded for the six months ended June 30, 2011 were \$242.2 million compared to \$158.5 million for the six months ended June 30, 2010, an increase of \$83.7 million, or 52.8%. Reinsurance premiums ceded on the property and marine lines increased by \$85.0 million and \$5.1 million, respectively. Reinsurance premiums ceded on the specialty lines decreased by \$6.3 million. Details of reinsurance premiums ceded by line of business are provided below.

|                               | Six Months Ended<br>June 30, 2011 |   | Six Months Ended<br>June 30, 2010 |   | %<br>Change  |
|-------------------------------|-----------------------------------|---|-----------------------------------|---|--------------|
|                               | Reinsurance<br>Premiums<br>Ceded  | Reinsurance<br>Premiums<br>Ceded<br>(%) | Reinsurance<br>Premiums<br>Ceded  | Reinsurance<br>Premiums<br>Ceded<br>(%) |              |
| <b>(Dollars in thousands)</b> |                                   |   |                                   |   |              |
| Property                      | \$ 180,467                        | 74.6%                                   | \$ 95,501                         | 60.3%                                   | 89.0%        |
| Marine                        | 31,600                            | 13.0%                                   | 26,548                            | 16.7%                                   | 19.0%        |
| Specialty                     | 30,099                            | 12.4%                                   | 36,416                            | 23.0%                                   | (17.3)%      |
| <b>Total</b>                  | <b>\$ 242,166</b>                 | <b>100.0%</b>                           | <b>\$ 158,465</b>                 | <b>100.0%</b>                           | <b>52.8%</b> |

*Validus Re.* Validus Re reinsurance premiums ceded for the six months ended June 30, 2011 were \$145.0 million compared to \$54.3 million for the six months ended June 30, 2010, an increase of \$90.7 million, or 167.2%. Details of Validus Re reinsurance premiums ceded by line of business are provided below.

| Six Months Ended<br>June 30, 2011 | Six Months Ended<br>June 30, 2010 |
|-----------------------------------|-----------------------------------|
|-----------------------------------|-----------------------------------|

| <b>(Dollars in thousands)</b> | <b>Reinsurance</b> | <b>Reinsurance</b> | <b>Reinsurance</b> | <b>Reinsurance</b> | <b>%<br/>Change</b> |
|-------------------------------|--------------------|--------------------|--------------------|--------------------|---------------------|
|                               | <b>Premiums</b>    | <b>Premiums</b>    | <b>Premiums</b>    | <b>Premiums</b>    |                     |
|                               | <b>Ceded</b>       | <b>Ceded</b>       | <b>Ceded</b>       | <b>Ceded</b>       |                     |
|                               |                    | <b>(%)</b>         |                    | <b>(%)</b>         |                     |
| Property                      | \$ 132,069         | 91.1%              | \$ 43,275          | 79.7%              | 205.2%              |
| Marine                        | 12,453             | 8.6%               | 11,293             | 20.8%              | 10.3%               |
| Specialty                     | 501                | 0.3%               | (283)              | (0.5)%             | 277.0%              |
| <b>Total</b>                  | <b>\$ 145,023</b>  | <b>100.0%</b>      | <b>\$ 54,285</b>   | <b>100.0%</b>      | <b>167.2%</b>       |

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Reinsurance premiums ceded in the Validus Re property line increased by \$88.8 million due primarily to the purchase of \$89.8 million in additional and replacement retrocessional coverage on the worldwide catastrophe portfolio. The additional US retrocessional coverage was purchased to ensure that the Company would be well positioned to take advantage of opportunities in a post loss environment. Reinsurance premiums ceded on the Validus Re marine and specialty lines have remained generally consistent with the six months ended June 30, 2010.

*Talbot.* Talbot reinsurance premiums ceded for the six months ended June 30, 2011 were \$134.7 million compared to \$165.3 million for the six months ended June 30, 2010, a decrease of \$30.6 million or 18.5%. Details of Talbot reinsurance premiums ceded by line of business are provided below.

|                               | Six Months Ended<br>June 30, 2011 |   | Six Months Ended<br>June 30, 2010 |   | %<br>Change    |
|-------------------------------|-----------------------------------|---|-----------------------------------|---|----------------|
|                               | Reinsurance<br>Premiums<br>Ceded  | Reinsurance<br>Premiums<br>Ceded<br>(%) | Reinsurance<br>Premiums<br>Ceded  | Reinsurance<br>Premiums<br>Ceded<br>(%) |                |
| <b>(Dollars in thousands)</b> |                                   |   |                                   |   |                |
| Property                      | \$ 77,327                         | 57.4%                                   | \$ 92,178                         | 55.8%                                   | (16.1)%        |
| Marine                        | 22,462                            | 16.7%                                   | 29,874                            | 18.1%                                   | (24.8)%        |
| Specialty                     | 34,903                            | 25.9%                                   | 43,207                            | 26.1%                                   | (19.2)%        |
| <b>Total</b>                  | <b>\$ 134,692</b>                 | <b>100.0%</b>                           | <b>\$ 165,259</b>                 | <b>100.0%</b>                           | <b>(18.5)%</b> |

Reinsurance premiums ceded in the Talbot property lines decreased by \$14.9 million for the six months ended June 30, 2011. The decrease was due primarily to a \$12.5 million decrease in premiums ceded in the onshore energy and property treaty lines as a direct result of lower written premiums and a \$4.2 million decrease in reinstatement premiums, partially offset by a \$1.8 million increase in premiums ceded in the property quota share lines. Reinsurance premiums ceded in the Talbot marine lines decreased by \$7.4 million for the six months ended June 30, 2011 primarily due to \$9.9 million decrease in marine treaty premiums ceded, partially offset by an increase of \$2.3 million in reinstatement premiums. Reinsurance premiums ceded in the Talbot specialty lines decreased by \$8.3 million for the six months ended June 30, 2011 due primarily to a \$7.0 million decrease in premiums ceded in the aviation treaty lines due to timing changes on the inception of the program.

**Net Premiums Written**

Net premiums written for the six months ended June 30, 2011 were \$1,213.1 million compared to \$1,229.3 million for the six months ended June 30, 2010, a decrease of \$16.2 million, or 1.3%. The ratios of net premiums written to gross premiums written for the six months ended June 30, 2011 and 2010 were 83.4% and 88.6%, respectively. Details of net premiums written by line of business are provided below.

|                               | Six Months Ended<br>June 30, 2011 |                                   | Six Months Ended<br>June 30, 2010 |                                   | %<br>Change   |
|-------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|---------------|
|                               | Net<br>Premiums<br>Written        | Net<br>Premiums<br>Written<br>(%) | Net<br>Premiums<br>Written        | Net<br>Premiums<br>Written<br>(%) |               |
| <b>(Dollars in thousands)</b> |                                   |                                   |                                   |                                   |               |
| Property                      | \$ 647,441                        | 53.4%                             | \$ 721,927                        | 58.7%                             | (10.3)%       |
| Marine                        | 353,391                           | 29.1%                             | 326,456                           | 26.6%                             | 8.3%          |
| Specialty                     | 212,285                           | 17.5%                             | 180,947                           | 14.7%                             | 17.3%         |
| <b>Total</b>                  | <b>\$ 1,213,117</b>               | <b>100.0%</b>                     | <b>\$ 1,229,330</b>               | <b>100.0%</b>                     | <b>(1.3)%</b> |

*Validus Re.* Validus Re net premiums written for the six months ended June 30, 2011 were \$807.9 million compared to \$870.3 million for the six months ended June 30, 2010, a decrease of \$62.5 million or 7.2%. Details of Validus Re net premiums written by line of business are provided below.



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| (Dollars in thousands) | Six Months Ended<br>June 30, 2011 |                                   | Six Months Ended<br>June 30, 2010 |                                   | %<br>Change   |
|------------------------|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|---------------|
|                        | Net<br>Premiums<br>Written        | Net<br>Premiums<br>Written<br>(%) | Net<br>Premiums<br>Written        | Net<br>Premiums<br>Written<br>(%) |               |
|                        | Property                          | \$ 556,307                        | 68.8%                             | \$ 630,701                        |               |
| Marine                 | 177,426                           | 22.0%                             | 174,103                           | 20.0%                             | 1.9%          |
| Specialty              | 74,133                            | 9.2%                              | 65,534                            | 7.5%                              | 13.1%         |
| <b>Total</b>           | <b>\$ 807,866</b>                 | <b>100.0%</b>                     | <b>\$ 870,338</b>                 | <b>100.0%</b>                     | <b>(7.2)%</b> |

The decrease in Validus Re net premiums written was driven by factors highlighted above in respect of gross premiums written and reinsurance premiums ceded. The ratios of net premiums written to gross premiums written were 84.8% and 94.1% for the six months ended June 30, 2011 and 2010, respectively. This reflects the increase in reinsurance premiums ceded as a result of the purchase of additional and replacement retrocessional coverage as described above.

*Talbot.* Talbot net premiums written for the six months ended June 30, 2011 were \$405.3 million compared to \$359.0 million for the six months ended June 30, 2010, an increase of \$46.3 million or 12.9%. Details of Talbot net premiums written by line of business are provided below.

| (Dollars in thousands) | Six Months Ended<br>June 30, 2011 |                                   | Six Months Ended<br>June 30, 2010 |                                   | %<br>Change  |
|------------------------|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|--------------|
|                        | Net<br>Premiums<br>Written        | Net<br>Premiums<br>Written<br>(%) | Net<br>Premiums<br>Written        | Net<br>Premiums<br>Written<br>(%) |              |
|                        | Property                          | \$ 91,134                         | 22.5%                             | \$ 91,226                         |              |
| Marine                 | 175,965                           | 43.4%                             | 152,353                           | 42.4%                             | 15.5%        |
| Specialty              | 138,152                           | 34.1%                             | 115,413                           | 32.2%                             | 19.7%        |
| <b>Total</b>           | <b>\$ 405,251</b>                 | <b>100.0%</b>                     | <b>\$ 358,992</b>                 | <b>100.0%</b>                     | <b>12.9%</b> |

The increase in Talbot net premiums written was driven by the factors highlighted above in respect of gross premiums written and reinsurance premiums ceded. The ratios of net premiums written to gross premiums written for the six months ended June 30, 2011 and 2010 were 75.1% and 68.5%, respectively, reflecting the lower reinsurance premiums ceded.

**Change in Unearned Premiums**

Change in unearned premiums for the six months ended June 30, 2011 was (\$357.9) million compared to (\$333.7) million for the six months ended June 30, 2010, a change of \$24.3 million or 7.3%.

| (Dollars in thousands) | Six Months<br>Ended<br>June 30, 2011 | Six Months<br>Ended<br>June 30, 2010 | %<br>Change |
|------------------------|--------------------------------------|--------------------------------------|-------------|
|                        | Change in<br>Unearned                | Change in<br>Unearned                |             |
|                        | Premiums                             | Premiums                             |             |
|                        |                                      |                                      |             |

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|                                       |    |                  |    |                  |             |
|---------------------------------------|----|------------------|----|------------------|-------------|
| Change in gross unearned premium      | \$ | (464,256)        | \$ | (460,166)        | 0.9%        |
| Change in prepaid reinsurance premium |    | 106,312          |    | 126,474          | (15.9)%     |
| <b>Net change in unearned premium</b> | \$ | <b>(357,944)</b> | \$ | <b>(333,692)</b> | <b>7.3%</b> |

*Validus Re.* Validus Re's change in unearned premiums for the six months ended June 30, 2011 was (\$322.9) million compared to (\$324.4) million for the six months ended June 30, 2010, a change of \$1.5 million, or 0.5%.

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|                                       | <b>Six Months<br/>Ended<br/>June 30, 2011<br/>Change in<br/>Unearned</b> | <b>Six Months<br/>Ended<br/>June 30, 2010<br/>Change in<br/>Unearned</b> | <b>%<br/>Change</b> |
|---------------------------------------|--|--|---------------------|
| <b>(Dollars in thousands)</b>         | <b>Premiums</b>  | <b>Premiums</b>  |                     |
| Change in gross unearned premium      | \$ (403,255)   | \$ (407,280)   | (1.0)%              |
| Change in prepaid reinsurance premium | 80,376   | 82,904   | (3.0)%              |
| <b>Net change in unearned premium</b> | <b>\$ (322,879)</b>  | <b>\$ (324,376)</b>  | <b>(0.5)%</b>       |

The Validus Re net change in unearned premium for the six months ended June 30, 2011 has remained generally consistent with the six months ended June 30, 2010.

*Talbot.* The Talbot change in unearned premiums for the six months ended June 30, 2011 was (\$35.1) million compared to (\$9.3) million for the six months ended June 30, 2010, a change of \$25.7 million, or 276.4%.

|                                       | <b>Six Months<br/>Ended<br/>June 30, 2011<br/>Change in<br/>Unearned</b> | <b>Six Months<br/>Ended<br/>June 30, 2010<br/>Change in<br/>Unearned</b> | <b>%<br/>Change</b> |
|---------------------------------------|--|--|---------------------|
| <b>(Dollars in thousands)</b>         | <b>Premiums</b>  | <b>Premiums</b>  |                     |
| Change in gross unearned premium      | \$ (61,001)  | \$ (52,886)  | 15.3%               |
| Change in prepaid reinsurance premium | 25,936   | 43,570   | (40.5)%             |
| <b>Net change in unearned premium</b> | <b>\$ (35,065)</b>   | <b>\$ (9,316)</b>  | <b>276.4%</b>       |

The Talbot net change in unearned premium has decreased for the six months ended June 30, 2011 due primarily to a significant decrease in reinsurance premiums ceded, partially offset by an increase in gross written premiums compared to the six months ended June 30, 2010.

**Net Premiums Earned**

Net premiums earned for the six months ended June 30, 2011 were \$855.2 million compared to \$895.6 million for the six months ended June 30, 2010, a decrease of \$40.5 million or 4.5%. The decrease in net premiums earned was driven by decreased premiums earned in the Validus Re segment of \$61.0 million and increased premiums earned in the Talbot segment of \$20.5 million. Details of net premiums earned by line of business are provided below.

|                               | <b>Six Months Ended<br/>June 30, 2011</b> |                                    | <b>Six Months Ended<br/>June 30, 2010</b> |                                    |                     |
|-------------------------------|---|------------------------------------|---|------------------------------------|---------------------|
|                               | <b>Net<br/>Premiums<br/>Earned</b>        | <b>Net<br/>Premiums<br/>Earned</b> | <b>Net<br/>Premiums<br/>Earned</b>        | <b>Net<br/>Premiums<br/>Earned</b> |                     |
| <b>(Dollars in thousands)</b> | <b>Earned</b>                             | <b>(%)</b>                         | <b>Earned</b>                             | <b>(%)</b>                         | <b>%<br/>Change</b> |
| Property                      | \$ 420,337                                | 49.2%                              | \$ 473,082                                | 52.8%                              | (11.1)%             |
| Marine                        | 243,793                                   | 28.5%                              | 215,818                                   | 24.1%                              | 13.0%               |
| Specialty                     | 191,043                                   | 22.3%                              | 206,738                                   | 23.1%                              | (7.6)%              |

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|              |            |        |            |        |        |
|--------------|------------|--------|------------|--------|--------|
| <b>Total</b> | \$ 855,173 | 100.0% | \$ 895,638 | 100.0% | (4.5)% |
|--------------|------------|--------|------------|--------|--------|

*Validus Re.* Validus Re net premiums earned for the six months ended June 30, 2011 were \$485.0 million compared to \$546.0 million for the six months ended June 30, 2010, a decrease of \$61.0 million or 11.2%. Details of Validus Re net premiums earned by line of business are provided below.

|                               | <b>Six Months Ended<br/>June 30, 2011</b> |  | <b>Six Months Ended<br/>June 30, 2010</b> |  | <b>%<br/>Change</b> |
|-------------------------------|---|--|---|--|---------------------|
|                               | <b>Net<br/>Premiums<br/>Earned</b>        | <b>Net<br/>Premiums<br/>Earned<br/>(%)</b> | <b>Net<br/>Premiums<br/>Earned</b>        | <b>Net<br/>Premiums<br/>Earned<br/>(%)</b> |                     |
| <b>(Dollars in thousands)</b> |   |  |   |  |                     |
| Property                      | \$ 343,549                                | 70.8%                                      | \$ 397,887                                | 72.9%                                      | (13.7)%             |
| Marine                        | 100,407                                   | 20.7%                                      | 89,183                                    | 16.3%                                      | 12.6%               |
| Specialty                     | 41,031                                    | 8.5%                                       | 58,892                                    | 10.8%                                      | (30.3)%             |
| <b>Total</b>                  | \$ 484,987                                | 100.0%                                     | \$ 545,962                                | 100.0%                                     | (11.2)%             |

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The decrease in Validus Re net premiums earned is generally consistent with the decrease in net premiums written for the six months ended June 30, 2011.

*Talbot.* Talbot net premiums earned for the six months ended June 30, 2011 were \$370.2 million compared to \$349.7 million for the six months ended June 30, 2010, an increase of \$20.5 million or 5.9%. Details of Talbot net premiums earned by line of business are provided below.

|                               | Six Months Ended<br>June 30, 2011 |                                  | Six Months Ended<br>June 30, 2010 |                                  | %<br>Change |
|-------------------------------|-----------------------------------|----------------------------------|-----------------------------------|----------------------------------|-------------|
|                               | Net<br>Premiums<br>Earned         | Net<br>Premiums<br>Earned<br>(%) | Net<br>Premiums<br>Earned         | Net<br>Premiums<br>Earned<br>(%) |             |
| <b>(Dollars in thousands)</b> |                                   |                                  |                                   |                                  |             |
| Property                      | \$ 76,788                         | 20.8%                            | \$ 75,195                         | 21.5%                            | 2.1%        |
| Marine                        | 143,386                           | 38.7%                            | 126,635                           | 36.2%                            | 13.2%       |
| Specialty                     | 150,012                           | 40.5%                            | 147,846                           | 42.3%                            | 1.5%        |
| <b>Total</b>                  | <b>\$ 370,186</b>                 | <b>100.0%</b>                    | <b>\$ 349,676</b>                 | <b>100.0%</b>                    | <b>5.9%</b> |

The increase in Talbot net premiums earned is due primarily to the increased levels of net premiums written and the reduced levels of reinsurance premiums ceded during the six months ended June 30, 2011 as compared to the six months ended June 30, 2010.

**Losses and Loss Expenses**

Losses and loss expenses for the six months ended June 30, 2011 were \$683.5 million compared to \$673.4 million for the six months ended June 30, 2010, an increase of \$10.1 million or 1.5%. The loss ratios, defined as losses and loss expenses divided by net premiums earned, for the six months ended June 30, 2011 and 2010 were 79.9% and 75.2%, respectively. Details of loss ratios by line of business are provided below.

|                  | Six Months<br>Ended | Six Months<br>Ended | Percentage<br>Point<br>Change |
|------------------|---------------------|---------------------|-------------------------------|
|                  | June 30, 2011       | June 30, 2010       |                               |
| Property         | 95.5%               | 93.8%               | 1.7                           |
| Marine           | 86.2%               | 66.0%               | 20.2                          |
| Specialty        | 37.7%               | 42.2%               | (4.5)                         |
| <b>All lines</b> | <b>79.9%</b>        | <b>75.2%</b>        | <b>4.7</b>                    |

|          |                                |                          | Six Months Ended June 30, |         | Percentage<br>Point<br>Change |
|----------|--------------------------------|--------------------------|---------------------------|---------|-------------------------------|
|          |                                |                          | 2011                      | 2010    |                               |
| Property | current period                 | excluding notable losses | 25.5%                     | 29.9%   | (4.4)                         |
| Property | current period                 | notable losses           | 74.1%                     | 71.5%   | 2.6                           |
| Property | change in prior accident years |                          | (4.1)%                    | (7.6)%  | 3.5                           |
| Property | loss ratio                     |                          | 95.5%                     | 93.8%   | 1.7                           |
| Marine   | current period                 | excluding notable losses | 49.7%                     | 46.0%   | 3.7                           |
| Marine   | current period                 | notable losses           | 42.6%                     | 32.5%   | 10.1                          |
| Marine   | change in prior accident years |                          | (6.1)%                    | (12.5)% | 6.4                           |

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|                  |                   |                          |         |        |       |
|------------------|-------------------|--------------------------|---------|--------|-------|
| Marine           | loss ratio        |                          | 86.2%   | 66.0%  | 20.2  |
| Specialty        | current period    | excluding notable losses | 43.5%   | 44.3%  | (0.8) |
| Specialty        | current period    | notable losses           | 4.7%    | 4.3%   | 0.4   |
| Specialty        | change in prior   | accident years           | (10.5)% | (6.4)% | (4.1) |
| Specialty        | loss ratio        |                          | 37.7%   | 42.2%  | (4.5) |
| All lines        | current period    | excluding notable losses | 36.4%   | 37.1%  | (0.7) |
| All lines        | current period    | notable losses           | 49.6%   | 46.6%  | 3.0   |
| All lines        | change in prior   | accident years           | (6.1)%  | (8.5)% | 2.4   |
| <b>All lines</b> | <b>loss ratio</b> |                          | 79.9%   | 75.2%  | 4.7   |

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*Validus Re.* Validus Re losses and loss expenses for the six months ended June 30, 2011 were \$404.6 million compared to \$472.7 million for the six months ended June 30, 2010, a decrease of \$68.1 million or 14.4%. The loss ratio, defined as losses and loss expenses divided by net premiums earned, was 83.4% and 86.6% for the six months ended June 30, 2011 and 2010, respectively. For the six months ended June 30, 2011, Validus Re incurred \$316.2 million of notable losses, which represented 65.2 percentage points of the Validus Re segment loss ratio, excluding reserve for potential development on notable loss events. For the six months ended June 30, 2010, Validus Re incurred \$356.3 million of notable losses, which represented 65.3 percentage points of the Validus Re segment loss ratio. Validus Re segment loss ratios, excluding prior year development and loss events identified above, for the six months ended June 30, 2011 and 2010 were 23.1% and 26.7%, respectively. Details of loss ratios by line of business and period of occurrence are provided below.

|                  |   | <b>Six Months ended June 30,</b> |              |              |
|------------------|---|----------------------------------|--------------|--------------|
|                  |   | <b>Percentage</b>                |              |              |
|                  |   | <b>Point</b>                     |              |              |
|                  |   | <b>Change</b>                    |              |              |
|                  |   | <b>2011</b>                      | <b>2010</b>  |              |
| Property         | current period excluding notable losses | 18.0%                            | 25.6%        | (7.6)        |
| Property         | current period notable losses           | 71.0%                            | 74.3%        | (3.3)        |
| Property         | change in prior accident years          | (3.6)%                           | (5.5)%       | 1.9          |
| Property         | loss ratio                              | 85.4%                            | 94.4%        | (9.0)        |
| Marine           | current period excluding notable losses | 40.9%                            | 34.4%        | 6.5          |
| Marine           | current period notable losses           | 67.6%                            | 59.7%        | 7.9          |
| Marine           | change in prior accident years          | (4.4)%                           | (8.6)%       | 4.2          |
| Marine           | loss ratio                              | 104.1%                           | 85.5%        | 18.6         |
| Specialty        | current period excluding notable losses | 21.6%                            | 22.4%        | (0.7)        |
| Specialty        | current period notable losses           | 11.0%                            | 12.7%        | (1.8)        |
| Specialty        | change in prior accident years          | (16.3)%                          | 0.3%         | (16.6)       |
| Specialty        | loss ratio                              | 16.3%                            | 35.4%        | (19.1)       |
| All lines        | current period excluding notable losses | 23.1%                            | 26.7%        | (3.6)        |
| All lines        | current period notable losses           | 65.2%                            | 65.3%        | (0.1)        |
| All lines        | change in prior accident years          | (4.9)%                           | (5.4)%       | 0.5          |
| <b>All lines</b> | <b>loss ratio</b>                       | <b>83.4%</b>                     | <b>86.6%</b> | <b>(3.2)</b> |

For the six months ended June 30, 2011, the Validus Re property line incurred \$305.9 million related to current year losses and \$12.5 million of favorable development relating to prior accident years. This favorable development is attributable to lower than expected claims development. For the six months ended June 30, 2010, the Validus Re property lines included \$397.5 million related to current year losses and \$21.9 million of favorable development relating to prior accident years. This favorable development was attributable to reduced losses estimated for the Dublin and U.K. flood events and windstorm Kyrill, as well as lower than expected claim development elsewhere.

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For the six months ended June 30, 2011, Validus Re's property line incurred \$243.8 million of notable losses, which represented 71.0 percentage points of the Validus Re property loss ratio, excluding the reserve for potential development on notable loss events. For the six months ended June 30, 2010, Validus Re's property line incurred \$295.6 million of notable losses, which represented 74.3 percentage points of the Validus Re property loss ratio. Validus Re property line loss ratios, excluding prior year development and loss events identified above, for the six months ended June 30, 2011 and 2010 were 18.0% and 25.6%, respectively.

For the six months ended June 30, 2011, the Validus Re marine line incurred \$108.9 million related to current year losses and \$4.4 million of favorable development relating to prior accident years. For the six months ended June 30, 2010, the Validus Re marine lines included \$83.9 million related to current year losses and \$7.6 million of favorable development relating to prior accident years. For the six months ended June 30, 2011, Validus Re marine line incurred \$67.9 million of notable losses, which represented 67.6 percentage points of the Validus Re marine loss ratio, excluding reserve for potential development on notable loss events. For the six months ended June 30, 2010, Validus Re's marine line incurred \$53.2 million of notable losses, which represented 59.7 percentage points of the Validus Re marine loss ratio. Validus Re marine line loss ratios, excluding prior year development and loss events identified above, for the six months ended June 30, 2011 and 2010 were 40.9% and 34.4%, respectively.

For the six months ended June 30, 2011, the Validus Re specialty line incurred \$13.4 million related to current year losses and \$6.7 million of favorable development relating to prior accident years. For the six months ended June 30, 2010, the Validus Re specialty lines included \$20.7 million related to current year losses and \$0.2 million of adverse development relating to prior accident years. For the six months ended June 30, 2011, Validus Re specialty line incurred \$4.5 million of notable losses, which represented 11.0 percentage points of the Validus Re specialty loss ratio, excluding the reserve for potential development on notable loss events. For the six months ended June 30, 2010, the Validus Re specialty line incurred \$7.5 million of notable losses, which represented 12.7 percentage points of the Validus Re specialty loss ratio. Validus Re specialty line loss ratios, excluding prior year development and loss events identified above, for the six months ended June 30, 2011 and 2010 were 21.6% and 22.4%, respectively.

*Talbot.* Talbot losses and loss expenses for the six months ended June 30, 2011 were \$278.9 million compared to \$200.7 million for the six months ended June 30, 2010, an increase of \$78.2 million, or 39.0%. The loss ratio, defined as losses and loss expenses divided by net premiums earned, was 75.3% and 57.4% for the six months ended June 30, 2011 and 2010, respectively. For the six months ended June 30, 2011, Talbot incurred \$307.5 million related to current year losses and \$28.6 million of favorable loss development relating to prior accident years. Favorable loss reserve development benefited the Talbot segment loss ratio by 7.7 percentage points for the six months ended June 30, 2011. For the six months ended June 30, 2010, Talbot incurred \$247.6 million related to current year losses and \$46.9 million of favorable loss development relating to prior accident years. Favorable loss reserve development benefitted the segment loss ratio by 13.4 percentage points for the six months ended June 30, 2010. For the six months ended June 30, 2011, Talbot incurred \$108.2 million of notable losses, which represented 29.2 percentage points of the Talbot segment loss ratio. For the six months ended June 30, 2010, Talbot incurred \$60.8 million of notable losses, which represented 17.4 percentage points of the Talbot segment loss ratio. Talbot loss ratios, excluding prior year development and loss events identified above, for the six months ended June 30, 2011 and 2010 were 53.8% and 53.4%, respectively. Details of loss ratios by line of business and period of occurrence are provided below.

|          |   | <b>Six Months Ended June 30,</b> |             |      |
|----------|---|----------------------------------|-------------|------|
|          |   | <b>Percentage</b>                |             |      |
|          |   | <b>Point</b>                     |             |      |
|          |   | <b>Change</b>                    |             |      |
|          |   | <b>2011</b>                      | <b>2010</b> |      |
| Property | current period excluding notable losses | 58.4%                            | 52.9%       | 5.5  |
| Property | current period notable losses           | 88.3%                            | 56.5%       | 31.8 |
| Property | change in prior accident years          | (6.2)%                           | (18.7)%     | 12.5 |
| Property | loss ratio                              | 140.5%                           | 90.7%       | 49.8 |



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|        |   |        |         |      |
|--------|---|--------|---------|------|
| Marine | current period excluding notable losses | 55.9%  | 54.2%   | 1.7  |
| Marine | current period notable losses           | 25.1%  | 13.4%   | 11.7 |
| Marine | change in prior accident years          | (7.3)% | (15.3)% | 8.0  |
| Marine | loss ratio                              | 73.7%  | 52.3%   | 21.4 |

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|                  |   | <b>Six Months Ended June 30,</b> |             |       |
|------------------|---|----------------------------------|-------------|-------|
|                  |   | <b>Percentage</b>                |             |       |
|                  |   | <b>Point</b>                     |             |       |
|                  |   | <b>Change</b>                    |             |       |
|                  |   | <b>2011</b>                      | <b>2010</b> |       |
| Specialty        | current period excluding notable losses | 49.6%                            | 53.1%       | (3.5) |
| Specialty        | current period notable losses           | 2.9%                             | 0.9%        | 2.0   |
| Specialty        | change in prior accident years          | (8.9)%                           | (9.2)%      | 0.3   |
| Specialty        | loss ratio                              | 43.6%                            | 44.8%       | (1.2) |
| All lines        | current period excluding notable losses | 53.8%                            | 53.4%       | 0.4   |
| All lines        | current period notable losses           | 29.2%                            | 17.4%       | 11.8  |
| All lines        | change in prior accident years          | (7.7)%                           | (13.4)%     | 5.7   |
| <b>All lines</b> | <b>loss ratio</b>                       | 75.3%                            | 57.4%       | 17.9  |

For the six months ended June 30, 2011, the Talbot property line incurred \$112.6 million related to current year losses and \$4.7 million of favorable loss development relating to prior accident years. This favorable development is attributable to lower than expected claims development. For the six months ended June 30, 2010, the Talbot property line included \$82.3 million related to current year losses and \$14.1 million of favorable loss development relating to prior accident years. The prior year favorable development was primarily due to lower than expected claim development on the property facultative and binder accounts, together with favorable development on hurricanes Katrina and Ike. For the six months ended June 30, 2011, the Talbot property line incurred \$67.8 million of notable losses, which represented 88.3 percentage points of the Talbot property line loss ratio. For the six months ended June 30, 2010, the Talbot property line incurred \$42.5 million of notable losses, which represented 56.5 percentage points of the Talbot property line loss ratio. Talbot property line loss ratio, excluding prior year development and the loss events identified above, for the six months ended June 30, 2011 and 2010 were 58.4% and 52.9%, respectively.

For the six months ended June 30, 2011, the Talbot marine line incurred \$116.1 million related to current year losses and \$10.5 million of favorable development relating to prior accident years. This favorable development is attributable to lower than expected claims development. For the six months ended June 30, 2010, the Talbot marine line included \$85.6 million related to current year losses and \$19.4 million of favorable development relating to prior accident years. The prior year favorable development was due to lower than expected attritional loss development mainly on the Hull lines. For the six months ended June 30, 2011, the Talbot marine line incurred \$36.0 million of notable losses, which represented 25.1 percentage points of the Talbot marine line loss ratio. For the six months ended June 30, 2010, the Talbot marine line incurred \$17.0 million of notable loss events, which represented 13.4 percentage points of the Talbot marine loss ratio. Talbot marine line loss ratios, excluding prior year development and the loss events identified above, for the six months ended June 30, 2011 and 2010 were 55.9% and 54.2%, respectively.

For the six months ended June 30, 2011, the Talbot specialty line incurred \$78.8 million relating to current year losses and \$13.4 million due to favorable development on prior accident years. This favorable development is attributable to lower than expected claims development. For the six months ended June 30, 2010, the Talbot specialty line included \$79.8 million relating to current year losses and \$13.5 million due to favorable development on prior accident years. The prior year favorable development was primarily due to lower than expected claims across most of the specialty sub-classes. For the six months ended June 30, 2011, Talbot incurred \$4.4 million of notable losses, which represented 2.9 percentage points of the Talbot specialty line loss ratio. For the six months ended June 30, 2010, the Talbot specialty line incurred \$1.3 million of notable losses, which represented 0.9 percentage points of the Talbot loss ratio. Talbot specialty line loss ratios, excluding prior year development and the loss events identified above, for the six months ended June 30, 2011 and 2010 were 49.6% and 53.1%, respectively.

At June 30, 2011 and 2010, gross and net reserves for losses and loss expenses were estimated using the methodology as outlined in the critical accounting policies and estimates as discussed in Item 7, *Management s*

*Discussion and Analysis of Results of Operations and Financial Condition* in the Company's Annual Report on Form 10-K for the year ended December 31, 2010. The Company did not make any significant changes in the assumptions or methodology used in its reserving process for the six months ended June 30, 2011.

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|                               | <b>As at June 30, 2011</b>                |                     |                      |
|-------------------------------|---|---------------------|----------------------|
|                               | <b>Total Gross Reserve for Losses and</b> |                     |                      |
| <b>(Dollars in thousands)</b> | <b>Gross Case Reserves</b>                | <b>Gross IBNR</b>   | <b>Loss Expenses</b> |
| Property                      | \$ 757,858                                | \$ 556,685          | \$ 1,314,543         |
| Marine                        | 404,886                                   | 372,778             | 777,664              |
| Specialty                     | 236,659                                   | 291,494             | 528,153              |
| <b>Total</b>                  | <b>\$ 1,399,403</b>                       | <b>\$ 1,220,957</b> | <b>\$ 2,620,360</b>  |

|                               | <b>As at June 30, 2011</b>              |                     |                      |
|-------------------------------|---|---------------------|----------------------|
|                               | <b>Total Net Reserve for Losses and</b> |                     |                      |
| <b>(Dollars in thousands)</b> | <b>Net Case Reserves</b>                | <b>Net IBNR</b>     | <b>Loss Expenses</b> |
| Property                      | \$ 544,165                              | \$ 522,391          | \$ 1,066,556         |
| Marine                        | 328,987                                 | 356,046             | 685,033              |
| Specialty                     | 184,767                                 | 244,199             | 428,966              |
| <b>Total</b>                  | <b>\$ 1,057,919</b>                     | <b>\$ 1,122,636</b> | <b>\$ 2,180,555</b>  |

The following table sets forth a reconciliation of gross and net reserves for losses and loss expenses by segment for the six months ended June 30, 2011.

|                                    | <b>Six Months Ended June 30, 2011</b> |               |                     |              |
|------------------------------------|---------------------------------------|---------------|---------------------|--------------|
| <b>(Dollars in thousands)</b>      | <b>Validus Re</b>                     | <b>Talbot</b> | <b>Eliminations</b> | <b>Total</b> |
| Gross reserves at period beginning | \$ 998,165                            | \$ 1,191,548  | \$ (153,740)        | \$ 2,035,973 |
| Losses recoverable                 | (80,219)                              | (356,655)     | 153,740             | (283,134)    |
| Net reserves at period beginning   | 917,946                               | 834,893       |                     | 1,752,839    |
| Incurred losses- current year      | 428,169                               | 307,557       |                     | 735,726      |
| Change in prior accident years     | (23,590)                              | (28,631)      |                     | (52,221)     |
| Incurred losses                    | 404,579                               | 278,926       |                     | 683,505      |
| Foreign exchange                   | 21,624                                | 6,890         |                     | 28,514       |
| Paid losses                        | (150,016)                             | (134,287)     |                     | (284,303)    |
| Net reserves at period end         | 1,194,133                             | 986,422       |                     | 2,180,555    |
| Losses recoverable                 | 182,306                               | 384,268       | (126,769)           | 439,805      |

|                              |              |              |              |              |
|------------------------------|--------------|--------------|--------------|--------------|
| Gross reserves at period end | \$ 1,376,439 | \$ 1,370,690 | \$ (126,769) | \$ 2,620,360 |
|------------------------------|--------------|--------------|--------------|--------------|

The amount of recorded reserves represents management's best estimate of expected losses and loss expenses on premiums earned. For the six months ended June 30, 2011, favorable loss reserve development on prior years totaled \$52.2 million. \$23.6 million of the favorable loss reserve development related to the Validus Re segment and \$28.6 million related to the Talbot segment. Favorable loss reserve development benefitted the Company's loss ratio by 6.1 percentage points for the six months ended June 30, 2011. For the six months ended June 30, 2010, favorable loss reserve development on prior years totaled \$76.3 million. \$29.4 million of the favorable development related to the Validus Re segment and \$46.9 million related to the Talbot segment. This favorable loss reserve development benefitted the Company's loss ratio by 8.5 percentage points.

During the three months ended June 30, 2011, the Company recorded losses of \$43,806 for the Cat 46 tornado, \$31,481 for the Cat 48 tornado and \$15,008 for the Jupiter 1 platform failure. During the six months ended June 30, 2011, in addition to the loss events for the three months ended June 30, 2011, the Company recorded losses of \$169,037 for the Tohoku earthquake, \$52,435 for the Gryphon Alpha mooring failure, \$62,093 for the Christchurch earthquake, \$31,002 for the Brisbane floods and \$19,500 for the CNRL Horizon explosion. For the six months ended June 30, 2011, the Company incurred \$424.4 million of notable losses, which represented 49.6 percentage points of the loss ratio, excluding reserve for potential development on notable loss events, as described below. Net of \$31.7 million in reinstatement premiums, the effect of these events on net income was \$392.7 million.

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During the three months ended June 30, 2010, the Company recorded losses of \$44,101 for the Deepwater Horizon oil spill, \$10,500 for the sinking of the Aban Pearl oil rig, \$7,500 for the Bangkok riots and \$8,390 for the Perth hailstorm. During the six months ended June 30, 2010, in addition to the loss events for the three months ended June 30, 2010, the Company recorded losses of \$317,435 for the Chilean earthquake, \$9,758 for the Xynthia windstorm and \$19,383 for the Melbourne hailstorm. For the six months ended June 30, 2010, the Company incurred \$417.1 million of notable losses which represented 46.6 percentage points of the loss ratio. The Company's loss ratio, excluding prior year development and notable loss events for the six months ended June 30, 2011 and 2010 were 36.4% and 37.1%, respectively.

Management of insurance and reinsurance companies use significant judgment in the estimation of reserves for losses and loss expenses. Given the magnitude of recent loss events and other uncertainties inherent in loss estimation, meaningful uncertainty remains regarding the estimation of recent notable loss events. The Company's actual ultimate net loss may vary materially from estimates. Validus Re ultimate losses for notable loss events are estimated through detailed review of contracts which are identified by the Company as potentially exposed to the specific notable loss event. However, there can be no assurance that the ultimate loss amount estimated for a specific contract will be accurate, or that all contracts with exposure to a specific notable loss event will be identified in a timely manner. Potential losses in excess of the estimated ultimate loss assigned to a contract on the basis of a specific review, or loss amounts from contracts not specifically included in the detailed review are reserved for in the reserve for potential development on notable loss events.

As at December 31, 2010 the reserve for potential development on 2010 events was \$33.4 million. During the six months ended June 30, 2011, \$8.9 million was allocated to the Deepwater Horizon loss. During the first quarter of 2011, the Company incurred \$50.0 million for a reserve for potential development on 2011 notable loss events as compared to a \$19.2 million reserve for potential development on 2010 notable loss events for the three months ended March 31, 2010. During the second quarter of 2011, \$20.1 million and \$20.2 million were allocated to the Tohoku earthquake and Christchurch earthquake, respectively. Therefore the reserve for development on notable loss events as at June 30, 2011 is \$34.2 million.

**Policy Acquisition Costs**

Policy acquisition costs for the six months ended June 30, 2011 were \$155.5 million compared to \$150.3 million for the six months ended June 30, 2010, an increase of \$5.2 million or 3.5%. Policy acquisition costs as a percent of net premiums earned for the six months ended June 30, 2011 and 2010 were 18.2% and 16.8%, respectively. Details of policy acquisition costs by line of business are provided below.

|                        | Six Months Ended<br>June 30, 2011 |                                       |                              | Six Months Ended<br>June 30, 2010 |                                       |  |             |
|------------------------|-----------------------------------|---------------------------------------|------------------------------|-----------------------------------|---------------------------------------|--|-------------|
|                        | Policy<br>Acquisition<br>Costs    | Policy<br>Acquisition<br>Costs<br>(%) | Acquisition<br>Cost<br>Ratio | Policy<br>Acquisition<br>Costs    | Policy<br>Acquisition<br>Costs<br>(%) | Policy<br>Acquisition<br>Cost<br>Ratio | %<br>Change |
| (Dollars in thousands) |                                   |                                       |                              |                                   |                                       |  |             |
| Property               | \$ 59,216                         | 38.0%                                 | 14.1%                        | \$ 67,716                         | 45.0%                                 | 14.3%                                  | (12.6)%     |
| Marine                 | 54,060                            | 34.8%                                 | 22.2%                        | 41,145                            | 27.4%                                 | 19.1%                                  | 31.4%       |
| Specialty              | 42,250                            | 27.2%                                 | 22.1%                        | 41,441                            | 27.6%                                 | 20.0%                                  | 2.0%        |
| <b>Total</b>           | <b>\$ 155,526</b>                 | <b>100.0%</b>                         | <b>18.2%</b>                 | <b>\$ 150,302</b>                 | <b>100.0%</b>                         | <b>16.8%</b>                           | <b>3.5%</b> |

*Validus Re.* Validus Re policy acquisition costs for the six months ended June 30, 2011 were \$75.8 million compared to \$81.5 million for the six months ended June 30, 2010, a decrease of \$5.6 million or 6.9%. Details of Validus Re policy acquisition costs by line of business are provided below.

Six Months Ended

Six Months Ended

|                        | June 30, 2011         |                       |                       | June 30, 2010         |                       |                       | %<br>Change   |
|------------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|---------------|
|                        | Policy<br>Acquisition | Policy<br>Acquisition | Policy<br>Acquisition | Policy<br>Acquisition | Policy<br>Acquisition | Policy<br>Acquisition |               |
| (Dollars in thousands) | Acquisition<br>Costs  | Costs<br>(%)          | Cost<br>Ratio         | Acquisition<br>Costs  | Costs<br>(%)          | Cost<br>Ratio         |               |
| Property               | \$ 48,421             | 63.9%                 | 14.1%                 | \$ 59,440             | 73.0%                 | 14.9%                 | (18.5)%       |
| Marine                 | 20,657                | 27.2%                 | 20.6%                 | 14,516                | 17.8%                 | 16.3%                 | 42.3%         |
| Specialty              | 6,757                 | 8.9%                  | 16.5%                 | 7,526                 | 9.2%                  | 12.8%                 | (10.2)%       |
| <b>Total</b>           | <b>\$ 75,835</b>      | <b>100.0%</b>         | <b>15.6%</b>          | <b>\$ 81,482</b>      | <b>100.0%</b>         | <b>14.9%</b>          | <b>(6.9)%</b> |

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Policy acquisition costs include brokerage, commission and excise tax, are generally driven by contract terms and are normally a set percentage of premiums and are also net of ceding commission income on retrocessions. Items such as ceded premium, earned premium adjustments and reinstatement premiums that are recognized in the period have an effect on policy acquisition costs. Validus Re policy acquisition costs as a percent of net premiums earned for the six months ended June 30, 2011 and 2010 were 15.6% and 14.9%, respectively. The policy acquisition cost ratio in the marine lines increased by 4.3 percentage points due primarily to the largest single contract, by gross written premium, having an acquisition cost ratio of 36% and specialty lines increased by 3.7 percentage points.

*Talbot.* Talbot policy acquisition costs for the six months ended June 30, 2011 were \$79.5 million compared to \$73.6 million for the six months ended June 30, 2010, an increase of \$5.9 million or 8.1%. Details of Talbot policy acquisition costs by line of business are provided below.

| (Dollars in thousands) | Six Months Ended<br>June 30, 2011 |                                       |  | Six Months Ended<br>June 30, 2010 |                                       |  | %<br>Change |
|------------------------|-----------------------------------|---------------------------------------|--|-----------------------------------|---------------------------------------|--|-------------|
|                        | Policy<br>Acquisition<br>Costs    | Policy<br>Acquisition<br>Costs<br>(%) | Policy<br>Acquisition<br>Cost<br>Ratio | Policy<br>Acquisition<br>Costs    | Policy<br>Acquisition<br>Costs<br>(%) | Policy<br>Acquisition<br>Cost<br>Ratio |             |
|                        |                                   |                                       |  |                                   |                                       |  |             |
| Property               | \$ 10,583                         | 13.3%                                 | 13.8%                                  | \$ 12,880                         | 17.5%                                 | 17.1%                                  | (17.8)%     |
| Marine                 | 33,427                            | 42.0%                                 | 23.3%                                  | 26,709                            | 36.3%                                 | 21.1%                                  | 25.2%       |
| Specialty              | 35,513                            | 44.7%                                 | 23.7%                                  | 34,003                            | 46.2%                                 | 23.0%                                  | 4.4%        |
| <b>Total</b>           | <b>\$ 79,523</b>                  | <b>100.0%</b>                         | <b>21.5%</b>                           | <b>\$ 73,592</b>                  | <b>100.0%</b>                         | <b>21.0%</b>                           | <b>8.1%</b> |

The policy acquisition cost ratio in the property lines decreased due primarily to increases in ceded intercompany policy acquisition costs on the property treaty lines. The policy acquisition cost ratio on the marine lines increased due primarily to acquisition cost rate increases in the Hull, Cargo and other treaty lines. Talbot policy acquisition costs as a percent of net premiums earned were 21.5% and 21.0%, respectively, for the six months ended June 30, 2011 and 2010.

**General and Administrative Expenses**

General and administrative expenses for the six months ended June 30, 2011 were \$109.3 million compared to \$105.9 million for the six months ended June 30, 2010, an increase of \$3.4 million or 3.2%. The increase was a result of increased expenses in the Talbot segment, offset by decreases in the Validus Re and Corporate segments.

| (Dollars in thousands)   | Six Months Ended<br>June 30, 2011            |   | Six Months Ended<br>June 30, 2010            |   | %<br>Change |
|--------------------------|--|---|--|---|-------------|
|                          | General<br>and<br>Administrative<br>Expenses | General<br>and<br>Administrative<br>Expenses<br>(%) | General<br>and<br>Administrative<br>Expenses | General<br>and<br>Administrative<br>Expenses<br>(%) |             |
|                          |  |   |  |   |             |
| Validus Re               | \$ 26,115                                    | 23.9%   | \$ 27,295                                    | 25.7%   | (4.3)%      |
| Talbot                   | 63,440                                       | 58.0%   | 50,508                                       | 47.7%   | 25.6%       |
| Corporate & Eliminations | 19,763                                       | 18.1%   | 28,145                                       | 26.6%   | (29.8)%     |
| <b>Total</b>             | <b>\$ 109,318</b>                            | <b>100.0%</b>                                       | <b>\$ 105,948</b>                            | <b>100.0%</b>                                       | <b>3.2%</b> |

General and administrative expenses of \$109.3 million in the six months ended June 30, 2011 represents 12.8 percentage points of the expense ratio. General and administrative expenses include salaries and benefits,



professional fees, rent and office expenses. Share compensation expenses are discussed in the following section. *Validus Re.* Validus Re general and administrative expenses for the six months ended June 30, 2011 were \$26.1 million compared to \$27.3 million for the six months ended June 30, 2010, a decrease of \$1.2 million or 4.3%. General and administrative expenses have remained generally consistent with the six months ended June 30, 2010.

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Validus Re's general and administrative expenses as a percent of net premiums earned for the six months ended June 30, 2011 and 2010 were 5.4% and 5.0%, respectively.

*Talbot.* Talbot general and administrative expenses for the six months ended June 30, 2011 were \$63.4 million compared to \$50.5 million for the six months ended June 30, 2010, an increase of \$12.9 million or 25.6%. To better align the Company's operating and reporting structure with its current strategy, there was an internal reallocation of expenses relating to the New York operations from the Corporate segment to the Talbot segment. For the six months ended June 30, 2011, these expenses amounted to \$3.8 million. Other factors contributing to the increase in general and administrative expenses are a \$5.0 million increase in staff costs as a result of an increase in staff from 241 at June 30, 2010 to 285 at June 30, 2011 and an increase of \$3.2 million in Talbot's syndicate costs. Talbot's general and administrative expenses as a percent of net premiums earned for the six months ended June 30, 2011 and 2010 were 17.1% and 14.4%, respectively.

*Corporate & Eliminations.* Corporate general and administrative expenses for the six months ended June 30, 2011 were \$19.8 million compared to \$28.1 million for the six months ended June 30, 2010, a decrease of \$8.4 million or 29.8%. To better align the Company's operating and reporting structure with its current strategy, there was an internal reallocation of expenses relating to the New York operations from the Corporate segment to the Talbot segment. For the six months ended June 30, 2011, these expenses amounted to \$3.8 million. There was also an allocation of corporate expenses of \$2.2 million to the operating segments relating to group-wide costs. Corporate general and administrative expenses are comprised of executive and board expenses, internal and external audit expenses and other costs relating to the Company as a whole.

**Share Compensation Expenses**

Share compensation expenses for the six months ended June 30, 2011 were \$19.7 million compared to \$13.4 million for the six months ended June 30, 2010, an increase of \$6.3 million or 46.6%. This expense is non-cash and has no net effect on total shareholders' equity, as it is balanced by an increase in additional paid-in capital.

|                               | Six Months Ended<br>June 30, 2011 |  | Six Months Ended<br>June 30, 2010 |  | %<br>Change  |
|-------------------------------|-----------------------------------|--|-----------------------------------|--|--------------|
|                               | Share<br>Compensation<br>Expenses | Share<br>Compensation<br>Expenses<br>(%) | Share<br>Compensation<br>Expenses | Share<br>Compensation<br>Expenses<br>(%) |              |
| <b>(Dollars in thousands)</b> |                                   |  |                                   |  |              |
| Validus Re                    | \$ 4,928                          | 25.1%                                    | \$ 3,378                          | 25.1%                                    | 45.9%        |
| Talbot                        | 4,745                             | 24.1%                                    | 3,027                             | 22.6%                                    | 56.8%        |
| Corporate & Eliminations      | 10,004                            | 50.8%                                    | 7,017                             | 52.3%                                    | 42.6%        |
| <b>Total</b>                  | <b>\$ 19,677</b>                  | <b>100.0%</b>                            | <b>\$ 13,422</b>                  | <b>100.0%</b>                            | <b>46.6%</b> |

Share compensation expenses of \$19.7 million in the six months ended June 30, 2011 represents 2.3 percentage points of the general and administrative expense ratio.

*Validus Re.* Validus Re share compensation expenses for the six months ended June 30, 2011 was \$4.9 million compared to \$3.4 million for the six months ended June 30, 2010, an increase of \$1.6 million or 45.9%. This increase was due primarily to a change in forfeiture rates during the three months ended March 31, 2011, resulting in an increase of \$1.2 million in share compensation expenses in the segment primarily relating to restricted share awards. Share compensation expenses as a percent of net premiums earned for the six months ended June 30, 2011 and 2010 were 1.0% and 0.6%, respectively.

*Talbot.* Talbot share compensation expenses for the six months ended June 30, 2011 was \$4.7 million compared to \$3.0 million for the six months ended June 30, 2010, an increase of \$1.7 million or 56.8%. This increase was due primarily to a change in forfeiture rates during the three months ended March 31, 2011, resulting in an increase of \$0.5 million in share compensation expenses in the segment primarily relating to restricted share awards. Share compensation expenses as a percent of net premiums earned for the six months ended June 30, 2011 and 2010 were

1.3% and 0.9%, respectively.

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*Corporate & Eliminations.* Corporate share compensation expenses for the six months ended June 30, 2011 was \$10.0 million compared to \$7.0 million for the six months ended June 30, 2010, an increase of \$3.0 million or 42.6%, due primarily to a change in forfeiture rates during the three months ended March 31, 2011, resulting in an increase of \$2.3 million in share compensation expenses in the segment primarily relating to restricted share awards.

**Selected Ratios**

The underwriting results of an insurance or reinsurance company are often measured by reference to its combined ratio, which is the sum of the loss ratio and the expense ratio. The net loss ratio is calculated by dividing losses and loss expenses incurred (including estimates for incurred but not reported losses) by net premiums earned. The expense ratio is calculated by dividing acquisition costs combined with general and administrative expenses by net premiums earned. The following table presents the losses and loss expenses ratio, policy acquisition cost ratio, general and administrative expense ratio, expense ratio and combined ratio for the six months ended June 30, 2011 and 2010.

|   | <b>Six Months<br/>Ended</b> | <b>Six Months<br/>Ended</b> | <b>Percentage<br/>point<br/>change</b> |
|---|-----------------------------|-----------------------------|--|
|   | <b>June 30, 2011</b>        | <b>June 30, 2010</b>        |  |
| Losses and loss expenses ratio                | 79.9%                       | 75.2%                       | 4.7                                    |
| Policy acquisition costs ratio                | 18.2%                       | 16.8%                       | 1.4                                    |
| General and administrative expenses ratio (a) | 15.1%                       | 13.3%                       | 1.8                                    |
| <b>Expense ratio</b>                          | <b>33.3%</b>                | <b>30.1%</b>                | <b>3.2</b>                             |
| <b>Combined ratio</b>                         | <b>113.2%</b>               | <b>105.3%</b>               | <b>7.9</b>                             |

|   | <b>Six Months<br/>Ended</b> | <b>Six Months<br/>Ended</b> | <b>Percentage<br/>point<br/>change</b> |
|---|-----------------------------|-----------------------------|--|
|   | <b>June 30, 2011</b>        | <b>June 30, 2010</b>        |  |
| <i>Validus Re</i>                             |                             |                             |  |
| Losses and loss expenses ratio                | 83.4%                       | 86.6%                       | (3.2)                                  |
| Policy acquisition costs ratio                | 15.6%                       | 14.9%                       | 0.7                                    |
| General and administrative expenses ratio (a) | 6.4%                        | 5.6%                        | 0.8                                    |
| <b>Expense ratio</b>                          | <b>22.0%</b>                | <b>20.5%</b>                | <b>1.5</b>                             |
| <b>Combined ratio</b>                         | <b>105.4%</b>               | <b>107.1%</b>               | <b>(1.7)</b>                           |

|   | <b>Six Months<br/>Ended</b> | <b>Six Months<br/>Ended</b> | <b>Percentage<br/>point<br/>change</b> |
|---|-----------------------------|-----------------------------|--|
|   | <b>June 30, 2011</b>        | <b>June 30, 2010</b>        |  |
| <i>Talbot</i>                                 |                             |                             |  |
| Losses and loss expenses ratio                | 75.3%                       | 57.4%                       | 17.9                                   |
| Policy acquisition costs ratio                | 21.5%                       | 21.0%                       | 0.5                                    |
| General and administrative expenses ratio (a) | 18.4%                       | 15.3%                       | 3.1                                    |
| <b>Expense ratio</b>                          | <b>39.9%</b>                | <b>36.3%</b>                | <b>3.6</b>                             |
| <b>Combined ratio</b>                         | <b>115.2%</b>               | <b>93.7%</b>                | <b>21.5</b>                            |

(a) Includes general and administrative expenses and share compensation expenses.

General and administrative expense ratios for the six months ended June 30, 2011 and 2010 were 15.1% and 13.3%, respectively. General and administrative expense ratio is the sum of general and administrative expenses and share compensation expense divided by net premiums earned.

| (Dollars in thousands)              | Six Months Ended<br>June 30, 2011 |   | Six Months Ended<br>June 30, 2010 |   |
|-------------------------------------|-----------------------------------|---|-----------------------------------|---|
|                                     | Expenses                          | Expenses as %<br>of Net<br>Earned<br>Premiums | Expenses                          | Expenses as %<br>of Net<br>Earned<br>Premiums |
| General and administrative expenses | \$ 109,318                        | 12.8%   | \$ 105,948                        | 11.8%   |
| Share compensation expenses         | 19,677                            | 2.3%  | 13,422                            | 1.5%  |
| <b>Total</b>                        | <b>\$ 128,995</b>                 | <b>15.1%</b>                                  | <b>\$ 119,370</b>                 | <b>13.3%</b>                                  |

**Table of Contents****Underwriting (Loss)**

Underwriting (loss) for the six months ended June 30, 2011 was (\$112.9) million compared to (\$47.5) million for the six months ended June 30, 2010, an increase of \$65.4 million or 137.8%.

| <b>(Dollars in thousands)</b> | <b>Six Months<br/>Ended June<br/>30, 2011</b> | <b>% of<br/>Sub-total</b> | <b>Six Months<br/>Ended<br/>June 30,<br/>2010</b> | <b>% of<br/>Sub-total</b> | <b>%<br/>Change</b> |
|-------------------------------|---|---------------------------|---|---------------------------|---------------------|
| Validus Re                    | \$ (26,470)                                   | 31.9%                     | \$ (38,906)                                       | 227.9%                    | 32.0%               |
| Talbot                        | (56,448)                                      | 68.1%                     | 21,837  | (127.9)%                  | (358.5)%            |
| Sub total                     | (82,918)                                      | 100.0%                    | (17,069)  | 100.0%                    | (385.8)%            |
| Corporate & Eliminations      | (29,935)                                      |                           | (30,390)  |                           | 1.5%                |
| <b>Total</b>                  | <b>\$ (112,853)</b>                           |                           | <b>\$ (47,459)</b>                                |                           | <b>(137.8)%</b>     |

The underwriting results of an insurance or reinsurance company are also often measured by reference to its underwriting income, which is a non-GAAP measure as previously defined. Underwriting income, as set in the table below, is reconciled to net income (the most directly comparable GAAP financial measure) by the addition or subtraction of certain Consolidated Statement of Operations and Comprehensive Income line items, as illustrated below.

| <b>(Dollars in thousands)</b>         | <b>Six Months<br/>Ended<br/>June 30, 2011</b> | <b>Six Months<br/>Ended<br/>June 30, 2010</b> |
|---------------------------------------|---|---|
| <b>Underwriting (loss)</b>            | <b>\$ (112,853)</b>                           | <b>\$ (47,459)</b>                            |
| Net investment income                 | 56,469  | 69,108  |
| Other income                          | 2,201   | 3,585   |
| Finance expenses                      | (30,362)                                      | (28,369)                                      |
| Net realized gains on investments     | 17,931  | 23,839  |
| Net unrealized gains on investments   | 5,698   | 57,053  |
| Foreign exchange (losses)             | (2,458)                                       | (12,863)                                      |
| <b>Net (loss) income before taxes</b> | <b>\$ (63,374)</b>                            | <b>\$ 64,894</b>                              |

Underwriting income indicates the performance of the Company's core underwriting function, excluding revenues and expenses such as the reconciling items in the table above. The Company believes the reporting of underwriting income enhances the understanding of our results by highlighting the underlying profitability of the Company's core insurance and reinsurance business. Underwriting profitability is influenced significantly by earned premium growth, adequacy of the Company's pricing and loss frequency and severity. Underwriting profitability over time is also influenced by the Company's underwriting discipline, which seeks to manage exposure to loss through favorable risk selection and diversification, its management of claims, its use of reinsurance and its ability to manage its expense ratio, which it accomplishes through its management of acquisition costs and other underwriting expenses. The Company believes that underwriting income provides investors with a valuable measure of profitability derived from underwriting activities.

The Company excludes the U.S. GAAP measures noted above, in particular net realized and unrealized gains and losses on investments, from its calculation of underwriting income because the amount of these gains and losses is heavily influenced by, and fluctuates in part, according to availability of investment market opportunities. The

Company believes these amounts are largely independent of its underwriting business and including them distorts the analysis of trends in its operations.

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In addition to presenting net income determined in accordance with U.S. GAAP, the Company believes that showing underwriting income enables investors, analysts, rating agencies and other users of its financial information to more easily analyze the Company's results of operations in a manner similar to how management analyzes the Company's underlying business performance. The Company uses underwriting income as a primary measure of underwriting results in its analysis of historical financial information and when performing its budgeting and forecasting processes. Analysts, investors and rating agencies who follow the Company request this non-GAAP financial information on a regular basis. In addition, underwriting income is one of the factors considered by the compensation committee of our Board of Directors in determining the bonus component of the total annual incentive compensation.

Underwriting income should not be viewed as a substitute for U.S. GAAP net income as there are inherent material limitations associated with the use of underwriting income as compared to using net income, which is the most directly comparable U.S. GAAP financial measure. The most significant limitation is the ability of users of the financial information to make comparable assessments of underwriting income with other companies, particularly as underwriting income may be defined or calculated differently by other companies. Therefore, the Company provides more prominence in this filing to the use of the most comparable U.S. GAAP financial measure, net income, which includes the reconciling items in the table above. The Company compensates for these limitations by providing both clear and transparent disclosure of net income and reconciliation of underwriting income to net income.

**Net Investment Income**

Net investment income for the six months ended June 30, 2011 was \$56.5 million compared to \$69.1 million for the six months ended June 30, 2010, a decrease of \$12.6 million or 18.3%. Net investment income decreased due to falling yields on fixed maturity investments. Net investment income includes accretion of premium or discount on fixed maturities, interest on coupon-paying bonds, short-term investments and cash and cash equivalents, partially offset by investment management fees. The components of net investment income for the six months ended June 30, 2011 and 2010 are provided below.

|   | <b>Six Months<br/>Ended</b> | <b>Six Months<br/>Ended</b> | <b>%<br/>Change</b> |
|---|-----------------------------|-----------------------------|---------------------|
| <b>(Dollars in thousands)</b>               | <b>June 30, 2011</b>        | <b>June 30, 2010</b>        |                     |
| Fixed maturities and short-term investments | \$ 56,470                   | \$ 72,101                   | (21.7)%             |
| Fixed maturities and short-term investments | 3,268                       | 897                         | 264.3%              |
| Cash and cash equivalents                   | 24                          | 119                         | (79.8)%             |
| <b>Total investment income</b>              | <b>59,762</b>               | <b>73,117</b>               | <b>(18.3)%</b>      |
| Investment expenses                         | (3,293)                     | (4,009)                     | (17.9)%             |
| <b>Net investment income</b>                | <b>\$ 56,469</b>            | <b>\$ 69,108</b>            | <b>(18.3)%</b>      |

Annualized effective investment yield is based on the weighted average investments held calculated on a simple period average and excludes net unrealized gains (losses), realized gains (losses) on investments, foreign exchange gains (losses) on investments and the foreign exchange effect of insurance balances. The Company's annualized effective investment yield was 1.90% and 2.36% for the six months ended June 30, 2011 and 2010, respectively and the average duration at June 30, 2011 was 1.57 years (December 31, 2010: 2.27 years).

**Other Income**

Other income for the six months ended June 30, 2011 was \$2.2 million compared to \$3.6 million for the six months ended June 30, 2010, a decrease of \$1.4 million or 38.6%.

**Finance Expenses**

Finance expenses for the six months ended June 30, 2011 were \$30.4 million compared to \$28.4 million for the six months ended June 30, 2010, an increase of \$2.0 million or 7.0%. Finance expenses also include the amortization of debt offering costs and discounts, and fees related to our credit facilities.





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| (Dollars in thousands)                           | Six Months Ended June 30,<br>2011 |                  |             |
|--|-----------------------------------|------------------|-------------|
|  | 2011                              | 2010             | %<br>Change |
| 9.069% Junior Subordinated Deferrable Debentures | \$ 6,816                          | \$ 7,177         | (5.0)%      |
| 8.480% Junior Subordinated Deferrable Debentures | 6,057                             | 6,057            | 0.0%        |
| 2010 Senior Notes due 2040                       | 11,194                            | 9,575            | 16.9%       |
| Credit facilities                                | 3,313                             | 2,420            | 36.9%       |
| AlphaCat Re 2011 fees (a)                        | 2,919                             |                  | NM          |
| Talbot FAL Facility                              | 63                                | 333              | (81.1)%     |
| Talbot other interest                            |                                   | 59               | NM          |
| Talbot third party FAL facility                  |                                   | 2,748            | NM          |
| <b>Finance expenses</b>                          | <b>\$ 30,362</b>                  | <b>\$ 28,369</b> | <b>7.0%</b> |

(a) Includes finance expenses attributable to noncontrolling interest.

NM: Not Meaningful

Capital in Lloyd's entities, whether personal or corporate, is required to be set annually for the prospective year and held by Lloyd's in trust (Funds at Lloyd's or FAL). For underwriting years up to and including 2007, Talbot's FAL has been provided both by Talbot and by third parties, thereafter Talbot's FAL has been provided exclusively by the Company. As all of the underwriting years up to and including 2007 are closed with effect from December 31, 2009, the FAL relating to these years has been returned to the third party providers. There were some costs paid in 2010, which are the final amounts payable under the Talbot third party FAL facility.

**Tax Benefit (Expense)**

Tax benefit for the six months ended June 30, 2011 was \$1.5 million compared to an expense of (\$3.5) million for the six months ended June 30, 2010, a change of \$5.0 million or 142.6%. For the six months ended June 30, 2011, the Talbot tax benefit arose primarily due to a reduction in the U.K. taxable profits and adjustments to deferred tax balances following a reduction in the effective U.K. tax rate from 28% to 26.5%.

**Net Realized Gains on Investments**

Net realized gains on investments for the six months ended June 30, 2011 were \$17.9 million compared to \$23.8 million for the six months ended June 30, 2010, a decrease of \$5.9 million or 24.8%.

**Net Unrealized Gains on Investments**

Net unrealized gains on investments for the six months ended June 30, 2011 were \$5.7 million compared to \$57.1 million for the six months ended June 30, 2010, a decrease of \$51.4 million or 90.0%. The net unrealized gains in the six months ended June 30, 2011 were partially as a result of downward shift in rates as the two-year Treasury rate fell from 0.59% to 0.46% (13 bps) and the five-year rate decreased from 2.01% to 1.76% (25 bps) in the period.

Net unrealized gains on investments are recorded as a component of net income. The Company has adopted all authoritative guidance on U.S. GAAP fair value measurements in effect as of the balance sheet date. Consistent with these standards, certain market conditions allow for fair value measurements that incorporate unobservable inputs where active market transaction based measurements are unavailable. Certain non-Agency RMBS securities were previously identified as trading in inactive markets.

**Foreign Exchange (Losses)**

Foreign exchange losses for the six months ended June 30, 2011 were (\$2.5) million compared to (\$12.9) million for the six months ended June 30, 2010, a favorable movement of \$10.4 million or 80.9%. The favorable movement in foreign exchange resulted primarily from the effect of the appreciation of the Euro and British pound sterling against the U.S. dollar on assets held in these foreign currencies.



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The Euro to U.S. dollar exchange rates were 1.33 and 1.44 at December 31, 2010 and June 30, 2011, respectively. The British pound sterling to U.S. dollar exchange rates were 1.55 and 1.60 at December 31, 2010 and June 30, 2011, respectively. During the six months ended June 30, 2011, the Euro appreciated by 8.3% and the British pound sterling appreciated by 3.2%. For the six months ended June 30, 2011, Validus Re recognized foreign exchange losses of (\$9.7) million and Talbot recognized foreign exchange gains of \$7.3 million.

For the six months ended June 30, 2011, the Validus Re segment foreign exchange losses were (\$9.7) million compared to losses of (\$6.0) million for the six months ended June 30, 2010, an unfavorable movement of \$3.7 million or 62.1%. The unfavorable movement in Validus Re foreign exchange losses was due primarily to a (\$5.3) million loss incurred as a result of the Company having liabilities in both New Zealand dollars and Japanese Yen during a period when both of these currencies strengthened against the U.S. dollar.

For the six months ended June 30, 2011, the Talbot segment foreign exchange gains were \$7.3 million compared to losses of (\$6.8) million for the six months ended June 30, 2010, a favorable movement of \$14.2 million or 206.9%. This increase was due primarily to gains of \$4.2 million on revaluation of funds held in Euros due to the strengthening of the Euro, compared to losses on revaluation of (\$3.7) million in the six months ended June 30, 2010. Certain premiums receivable and liabilities for losses incurred in currencies other than the U.S. dollar are exposed to the risk of changes in value resulting from fluctuations in foreign exchange rates and may affect financial results in the future.

At June 30, 2011, Talbot's balance sheet includes net unearned premiums and deferred acquisition costs denominated in foreign currencies of approximately \$103.7 million and \$21.6 million, respectively. These balances consisted of British pounds sterling and Canadian dollars of \$73.0 million and \$9.1 million, respectively. Net unearned premiums and deferred acquisition costs are classified as non-monetary items and are translated at historic exchange rates. All of Talbot's other balance sheet items are classified as monetary items and are translated at period end exchange rates. Additional foreign exchange (losses) gains may be incurred on the translation of net unearned premiums and deferred acquisition costs arising from insurance and reinsurance premiums written in future periods.

**Net Income Attributable to Noncontrolling Interest**

On May 25, 2011, the Company joined with other investors in capitalizing AlphaCat Re 2011, a new special purpose sidecar reinsurer formed for the purpose of writing collateralized reinsurance and retrocessional reinsurance. Validus Re has an equity interest in AlphaCat Re 2011 and as Validus Re holds a majority of AlphaCat Re 2011's outstanding voting rights, the financial statements of AlphaCat Re 2011 are included in the consolidated financial statements of the Company. The portion of AlphaCat Re 2011's earnings attributable to third party investors for the three months ended June 30, 2011 is recorded in the consolidated statement of operations and comprehensive income as net income attributable to noncontrolling interest.

**Other Non-GAAP Financial Measures**

In presenting the Company's results, management has included and discussed certain schedules containing net operating income, underwriting income (loss), annualized return on average equity and diluted book value per common share that are not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. The calculation of annualized return on average equity is discussed in the section above entitled Financial Measures. A reconciliation of underwriting income to net income, the most comparable U.S. GAAP financial measure, is presented above in the section entitled Underwriting Income. A reconciliation of diluted book value per share to book value per share, the most comparable U.S. GAAP financial measure, is presented below. Operating income is calculated based on net income (loss) excluding net realized gains (losses), net unrealized gains (losses) on investments, gains (losses) arising from translation of non-US\$ denominated balances and non-recurring items. A reconciliation of operating income to net income, the most comparable U.S. GAAP financial measure, is embedded in the table presenting results of operations for the six months ended June 30, 2011 and 2010 in the section above entitled Results of Operations.

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Realized gains (losses) from the sale of investments are driven by the timing of the disposition of investments, not by our operating performance. Gains (losses) arising from translation of non-US dollar denominated balances are unrelated to our underlying business.

The following tables present reconciliations of diluted book value per share to book value per share, the most comparable U.S. GAAP financial measure, at June 30, 2011 and December 31, 2010.

|  |  | <b>As at June 30, 2011<br/>(unaudited)</b> |                    |                           |                                     |
|--|--|--|--------------------|---------------------------|-------------------------------------|
|  |  | <b>Equity<br/>Amount</b>                   | <b>Shares</b>      | <b>Exercise<br/>Price</b> | <b>Book Value<br/>Per<br/>Share</b> |
| <b>Book value per common share</b>             |  |  |                    |                           |                                     |
| Total shareholders equity available to Validus |  | \$ 3,408,317                               | 98,763,928         |                           | \$ 34.51                            |
| <b>Diluted book value per common share</b>     |  |  |                    |                           |                                     |
| Total shareholders equity available to Validus |  | 3,408,317                                  | 98,763,928         |                           |                                     |
| Assumed exercise of outstanding warrants       |  | 137,992                                    | 7,862,262          | \$ 17.55                  |                                     |
| Assumed exercise of outstanding stock options  |  | 45,604                                     | 2,266,801          | \$ 20.12                  |                                     |
| Unvested restricted shares                     |  |  | 3,670,942          |                           |                                     |
| <b>Diluted book value per common share</b>     |  | <b>\$ 3,591,913</b>                        | <b>112,563,933</b> |                           | <b>\$ 31.91</b>                     |

|  |  | <b>As at December 31, 2010</b> |                    |                           |                                     |
|--|--|--------------------------------|--------------------|---------------------------|-------------------------------------|
|  |  | <b>Equity<br/>Amount</b>       | <b>Shares</b>      | <b>Exercise<br/>Price</b> | <b>Book<br/>Value<br/>Per Share</b> |
| <b>Book value per common share</b>             |  |                                |                    |                           |                                     |
| Total shareholders equity available to Validus |  | \$ 3,504,831                   | 98,001,226         |                           | \$ 35.76                            |
| <b>Diluted book value per common share</b>     |  |                                |                    |                           |                                     |
| Total shareholders equity available to Validus |  | 3,504,831                      | 98,001,226         |                           |                                     |
| Assumed exercise of outstanding warrants       |  | 139,272                        | 7,934,860          | \$ 17.55                  |                                     |
| Assumed exercise of outstanding stock options  |  | 54,997                         | 2,723,684          | \$ 20.19                  |                                     |
| Unvested restricted shares                     |  |                                | 3,496,096          |                           |                                     |
| <b>Diluted book value per common share</b>     |  | <b>\$ 3,699,100</b>            | <b>112,155,866</b> |                           | <b>\$ 32.98</b>                     |

**Financial Condition and Liquidity**

Validus Holdings, Ltd. is a holding company and conducts no operations of its own. The Company relies primarily on cash dividends and other permitted payments from Validus Re and Talbot to pay finance expenses and other holding company expenses. There are restrictions on the payment of dividends from Validus Re and Talbot to the

Company. Please refer to Part II, Item 5, Market for Registrants, Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities in the Company's Annual Report on Form 10-K for the year ended December 31, 2010 for further discussion of the Company's dividend policy.

Three main sources provide cash flows for the Company: operating activities, investing activities and financing activities. Cash flow from operating activities is derived primarily from the net receipt of premiums less claims and expenses related to underwriting activities. Cash flow from investing activities is derived primarily from the receipt of net proceeds on the Company's total investment portfolio. Cash flow from financing activities is derived primarily from the issuance of common shares and debentures payable. The movement in net cash provided by operating activities, net cash (used in) provided by investing activities, net cash provided by (used in) financing activities and the effect of foreign currency rate changes on cash and cash equivalents for the six months ended June 30, 2011 and 2010 is provided in the following table.

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| (Dollars in thousands)   | Six Months Ended June 30, |                   |              |
|--|---------------------------|-------------------|--------------|
|  | 2011                      | 2010              | %            |
| Net cash provided by operating activities                            | \$ 309,614                | \$ 263,582        | 17.5%        |
| Net cash (used in) provided by investing activities                  | (211,059)                 | 101,434           | (308.1)%     |
| Net cash provided by (used in) financing activities                  | 79,584                    | (243,398)         | 132.7%       |
| Effect of foreign currency rate changes on cash and cash equivalents | 17,042                    | (16,714)          | 202.0%       |
| <b>Net increase in cash</b>  | <b>\$ 195,181</b>         | <b>\$ 104,904</b> | <b>86.1%</b> |

During the six months ended June 30, 2011, net cash provided by operating activities of \$309.6 million was driven primarily by a significant portion of the 2011 incurred losses which have yet to be paid. Net cash used in investing activities of \$211.1 million was driven primarily by a net purchase of investments of \$212.0 million. Net cash provided by financing activities of \$79.6 million was driven primarily by \$134.3 million of third party investment in AlphaCat Re 2011, partially offset by the payment of \$54.0 million of quarterly dividends.

During the six months ended June 30, 2010, net cash provided by operating activities of \$263.6 million was driven primarily by a \$452.5 million change in unearned premiums relating to increased premiums written following the IPC acquisition. In addition, there was an increase of \$367.8 million in reserve for losses and loss expenses primarily due to the increase in notable loss events in the six months ended June 30, 2010 and a \$61.4 million contribution from net income in the six months ended June 30, 2010. These amounts were partially offset by an increase of \$383.7 million in premiums receivable and a combined \$166.2 million decrease in deferred acquisition costs and prepaid reinsurance premiums. Net cash provided by investing activities of \$101.4 million was driven primarily by the net sales of short term investments. Net cash used in financing activities of \$243.4 million was driven primarily by the purchase of \$444.0 million of common shares under the share repurchase program and the payment of \$56.0 million in quarterly dividend, partially offset by the issuance of \$246.8 million of 8.875% Senior Notes due 2040.

As at June 30, 2011, the Company's portfolio was composed of fixed income investments including; short-term investments, agency securities and sovereign securities amounting to \$5,347.5 million or 86.8% of total cash and investments. Details of the Company's debt and financing arrangements at June 30, 2011 are provided below.

| (Dollars in thousands)                                   | Maturity Date /<br>Term | In Use/<br>Outstanding |
|--|-------------------------|------------------------|
| 2006 Junior Subordinated Deferrable Debentures           | June 15, 2036           | \$ 150,000             |
| 2007 Junior Subordinated Deferrable Debentures           | June 15, 2037           | 139,800                |
| 2010 Senior Notes due 2040                               | January 26, 2040        | 250,000                |
| \$340,000 syndicated unsecured letter of credit facility | March 12, 2013          |                        |
| \$60,000 bilateral unsecured letter of credit facility   | March 12, 2013          |                        |
| \$500,000 secured letter of credit facility              | March 12, 2012          | 277,679                |
| Talbot FAL facility                                      | April 13, 2011          | 25,000                 |
| IPC Bi-Lateral Facility                                  | December 31,<br>2010    | 63,284                 |
| <b>Total</b>   |                         | <b>\$ 905,763</b>      |

**Capital Resources**

Shareholders' equity at June 30, 2011 was \$3,408.3 million.

On February 9, 2011, the Company announced that its Board of Directors (the Board) had increased the Company's annual dividend by 13.6% from \$0.88 to \$1.00 per common share and common share equivalent for which each

outstanding warrant is exercisable.



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On May 4, 2011, the Company announced a quarterly cash dividend of \$0.25 per common share and \$0.25 per common share equivalent for which each outstanding warrant is exercisable, payable on June 30, 2011 to holders of record on June 5, 2011.

On August 3, 2011 the Company announced a quarterly cash dividend of \$0.25 per common share and \$0.25 per common share equivalent for which each outstanding warrant is exercisable, payable on September 30, 2011 to holders of record on September 15, 2011.

The timing and amount of any future cash dividends, however, will be at the discretion of the Board and will depend upon our results of operations and cash flows, our financial position and capital requirements, general business conditions, legal, tax, regulatory, rating agency and contractual constraints or restrictions and any other factors that the Board deems relevant.

The Company may from time to time repurchase its securities, including common shares, Junior Subordinated Deferrable Debentures and Senior Notes. In November 2009, the Board of Directors of the Company authorized an initial \$400.0 million share repurchase program. On February 17, 2010, the Board of Directors of the Company authorized the Company to return up to \$750.0 million to shareholders. This amount was in addition to, and in excess of, the \$135.5 million of common shares purchased by the Company through February 17, 2010 under its previously authorized \$400.0 million share repurchase program. On May 6, 2010, the Board of Directors authorized a self tender offer pursuant to which the Company has repurchased \$300.0 million in common shares. On November 4, 2010, the Board of Directors authorized a self tender offer pursuant to which the Company has repurchased \$238.4 million in common shares. In addition, the Board of Directors authorized separate repurchase agreements with funds affiliated with or managed by each of Aquiline Capital Partners LLC, New Mountain Capital LLC, and Vestar Capital Partners pursuant to which the Company has repurchased \$61.6 million in common shares. On December 20, 2010, the Board of Directors authorized the Company to return up to \$400.0 million to shareholders. This amount is in addition to the \$929.2 million of common shares purchased by the Company through December 23, 2010 under its previously authorized share repurchase program.

The Company expects the purchases under its share repurchase program to be made from time to time in the open market or in privately negotiated transactions. The timing, form and amount of the share repurchases under the program will depend on a variety of factors, including market conditions, the Company's capital position relative to internal and rating agency targets, legal requirements and other factors. The repurchase program may be modified, extended or terminated by the Board of Directors at any time.

The Company repurchased 35.0 million shares at a cost of \$947.2 million under the share repurchase programs for the period November 4, 2009 through August 4, 2011.

On August 7, 2008, the Company filed a shelf registration statement on Form S-3 (No. 333-152856) with the U.S Securities Exchange Committee in which we may offer from time to time common shares, preference shares, depository shares representing common shares or preference shares, senior or subordinated debt securities, warrants to purchase common shares, preference shares and debt securities, share purchase contracts, share purchase units and units which may consist of any combination of the securities listed above. In addition, the shelf registration statement will provide for secondary sales of common shares sold by the Company's shareholders. The registration statement is intended to provide the Company with additional flexibility to access capital markets for general corporate purposes, subject to market conditions and the Company's capital needs.

On May 25, 2011, the Company joined with other investors in capitalizing AlphaCat Re 2011, a new special purpose sidecar reinsurer formed for the purpose of writing collateralized reinsurance and retrocessional reinsurance. Validus Re has an equity interest in AlphaCat Re 2011 and as Validus Re holds a majority of AlphaCat Re 2011's outstanding voting rights, the financial statements of AlphaCat Re 2011 are included in the consolidated financial statements of the Company. The portion of AlphaCat Re 2011's earnings attributable to third party investors for the three months ended June 30, 2011 is recorded in the consolidated statement of operations and comprehensive income as net income attributable to noncontrolling interest.

The following table details the capital resources of the Company's more significant subsidiaries on an unconsolidated basis.



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| <b>(Dollars in thousands)</b>                                   | <b>Capital at<br/>June 30, 2011</b> |
|---|-------------------------------------|
| Validus Reinsurance, Ltd. (consolidated), excluding IPCRe, Ltd. | \$ 3,004,720                        |
| IPCRe, Ltd.   | 314,310                             |
| <b>Total Validus Reinsurance, Ltd. (consolidated)</b>           | <b>3,319,030</b>                    |
| Noncontrolling interest in AlphaCat Re 2011, Ltd.               | 134,895                             |
| Talbot Holdings, Ltd.   | 627,554                             |
| Other subsidiaries  | 3,933                               |
| Other, net  | (5,472)                             |
| <b>Total consolidated capitalization</b>                        | <b>4,079,940</b>                    |
| Senior notes payable  | (246,928)                           |
| Debentures payable  | (289,800)                           |
| <b>Total shareholders equity</b>                                | <b>\$ 3,543,212</b>                 |

**Ratings**

The following table summarizes the financial strength ratings of the Company and its principal reinsurance and insurance subsidiaries from internationally recognized rating agencies as of August 5, 2011:

|   | <b>A.M. Best</b> | <b>S&amp;P</b> | <b>Moody's</b> | <b>Fitch</b> |
|---|------------------|----------------|----------------|--------------|
| <b>Validus Holdings, Ltd.</b>                                 |                  |                |                |              |
| Issuer credit rating  | bbb-             | BBB            | Baa2           | BBB+         |
| Senior debt   | bbb-             | BBB            | Baa2           | BBB          |
| Subordinated debt   | bb+              | BBB-           | Baa3           | BB+          |
| Preferred stock   | bb               | BB+            | Ba1            |              |
| Outlook on ratings  | Positive         | Stable         | Stable         | Stable       |
| <b>Validus Reinsurance, Ltd.</b>                              |                  |                |                |              |
| Financial strength rating                                     | A-               | A-             | A3             | A-           |
| Issuer credit rating  | a-               |                |                |              |
| Outlook on ratings  | Positive         | Stable         | Stable         | Stable       |
| <b>IPCRe Ltd.</b>   |                  |                |                |              |
| Financial strength rating                                     | A-               |                |                |              |
| Issuer credit rating  | a-               |                |                |              |
| Outlook on rating   | Stable           |                |                |              |
| <b>Validus Re Europe Ltd.</b>                                 |                  |                |                |              |
| Financial strength rating                                     | A-               |                |                |              |
| Issuer credit rating  | a-               |                |                |              |
| Outlook on rating   | Stable           |                |                |              |
| <b>Talbot</b>   |                  |                |                |              |
| Financial strength rating applicable to all Lloyds syndicates | A                | A+             |                | A+           |

**Table of Contents****Recent accounting pronouncements**

Please refer to Note 2 to the Consolidated Financial Statements (Part I, Item I) for further discussion of relevant recent accounting pronouncements.

**Debt and Financing Arrangements**

The following table details the Company's borrowings and credit facilities as at June 30, 2011.

| <b>(Dollars in thousands)</b>                            | <b>Commitments</b>  | <b>Outstanding</b> |
|--|---------------------|--------------------|
|  | <b>(a)</b>          |                    |
| 2006 Junior Subordinated Deferrable Debentures           | \$ 150,000          | \$ 150,000         |
| 2007 Junior Subordinated Deferrable Debentures           | 200,000             | 139,800            |
| 2010 Senior Notes due 2040                               | 250,000             | 250,000            |
| \$340,000 syndicated unsecured letter of credit facility | 340,000             |                    |
| \$60,000 bilateral unsecured letter of credit facility   | 60,000              |                    |
| \$500,000 secured letter of credit facility              | 500,000             | 277,679            |
| Talbot FAL facility (b)                                  | 25,000              | 25,000             |
| IPC Bi-Lateral Facility                                  | 80,000              | 63,284             |
| <b>Total</b>   | <b>\$ 1,605,000</b> | <b>\$ 905,763</b>  |

(a) Indicates utilization of commitment amount, not drawn borrowings.

(b) Talbot operates in Lloyd's through a corporate member, Talbot 2002 Underwriting Capital Ltd (T02), which is the sole participant in Syndicate 1183. Lloyd's sets T02's required capital annually based on syndicate 1183's business plan, rating environment, reserving environment together with input arising from Lloyd's discussions with, inter alia, regulatory and rating agencies. Such capital, called Funds at Lloyd's (FAL), comprises: cash, investments and a letter of credit facility of up to \$25 million.

Please refer to Note 10 the Consolidated Financial Statements (Part I, Item I) for further discussion of the Company's debt and financing arrangements.

**Investments**

A significant portion of contracts written provide short-tail reinsurance coverage for losses resulting mainly from natural and man-made catastrophes, which could result in a significant amount of losses on short notice. Accordingly, the Company's investment portfolio is structured to provide significant liquidity and preserve capital, which means the investment portfolio contains a significant amount of relatively short-term fixed maturity investments, such as U.S. government securities, U.S. government-sponsored enterprises securities, corporate debt securities and mortgage-backed and asset-backed securities.

Substantially all of the fixed maturity investments held at June 30, 2011 were publicly traded. At June 30, 2011, the average duration of the Company's fixed maturity portfolio was 1.57 years (December 31, 2010: 2.27 years) and the average rating of the portfolio was AA- (December 31, 2010: AA+). At June 30, 2011, the total fixed maturity portfolio was \$4,603.5 million (December 31, 2010: \$4,823.9 million), of which \$2,237.0 million (December 31, 2010: \$2,946.5 million) were rated AAA.

With the exception of the bank loan portfolio, the Company's investment guidelines require that investments be rated BBB- or higher at the time of purchase. The Company reports the ratings of its investment portfolio securities at the lower of Moody's or Standard & Poor's rating for each investment security and, as a result, the Company's investment portfolio now has \$34.2 million of non-agency mortgage backed securities rated less than investment grade.

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The other components of less than investment grade securities held by the Company at June 30, 2011 were \$29.9 million of catastrophe bonds, \$375.3 million of bank loans and \$2.3 million of corporate bonds.

Cash and cash equivalents and investments in Talbot of \$1,545.5 million at June 30, 2011 were held in trust for the benefit of cedants and policyholders and to facilitate the accreditation as an alien insurer/reinsurer by certain regulators (December 31, 2010: \$1,489.2 million). Total cash and cash equivalents and investments in Talbot were \$1,649.2 million at June 30, 2011 (December 31, 2010: \$1,592.1 million).

As of June 30, 2011, the Company had approximately \$1.2 million of asset-backed securities with sub-prime collateral (December 31, 2010: \$1.6 million) and \$8.5 million of Alt-A RMBS (December 31, 2010: \$9.9 million).

**Cash Flows**

During the six months ended June 30, 2011 and 2010, the Company generated net cash from operating activities of \$309.6 million and \$263.6 million, respectively. Cash flows from operations generally represent premiums collected, less losses and loss expenses paid and underwriting and other expenses paid. Cash flows from operations may differ substantially from net income.

As of June 30, 2011 and December 31, 2010, the Company had cash and cash equivalents of \$815.9 million and \$620.7 million, respectively.

The Company has written certain business that has loss experience generally characterized as having low frequency and high severity. This results in volatility in both results and operational cash flows. The potential for large claims or a series of claims under one or more reinsurance contracts means that substantial and unpredictable payments may be required within relatively short periods of time. As a result, cash flows from operating activities may fluctuate, perhaps significantly, between individual quarters and years. Management believes the Company's unused credit facility amounts and highly liquid investment portfolio are sufficient to support any potential operating cash flow deficiencies. Please refer to the table detailing the Company's borrowings and credit facilities as at June 30, 2011, presented above.

In addition to relying on premiums received and investment income from the investment portfolio, the Company intends to meet these cash flow demands by carrying a substantial amount of short and medium term investments that would mature, or possibly be sold, prior to the settlement of expected liabilities. The Company cannot provide assurance, however, that it will successfully match the structure of its investments with its liabilities due to uncertainty related to the timing and severity of loss events.

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**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

The Private Securities Litigation Reform Act of 1995 ( PSLRA ) provides a safe harbor for forward-looking statements. Any prospectus, prospectus supplement, the Company s Annual Report to shareholders, any proxy statement, any other Form 10-K, Form 10-Q or Form 8-K of the Company or any other written or oral statements made by or on behalf of the Company may include forward-looking statements that reflect the Company s current views with respect to future events and financial performance. Such statements include forward-looking statements both with respect to the Company in general, and to the insurance and reinsurance sectors in particular. Statements that include the words expect , intend , plan , believe , project , anticipate , will , may , and similar statements of a forward-looking nature identify forward-looking statements for purposes of the PSLRA or otherwise. All forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause actual results to differ materially from those indicated in such statements and, therefore, you should not place undue reliance on any such statement.

We believe that these factors include, but are not limited to, the following:

- unpredictability and severity of catastrophic events;
- our ability to obtain and maintain ratings, which may affect by our ability to raise additional equity or debt financings, as well as other factors described herein;
- adequacy of the Company s risk management and loss limitation methods;
- cyclicality of demand and pricing in the insurance and reinsurance markets;
- the Company s ability to implement its business strategy during soft as well as hard markets;
- adequacy of the Company s loss reserves;
- continued availability of capital and financing;
- the Company s ability to identify, hire and retain, on a timely and unimpeded basis and on anticipated economic and other terms, experienced and capable senior management, as well as underwriters, claims professionals and support staff;
- acceptance of our business strategy, security and financial condition by rating agencies and regulators, as well as by brokers and (re)insureds;
- competition, including increased competition, on the basis of pricing, capacity, coverage terms or other factors;
- potential loss of business from one or more major insurance or reinsurance brokers;
- the Company s ability to implement, successfully and on a timely basis, complex infrastructure, distribution capabilities, systems, procedures and internal controls, and to develop accurate actuarial data to support the business and regulatory and reporting requirements;
- general economic and market conditions (including inflation, volatility in the credit and capital markets, interest rates and foreign currency exchange rates) and conditions specific to the insurance and reinsurance markets in which we operate;
- the integration of businesses we may acquire or new business ventures, including overseas offices, we may start;

accuracy of those estimates and judgments used in the preparation of our financial statements, including those related to revenue recognition, insurance and other reserves, reinsurance recoverables, investment valuations, intangible assets, bad debts, taxes, contingencies, litigation and any determination to use the deposit method of accounting, which, for a relatively new insurance and reinsurance company like our

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company, are even more difficult to make than those made in a mature company because of limited historical information;

the effect on the Company's investment portfolio of changing financial market conditions including inflation, interest rates, liquidity and the possible downgrade of U.S. securities by credit rating agencies and the resulting effect on the value of securities in the Company's investment portfolio, as well as other factors;

acts of terrorism, political unrest, outbreak of war and other hostilities or other non-forecasted and unpredictable events;

availability and cost of reinsurance and retrocession coverage;

the failure of reinsurers, retrocessionaires, producers or others to meet their obligations to us;

the timing of loss payments being faster or the receipt of reinsurance recoverables being slower than anticipated by us;

changes in domestic or foreign laws or regulations, or their interpretations;

changes in accounting principles or the application of such principles by regulators;

statutory or regulatory or rating agency developments, including as to tax policy and reinsurance and other regulatory matters such as the adoption of proposed legislation that would affect Bermuda-headquartered companies and/or Bermuda-based insurers or reinsurers; and

the other factors set forth herein under Part I Item 1A "Risk Factors" and under Part II Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the other sections of the Company's Annual Report on Form 10-K for the year ended December 31, 2010, as well as the risk and other factors set forth in the Company's other filings with the SEC, as well as management's response to any of the aforementioned factors.

In addition, other general factors could affect our results, including: (a) developments in the world's financial and capital markets and our access to such markets; (b) changes in regulations or tax laws applicable to us, including, without limitation, any such changes resulting from the recent investigations relating to the insurance industry and any attendant litigation; and (c) the effects of business disruption or economic contraction due to terrorism or other hostilities.

The foregoing review of important factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements that are included herein or elsewhere. Any forward-looking statements made in this report are qualified by these cautionary statements, and there can be no assurance that the actual results or developments anticipated by us will be realized or, even if substantially realized, that they will have the expected consequences to, or effects on, us or our business or operations. We undertake no obligation to update publicly or revise any forward-looking statement, whether as a result of new information, future developments or otherwise.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We believe we are principally exposed to five types of market risk:

interest rate risk;

foreign currency risk;

credit risk;



liquidity risk; and

effects of inflation.

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*Interest Rate Risk:* The Company's primary market risk exposure is to changes in interest rates. The Company's fixed maturity portfolio is exposed to interest rate risk. Fluctuations in interest rates have a direct impact on the market valuation of these investments. As interest rates rise, the market value of the Company's fixed maturity portfolio falls and the Company has the risk that cash outflows will have to be funded by selling assets, which will be trading at depreciated values. As interest rates decline, the market value of the Company's fixed income portfolio increases and the Company has reinvestment risk, as funds reinvested will earn less than is necessary to match anticipated liabilities. We manage interest rate risk by selecting investments with characteristics such as duration, yield, currency and liquidity tailored to the anticipated cash outflow characteristics of the insurance and reinsurance liabilities the Company assumes.

As at June 30, 2011, the impact on the Company's fixed maturity and short-term investments from an immediate 100 basis point increase in market interest rates (based on U.S. treasury yield) would have resulted in an estimated decrease in market value of 1.6%, or approximately \$82.2 million. As at June 30, 2011, the impact on the Company's fixed maturity portfolio from an immediate 100 basis point decrease in market interest rates would have resulted in an estimated increase in market value of 1.1% or approximately \$57.2 million.

As at June 30, 2010, the impact on the Company's fixed maturity and short-term investments from an immediate 100 basis point increase in market interest rates (based on U.S. treasury yield) would have resulted in an estimated decrease in market value of 2.3%, or approximately \$122.0 million. As at June 30, 2010, the impact on the Company's fixed maturity portfolio from an immediate 100 basis point decrease in market interest rates would have resulted in an estimated increase in market value of 1.9% or approximately \$102.9 million.

As at June 30, 2011, the Company held \$806.7 million (December 31, 2010: \$644.4 million), or 17.5% (December 31, 2010: 13.4%), of the Company's fixed maturity portfolio in asset-backed and mortgage-backed securities. These assets are exposed to prepayment risk, which occurs when holders of underlying loans increase the frequency with which they prepay the outstanding principal before the maturity date and refinance at a lower interest rate cost. The adverse impact of prepayment is more evident in a declining interest rate environment. As a result, the Company will be exposed to reinvestment risk, as cash flows received by the Company will be accelerated and will be reinvested at the prevailing interest rates.

*Foreign Currency Risk:* Certain of the Company's reinsurance contracts provide that ultimate losses may be payable in foreign currencies depending on the country of original loss. Foreign currency exchange rate risk exists to the extent that there is an increase in the exchange rate of the foreign currency in which losses are ultimately owed. Therefore, we attempt to manage our foreign currency risk by seeking to match our liabilities under insurance and reinsurance policies that are payable in foreign currencies with cash and investments that are denominated in such currencies. As of June 30, 2011, \$727.1 million, or 8.8% of our total assets and \$910.1 million, or 19.3% of our total liabilities were held in foreign currencies. As of June 30, 2011, \$108.8 million, or 2.3% of our total liabilities held in foreign currencies was non-monetary items which do not require revaluation at each reporting date. As of June 30, 2010, \$526.3 million, or 6.9% of our total assets and \$494.3 million, or 12.3% of our total liabilities were held in foreign currencies. As of June 30, 2010, \$95.9 million, or 2.4% of our total liabilities held in foreign currencies were non-monetary items which do not require revaluation at each reporting date.

*Credit Risk:* We are exposed to credit risk primarily from the possibility that counterparties may default on their obligations to us. We attempt to limit our credit exposure by purchasing high quality fixed income investments to maintain an average portfolio credit quality of AA- or higher with mortgage and commercial mortgage-backed issues having an aggregate weighted average credit quality of AAA. In addition, we have limited our exposure to any single issuer to 3.0% or less of total investments, excluding treasury and agency securities. With the exception of the bank loan portfolio, the minimum credit rating of any security purchased is BBB-/Baa3 and where investments are downgraded below BBB-/Baa3, we permit our investment managers to hold up to 2.0% in aggregate market value, or up to 10.0% with written authorization of the Company. At June 30, 2011, 1.0% of the portfolio, excluding bank loans was below BBB-/Baa3 and we did not have an aggregate exposure to any single issuer of more than 1.1% of total investments, other than with respect to government securities.

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The amount of the maximum exposure to credit risk is indicated by the carrying value of the Company's financial assets. The Company's primary credit risks reside in investment in U.S. corporate bonds and recoverables from reinsurers. The Company evaluates the financial condition of its reinsurers and monitors concentration of credit risk arising from its exposure to individual reinsurers. The reinsurance program is generally placed with reinsurers whose rating, at the time of placement, was A- or better rated by S & P or the equivalent with other rating agencies. Exposure to a single reinsurer is also controlled with restrictions dependent on rating. At June 30, 2011, 99.1% of reinsurance recoverables (which includes loss reserves recoverable and recoverables on paid losses) were from reinsurers rated A- or above, or from reinsurers posting full collateral (December 31, 2010: 97.4%, rated A-).

*Liquidity risk:* Certain of the Company's investments may become illiquid. Disruption in the credit markets may materially affect the liquidity of the Company's investments, including residential mortgage-backed securities which represent 8.5% (December 31, 2010: 8.8%) of total cash and investments. If the Company requires significant amounts of cash on short notice in excess of normal cash requirements (which could include claims on a major catastrophic event) in a period of market illiquidity, the investments may be difficult to sell in a timely manner and may have to be disposed of for less than what may otherwise have been possible under other conditions. At June 30, 2011, the Company had \$1,685.6 million of unrestricted, liquid assets, defined as unpledged cash and cash equivalents, short term investments, government and government agency securities. Details of the Company's debt and financing arrangements at June 30, 2011 are provided below.

| <b>(Dollars in thousands)</b>                            | <b>Maturity Date /<br/>Term</b> | <b>In Use/<br/>Outstanding</b> |
|--|---------------------------------|--------------------------------|
| 2006 Junior Subordinated Deferrable Debentures           | June 15, 2036                   | \$ 150,000                     |
| 2007 Junior Subordinated Deferrable Debentures           | June 15, 2037                   | 139,800                        |
| 2010 Senior Notes due 2040                               | January 26, 2040                | 250,000                        |
| \$340,000 syndicated unsecured letter of credit facility | March 12, 2013                  |                                |
| \$60,000 bilateral unsecured letter of credit facility   | March 12, 2013                  |                                |
| \$500,000 secured letter of credit facility              | March 12, 2012                  | 277,679                        |
| Talbot FAL facility                                      | April 13, 2011                  | 25,000                         |
| IPC Bi-Lateral Facility                                  | December 31, 2010               | 63,284                         |
| <b>Total</b>   |                                 | <b>\$ 905,763</b>              |

*Effects of Inflation:* We do not believe that inflation has had or will have a material effect on our combined results of operations, except insofar as (a) inflation may affect interest rates, and (b) losses and loss expenses may be affected by inflation.

**ITEM 4. CONTROLS AND PROCEDURES****Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures**

The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of disclosure controls and procedures pursuant to Rules 13a-15 and 15d-15 promulgated under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this report.

Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures are effective to provide reasonable assurance that all material information relating to the Company required to be filed in this report has been recorded, processed, summarized and reported when required and the information is accumulated and communicated, as appropriate, to allow timely decisions regarding required disclosures.

**Table of Contents****Changes in Internal Control Over Financial Reporting**

There have been no changes in internal control over financial reporting identified in connection with the Company's evaluation required pursuant to Rules 13a-15 and 15d-15 promulgated under the Securities Exchange Act of 1934, as amended, that occurred during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II OTHER INFORMATION****ITEM 1. LEGAL PROCEEDINGS**

On June 12, 2011, Transatlantic Holdings, Inc. ( "Transatlantic" ), Allied World Assurance Company Holdings, AG ( "Allied World" ) and Go Sub, LLC entered into an Agreement and Plan of Merger (the "Transatlantic-Allied World Merger Agreement" ). Pursuant to the Transatlantic-Allied World Merger Agreement, Transatlantic's stockholders (including the stockholders that do not vote in favor of the Transatlantic-Allied World Merger Agreement) will, after the effective time, have the right to receive 0.88 validly issued, fully paid and non-assessable registered ordinary shares, par value CHF 15.00 per share (as may be adjusted in connection with the payment of dividends by virtue of a par value reduction, as approved by Allied World's shareholders at its 2011 Annual General Meeting) of Allied World, together with any cash paid in lieu of fractional shares, in exchange for each Transatlantic Common Share they hold.

On July 12, 2011, the Company announced that it had delivered to the Board of Directors of Transatlantic a proposal to merge the businesses of the Company and Transatlantic. Pursuant to the proposal, Transatlantic stockholders would receive 1.5564 Validus voting common shares in the merger and \$8.00 in cash per share pursuant to a one-time special dividend from Transatlantic immediately prior to closing of the merger for each share of Transatlantic common stock they own.

On July 20, 2011, the Company filed a preliminary proxy statement with the SEC in connection with the special meeting of stockholders of Transatlantic, urging the Transatlantic shareholders to vote against the Transatlantic-Allied World Merger Agreement.

On July 25, 2011, the Company commenced an exchange offer for all of the outstanding shares of common stock of Transatlantic. Under the terms of the exchange offer, Transatlantic stockholders would receive 1.5564 Validus voting common shares and \$8.00 in cash for each share of Transatlantic common stock they own. The terms and conditions of the exchange offer are set forth in the offering documents that the Company has filed with the SEC.

On July 28, 2011, Transatlantic filed a lawsuit against the Company in the United States District Court for the District of Delaware, alleging that the Company violated the U.S. securities laws by making false and misleading statements to Transatlantic's stockholders in the Company's proxy and exchange offer materials. The lawsuit seeks to compel the Company to correct alleged misstatements and omissions made in its proxy and exchange offer materials. The Company intends to vigorously defend this action. The Company believes that the ultimate outcome of this litigation will not have a material adverse effect on its consolidated financial condition, operating results and/or liquidity.

The Company anticipates that, similar to the rest of the insurance and reinsurance industry, it will be subject to litigation and arbitration in the ordinary course of business.

**ITEM 1A. RISK FACTORS**

Please refer to the discussion of Risk Factors in Item 1A of the Company's Annual Report on Form 10-K for the year ended December 31, 2010.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

In November 2009, the Board of Directors of the Company authorized an initial \$400.0 million share repurchase program. On February 17, 2010, the Board of Directors of the Company authorized the Company to return up to \$750.0 million to shareholders. This amount was in addition to, and in excess of, the \$135.5 million of common shares purchased by the Company through February 17, 2010 under its previously authorized \$400.0 million share repurchase program. On May 6, 2010, the Board of Directors authorized a self tender offer pursuant to which the Company has repurchased \$300.0 million in common shares.

On November 4, 2010, the Company announced that its Board of Directors had approved share repurchase transactions aggregating \$300.0 million. These repurchases were effected by a tender offer which the Company commenced on Monday November 8, 2010, for up to 7,945,400 of its common shares at a price of \$30.00 per share.

In addition, the Board of Directors authorized separate repurchase agreements with funds affiliated with or managed by each of Aquiline Capital Partners LLC, New Mountain Capital, LLC and Vestar Capital Partners pursuant to which the Company has repurchased \$61.6 million in common shares. On December 20, 2010, the Board of Directors authorized the Company to return up to \$400.0 million to shareholders. This amount was in addition to the \$929.2 million of common shares purchased by the Company through December 23, 2010 under its previously authorized share repurchase program.

The Company expects the purchases under its share repurchase program to be made from time to time in the open market or in privately negotiated transactions. The timing, form and amount of the share repurchases under the program will depend on a variety of factors, including market conditions, the Company's capital position relative to internal and rating agency targets, legal requirements and other factors. The repurchase program may be modified, extended or terminated by the Board of Directors at any time.

The Company has repurchased approximately 35.0 million common shares for an aggregate purchase price of \$947.2 million from the inception of the share repurchase program to August 4, 2011.

Share repurchases include repurchases by the Company of shares, from time to time, from employees in order to facilitate the payment of withholding taxes on restricted shares granted and the exercise of stock appreciation rights. We purchased these shares at their fair market value, as determined by reference to the closing price of our common shares on the day the restricted shares vested or the stock appreciation rights were exercised.

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| <b>Share Repurchase Activity</b><br>(Expressed in thousands of U.S. dollars except for share and per share information) |  |              |            |             |  |
|---|--|--------------|------------|-------------|--|
|   | <b>As at March<br/>31,<br/>2011<br/>(cumulative)</b> | <b>April</b> | <b>May</b> | <b>June</b> | <b>Quarter<br/>ended June<br/>30, 2011</b> |
| <b>Effect of share repurchases:</b>   |  |              |            |             |  |
| Aggregate purchase price (a)  | \$ 947,170   | \$           | \$         | \$          | \$   |
| Shares repurchased  | 35,031,985   |              |            |             |  |
| Average price (a)   | \$ 27.04   | \$           | \$         | \$          | \$   |
| Estimated net accretive<br>(dilutive) impact on:  |  |              |            |             |  |
| Diluted BV per common share (b)   |  |              |            |             | \$ 1.16                                    |
| Diluted EPS Quarter (c)   |  |              |            |             | \$ 0.26                                    |

| <b>Share Repurchase Activity</b><br>(Expressed in thousands of U.S. dollars except for share and per share information) |   |             |               |                                     |  |
|---|---|-------------|---------------|-------------------------------------|--|
|   | <b>As at June<br/>30, 2011<br/>(cumulative)</b> | <b>July</b> | <b>August</b> | <b>As at<br/>August 4,<br/>2011</b> | <b>Cumulative to<br/>Date<br/>Effect</b> |
| <b>Effect of share repurchases:</b>   |   |             |               |                                     |  |
| Aggregate purchase price (a)  | \$ 947,170                                      | \$          | \$            | \$                                  | \$ 947,170                               |
| Shares repurchased  | 35,031,985                                      |             |               |                                     | 35,031,985                               |
| Average price (a)   | \$ 27.04  | \$          | \$            | \$                                  | \$ 27.04                                 |

- (a) Share transactions are on a trade date basis through August 4, 2011 and are inclusive of commissions. Average share price is rounded to two decimal places.
- (b) As the average price per share repurchased during the periods 2009, 2010 and 2011 was lower than the book value per common share, the repurchase of shares increased the Company's period ending book value per share.
- (c) The estimated impact on diluted earnings per share was calculated by comparing reported results versus i) net income per share plus an estimate of lost net investment income on the cumulative share repurchases divided by ii) weighted average diluted shares outstanding excluding the weighted average impact of cumulative share repurchases. The impact of cumulative share repurchases was accretive to diluted earnings per share.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. (Removed and Reserved)****ITEM 5. OTHER INFORMATION**

None.

**Table of Contents****ITEM 6. EXHIBITS**

| <b>Exhibit</b>     | <b>Description</b>  |
|--------------------|---|
| Exhibit 31.1*      | Certification of Chief Executive Officer pursuant to Section 302 of The Sarbanes-Oxley Act of 2002.                     |
| Exhibit 31.2*      | Certification of Chief Financial Officer pursuant to Section 302 of The Sarbanes-Oxley Act of 2002.                     |
| Exhibit 32*        | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of The Sarbanes-Oxley Act of 2002. |
| Exhibit 101.1 INS* | XBRL Instance Document  |
| Exhibit 101.SCH*   | XBRL Taxonomy Extension Schema Document   |
| Exhibit 101.CAL*   | XBRL Taxonomy Extension Calculation Linkbase Document   |
| Exhibit 101.LAB*   | XBRL Taxonomy Extension Label Linkbase Document   |
| Exhibit 101.PRE*   | XBRL Taxonomy Extension Presentation Linkbase Document  |
| Exhibit 101.DEF*   | XBRL Taxonomy Extension Definition Linkbase Document  |

\* Filed herewith

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**SIGNATURES**

Pursuant to the requirements of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**VALIDUS HOLDINGS, LTD.**  
(Registrant)

Date: August 5, 2011

/s/ Edward J. Noonan  
Edward J. Noonan  
Chief Executive Officer

Date: August 5, 2011

/s/ Joseph E. (Jeff) Consolino  
Joseph E. (Jeff) Consolino  
President and Chief Financial Officer

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