

W.R. Berkley Corp. And Operating Subsidiaries

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W.R. Berkley Corp. And Operating Subsidiaries

Major Rating Factors

Strengths:

- Strong underwriting and operating performance
- Strong, well-diversified competitive position
- Strong liquidity

Weaknesses:

- Somewhat aggressive historical financial leverage at the holding company
- Capitalization is below rating level and considered to be a weakness to the rating

Holding Company: W.R. Berkley Corp.
Counterparty Credit Rating <i>Local Currency</i> BBB+/Stable/--
Operating Companies Covered By This Report
Financial Strength Rating <i>Local Currency</i> A+/Stable/--

Rationale

The counterparty credit rating on W. R. Berkley Corp. and the counterparty credit and financial strength ratings on its operating insurance companies (collectively referred to as WRB) reflect the group's strong competitive position and operating performance, which stem from its well-diversified business platform that has contributed to the highly favorable underwriting performance and the lower earnings volatility compared with the industry and most of its peers. Offsetting these strengths are WRB's somewhat aggressive historical financial leverage, the above-average net underwriting leverage, and the operating companies' capital that, though good, is lower than what we expect for the rating.

WRB's average five-year generally accepted accounting principles (GAAP) combined ratio of 91.6% highlights its consistent track record of highly favorable underwriting performance compared with that of the industry and many global peers and is a core strength to the rating. That, in our view, is largely attributed to Berkley's well-established business strategies, which feature individual operating units focused on specific niche markets that are primarily defined by geography and product orientation. The group's market expertise has led to favorable operating results and helped long-term stability, resulting in above-average retention. We believe these favorable operating results will continue, and we view the group's established market position despite persisting competition as a strength to the rating. Lower-than-average catastrophe exposure, appropriate cycle management, and its moderate risk profile are significant rating strengths as well.

We view WRB's competitive position as strong, based on its well-diversified revenue profile, long-standing relationships with producers, economies of scale, and market position. WRB has a highly diversified competitive profile, with operations in five segments of the property/casualty (P/C) market: specialty lines (excess and surplus and specialty admitted lines), regional (commercial P/C), alternative markets (fee-based and workers' compensation), reinsurance, and international. The group has a complex insurance-risk portfolio, mainly because of a sizable casualty book, which grows (21 new units launched since 2006) by adding new products and new regions. The company is expanding internationally with nearly 15% of its business coming from outside the U.S. The group also shows geographic diversification, which organic growth has primarily supported. The newer units focus on health care, energy, agriculture, and international markets, including Lloyds, Australia, Southeast Asia, and South America.

We consider the group's liquidity to be strong, with strong operating cash flow and with support from high-quality fixed maturities and cash equivalents that made up 86% of the investment portfolio as of June 30, 2011. The average credit quality of the bond portfolio is 'AA', with an average duration of approximately 3.5 years. WRB's overall portfolio is sound. The group posted a net unrealized gain of \$53 million as of June 30, 2011, on a fixed maturity portfolio at the amortized cost of \$10.7 billion (\$11.2 billion fair value). This compares well with the total loss reserves of more than \$9 billion with a duration of more than three years and limited catastrophe exposure, underlining the group's strong liquidity.

WRB somewhat aggressively manages capital. At year-end 2010, its capitalization, though good, was lower than what we expect for the rating, and we consider it to be a weakness. Furthermore, WRB has a track record of temporarily allowing capital to fall to lower than what we expect for the rating when market conditions are favorable to pursue rapid growth, such as in 2003 and 2004 when WRB's growth peaked at 35%. In addition, although WRB have had a favorable development on reserves for recent accident years, which we expect to be lower going forward, it continues to experience some adverse loss reserve development in older accident years.

We view WRB's enterprise risk management as adequate with strong risk controls. The group shows strong risk management culture and strong insurance-risk controls, which its favorable underwriting results demonstrate. WRB employs overall sound practices to address the group's key risks, with strong underwriting fundamentals and qualitative approaches to risk management. This has traditionally boded well for the firm's risk portfolio, which is largely noncatastrophe, conservative, and casualty-driven.

The issuer credit and debt ratings on WRB reflect its substantial financial flexibility, shown in the group's ability to access capital markets and maintain investor interest. Although WRB has historically maintained considerable financial leverage, strong earnings have fueled the improved capital of its subsidiaries since 2005. However, its leverage has remained higher than that of industry peers. As of Dec. 31, 2010, WRB's financial leverage, which we measure by total debt including qualifying hybrids, was 33.5%, at almost the top of its target range of 25% to 35%. Although total financial leverage (32.7% as of June 30, 2011) is consistent with the rating, debt leverage (28.5%) is higher than our criteria threshold of 20%, with the excess leverage deducted in our assessment of capitalization. WRB has a low reliance on reinsurance (about a 12% utilization rate, which is lower than most of its global peers), as well as a low proportion of intangible assets to surplus.

We believe WRB may continue to modestly strain capital and financial leverage to grow, particularly when the underwriting cycle improves.

Although the competitive property/casualty operating environment is still likely to hamper 2011 underwriting results, we expect WRB's earnings to remain strong, and both its cash coverage ratios and its financial leverage should remain supportive of the ratings.

Factors Specific To Holding Company

Standard & Poor's Ratings Services applies standard notching (one full category, or three notches) between WRB's operating companies and holding company. The three-notch difference reflects the holding company's dependence on dividends from its operating subsidiaries and regulators' ability to prohibit those dividends. In 2010, the insurance subsidiaries issued \$406 million in dividends, and the company may withdraw \$490 million of dividends from its subsidiaries without regulatory approval in 2011. As of June Dec. 31, 2010, the holding company had cash

and investments of \$385 million.

As of June 30, 2011, the company had senior notes, junior subordinated debentures, and other debt outstanding with a carrying value of \$1.74 billion and a face amount of \$1.76 billion. About \$9 million of the outstanding debt matures in 2011, \$25 million in 2012, \$200 million in 2013, \$200 million in 2015, \$2 million in 2016, \$450 million in 2019, \$300 million in 2022, \$76 million in 2020, \$1 million in 2023, \$250 million in 2037, and \$250 million in 2045.

Holding company financial metrics are consistent with the rating, with debt leverage of 28.5%, versus 26% a year ago, and intermediate hybrid equity leverage of 5% as of June 2011. WRB exceeds our debt double-leverage tolerance by \$488 million. Consistent with our criteria, we reduced our view of capital at the operating company level by this amount. Even with this adjustment, we view operating company capitalization as good. WRB's EBITDA fixed-charge coverage ratio, excluding realized gains and losses, of 6.24x at year-end 2010 and at 4.39x for the six months ended June 30, 2011, supports the rating. Although adverse pricing conditions could result in lower earnings and coverage metrics in the next 12-24 months, we expect fixed-charge coverage to remain a strength to the rating.

Notwithstanding current metrics, the company has a track record of stressing financial leverage to pursue growth—total debt leverage exceeded 35% in the height of the favorable market cycle in 2005. Standard & Poor's views this as a modest strain on financial flexibility, particularly if the company's operations were to unexpectedly worsen.

Table 1

W.R. Berkley Corp.--Financial Statistics					
	2010	2009	2008	2007	2006
EBIT interest coverage	6.43	6.22	9.81	14.04	16.06
EBIT fixed-charge coverage	5.53	5.14	8.05	11.58	12.73
EBITDA interest coverage	7.25	7.20	10.89	14.96	17.08
EBITDA fixed-charge coverage	6.24	5.95	8.94	12.34	13.53
Debt leverage including additional pension deficit as debt (%)	29.22	27.60	27.10	22.92	20.45
Financial leverage including additional pension deficit as debt (%)	33.55	32.39	33.14	27.59	29.45

Outlook

The stable outlook reflects the consistently favorable underwriting and operating performance from the solidly positioned, diversified subsidiaries, which offset WRB's modestly aggressive financial profile. We expect the holding company's financial leverage to be less than 35%. Although we expect difficult market conditions to somewhat hinder WRB's top- and bottom-line operating performance, it should remain favorable relative to the industry with a combined ratio of 100%-102%, including weather-related incidents in the first half of 2011 and considering a normal level of catastrophe losses for the remainder of the year. We expect WRB to post return on revenue (ROR) of more than 9% (strong for this stage of the insurance cycle) and fixed-charge coverage, excluding realized investment gains and losses and investment fund losses, exceeding 5x.

If there is an adverse change to WRB's strong earnings profile (the company's combined ratio is no longer better than the industry average by at least two percentage points or there is significant adverse reserve development) or we

believe its enterprise risk management (ERM) at the operating company declines, we could lower the rating. We could raise the rating if WRB, while sustaining its earnings profile, improves its ERM to strong and consistently demonstrates capitalization and financial leverage more appropriate for a higher rating.

Competitive Position: Booking Strong Operating Results And Maintaining Well-Diversified Business

WRB's competitive position is strong, based on its well-diversified revenue profile by business segment, long-standing relationships with its diversified distribution channels, and economies of scale.

Founded in 1967, WRB is now the 21st-largest property/casualty insurance company in the U.S. based on net premiums written. The group's strongly positioned diversified operating segments and its long-term relationship with brokers and agents allow it to compete effectively with larger peers and are clear strengths to the rating. The group's consistent solid performance underlines its strong competitive position. WRB runs its operations using a decentralized strategy, which allows each unit to take responsibility to identify and respond to changing market conditions based on specifics of the region and its product mix.

In 2010 and as of June 30, 2011, the international markets drove company growth the most. Since 2006, the company has started 21 new units that should aid growth in the next favorable underwriting cycle, in areas such as health care, energy, and international markets like Lloyds, Australia, Asia, South America, and Canada. The company typically sets up these new units by hiring talent displaced from struggling competitors and management monitors performance.

Table 2

W.R. Berkley Corp.'s Operating Companies--Competitive Position					
(Mil. \$)	2010	2009	2008	2007	2006
Gross premiums written	4,416.1	4,253	4,520.1	5,053.2	5,277
Year-over-year change (%)	4	(5.9)	(10.5)	(4.2)	3.7
Net premiums written	3,835.6	3,730.1	4,033.9	4,576	4,819
Year-over-year change (%)	2.8	(7.5)	(11.8)	(5)	4.6
Reinsurance utilization (%)	11.7	12.3	10.8	9.4	8.7
Net premiums by line of business					
Specialty insurance (%)	33.6	35.6	36.1	37.3	37.7
Alternative markets (%)	15.8	15.7	15.4	14.3	13.5
Reinsurance (%)	11	10.8	10.8	14.9	18.5
Regional (%)	27.8	29.3	30	27.7	25.6
International (%)	11.8	8.5	7.7	5.8	4.7

Diversification

Specialty segment The specialty segment (35% of consolidated gross premium written [GPW] in 2010) has a strong competitive position in underwriting third-party liability risks, within excess and surplus lines and on an admitted basis. The largest types of specialty insurance the group underwrote in 2010 are premises operations (29%), property (21%), professional liability (18%), commercial auto (8%), and products liability (6%). Even though the underwriting environment for the specialty segment continued to be soft in 2010, GPW increased 4.2% to \$1.53 billion from the previous year and, picking up momentum in second-quarter 2011, increased 12% from the same

period a year ago. In 2010, we attributed the GPW increase to a 16% increase in both the property and professional liability lines, which a 32% decrease in commercial automobile, 15% decrease in products liability, and a 4% decrease in other liability slightly offset.

Berkley conducts its specialty business through 18 operating units that focus on different customer bases and products. The largest are:

- Admiral Insurance Co. (16.7% of segment GPW in 2010) provides excess and surplus lines coverage in the commercial general liability, professional liability, commercial property, and commercial excess and umbrella liability lines of business. Distribution for these relatively complex and high-risk products is through wholesale brokers to middle-market commercial accounts.
- Nautilus Insurance Co. (15.9% of GPW in the segment), though marketing similar products, targets less complex risk (less than \$2,500 average premium) from significantly smaller clients. Unlike Admiral, Nautilus business is written on a binding authority basis, or individually underwritten wholesale broker business.
- Monitor Liability Managers Inc. (10.1% of GPW) specializes in professional liability insurance, including directors' and officers' liability, employment practices liability, lawyers' professional liability, management liability, nonprofit directors' and officers' liability, and accountants' preferred liability. WRB distributes its insurance through a network of independent agents and brokers.
- Berkley Specialty (12% of GPW in the segment) underwrites general liability coverage with an emphasis on products liability. They also underwrite P/C insurance products, both on an admitted and nonadmitted basis, for the entertainment industry and sports-related organizations. The environmental division underwrites specialty insurance products to environmental customers such as contractors, consultants, and owners of sites and facilities.
- Monitor Liability Managers Inc. (10.1% of GPW) specializes in professional liability insurance, including directors' and officers' liability, employment practices liability, lawyers' professional liability, management liability, nonprofit directors' and officers' liability, and accountants' preferred liability. WRB distributes its insurance through a network of independent agents and brokers.
- Berkley Underwriting Partners (7% of GPW) underwrites specialty insurance products through program administrators and managing general underwriters nationwide on both an admitted and nonadmitted basis.

Regional segment The regional segment (26.3% of 2010 consolidated GPW and 23% as of second-quarter 2011 GPW) has historically had a strong competitive position, based on its position within commercial lines. Approximately 36% of premiums the group writes are from multiperil, 25% for automobile, 18% for workers' compensation, and 3% for assigned risk plans. The specific target market of WRB's regional platforms is small to midsize businesses and government entities. Business is well diversified by state, with the top five states—Massachusetts (7.2%), Texas (7.1%), Massachusetts (4.2%), Pennsylvania (6.7%), Maine (5.7%) and New Hampshire (5.3%)—constituting 32% of regional segment premium volume in 2010.

However, the soft underwriting environment has hurt premium income. Net premiums written had declined by 10.7% from 2008 to 2009 and by 3.4% from 2009 to 2010, mainly because of significant pricing pressures that caused the company to let business go, especially in the large account segment. However, written premium income in the first half of 2011 for the regional segment increased by 2%, which shows some signs of recovery.

The regional companies are organized geographically to provide them with the flexibility to adapt quickly to the local market. The four largest comprise 86.7% of the regional segment premiums:

- Continental Western Group (23.9% of segment GPW in 2010) underwrites commercial insurance services throughout the Midwest. Although it underwrites insurance in a variety of niche markets, such as fire departments, schools, public entities, utilities, and churches, its main strength is in the agriculture-based business. In 2009, Continental Western expanded its market position in the agriculture business by setting up Berkley Agribusiness Risk Specialists, which we expect to operate nationally.
- Acadia Insurance Group (26.4% of segment GPW) underwrites insurance to the Northeastern U.S. through local independent agents. It has built specialized expertise in construction and lumber, and specialty lines of insurance such as ocean marine.
- Union Standard Insurance Group (18.5% of segment GPW) provides commercial P/C insurance products to a variety of small to midsize commercial entities through independent insurance agents in eight Southern states.
- Berkley Mid-Atlantic Group (17.9% of segment GPW) covers Delaware, the District of Columbia, Maryland, North Carolina, Ohio, Pennsylvania, South Carolina, and Virginia. It focuses on middle-market commercial accounts managed through independent brokers.

Alternative segment The alternative market segment (16% of 2010 consolidated GPW) specializes in insuring, reinsuring, and administering self-insurance programs and other alternative risk-transfer mechanisms. Midwest Employers Casualty Co. (31% of 2010 gross segment premiums) provides excess workers' compensation to self-insured employers and groups above their self-insured or retented limits. Key Risk Insurance Co. (16% of the segment GPW) offers primary workers' compensation principally in the Southeastern states. Berkley Accident and Health (11% of the segment GPW) underwrites accident and health insurance and reinsurance products through four primary business segments: medical stop loss, managed care, special risk, and group captive. Berkley Net Underwriters (10% of the segment GPW) uses a Web-based system to allow producers to quote, bind, and service insurance policies. Its initial focus is on the workers' compensation market. Preferred Employers Insurance Co. (9% of the segment GPW) offers primary workers' compensation to owner-managed, small employers in California.

Its largest alternative market segment company, Midwest Employers Casualty Co. (31% of the segment GPW), provides excess workers' compensation to self-insured employers and groups above their self-insured or retained limits. Midwest Employers Casualty Co. has a specialized service to analyze its client's historical costs and processes to design programs to mitigate risk and future costs. Two relatively new units, Berkley Net Underwriters LLC (Berkley Net) and Berkley Accident and Health LLC (Berkley A&H), contributed 11% of alternative market segment production. Berkley Net uses a web-based system to allow producers to quote, bind, and service insurance policies, with the initial focus on the workers' compensation market. This company increased premium earned to \$25 million in 2010 from approximately \$15 million in 2007. Berkley A&H underwrites accident and health insurance and reinsurance products for medical stop loss, managed care, special risk, and group captive.

The weak economy and high unemployment hurt the alternative market segment's premium revenue, which declined by 5% in both 2008 and 2009. Although the decline slowed to about 1% in 2010, the cumulative effect contributed to the 4% decline in premiums earned in second-quarter 2011 compared with the same period a year ago.

Reinsurance segment Like its primary operations, WRB's reinsurance operations (9.6% of 2010 consolidated GPW) focus on specialty lines of business, offering reinsurance on an individual basis primarily through facultative reinsurance, as well as treaty reinsurance. Gross premiums were flat in 2009 and declined by 7% in 2010 as a result of the weak market. The segment writes the majority of its business on behalf of Berkley Insurance Co. (BIC), which had \$2.6 billion in policyholder's surplus at the end of 2010. The reinsurance business originates primarily from brokers, and direct marketing and its long-term relationships have resulted in an ability to implement a customer-focused, very specialized strategy. Similar to the specialty segments, the reinsurance operations consist of

seven underwriting units specializing in various subsegments of the reinsurance market. The largest are Berkley Re America (formerly Signet Star) (65% of total segment GPW), which focuses on casualty excess-of-loss treaties produced through reinsurance brokers and intermediaries. Facultative ReSources Inc. (14%) specializes in individual certificate and program facultative business produced through brokers. BF Re Underwriters LLC (10%) is a direct casualty facultative reinsurance underwriting manager. Berkley also maintains a reinsurance presence in the Lloyd's market that constituted 16% of Berkley's overall reinsurance book in 2010, where it assumes a range of short-tailed lines (including some catastrophe-exposed property) through a Lloyd's syndicate (16% of GPW in 2010). In 2010, the reinsurance business had a 68/32 split between casualty and property compared with 83/17 in 2008.

International segment WRB entered the international business in 1995 with operations in Argentina—its largest international operation in 2010. Berkley's main growth driver continues to be the international segment (13.6% of 2010 consolidated GPW), which underwrites insurance in Europe (mainly the U.K. and continental Europe), South America, Asia, and Australia, Canada, and through Lloyds of London. The international segment's premiums increased by 18.8% in 2009 and by 37% in 2010. In contrast to Berkley's other business units, which service the crowded U.S. market, it recorded flat premium volume in 2010.

The largest international segment is Berkley International Latinoamerica S.A. (BILSA), which provides commercial and personal P/C insurance primarily in Argentina, Brazil, and Uruguay. This accounts for 37% of the segment's revenue. The second largest is W.R. Berkley Insurance (Europe) Ltd. (30% of the segment GPW), which is based out of the U.K. but has branch offices in Spain, Ireland, Norway, Germany, and Australia. Berkley Re Australia (16% of the segment GPW), which began operations in 2007, provides P/C reinsurance on a treaty and facultative basis in Australia and through its division in Hong Kong. In 2009, Berkley also set up two new international groups. One is a new Lloyds syndicate (Syndicate 1967), which underwrites property and accident classes of business (14% of the segment GPW). The other is its Canadian operations (3% of the segment GPW), which underwrites specialty casualty commercial insurance products in Canada. WRB's goal is to establish these operations in the current competitive market and grow when market opportunities arise. For 2011, the Lloyds syndicate has underwriting capacity of approximately \$150 million, and we expect it will continue to grow in the specialized book of marine business, in addition to its established books of accident and commercial property lines of business.

Prospective

We believe that WRB's disciplined underwriting will remain strong, even amid high competition. We expect the group's consolidated net premium to stabilize throughout 2011 and 2012, and for WRB to be well-positioned to maintain its market share. We also expect that WRB will be able to raise premium revenue by expanding in its foreign and specialty markets, which should help increase its overall net written premium by 2%-3% in 2011 and 2012. We also expect WRB to continue to outperform the industry and most of its peers with a combined ratio of less than 98% for the year (excluding catastrophe losses). Just as WRB's continued underwriting discipline resulted in a double-digit volume decline from 2007 to 2009, premium revenues might increase, depending on the degree of favorable market conditions through 2012. Should the underwriting environment improve substantially, WRB might experience double-digit growth in premium revenue. During the height of the last favorable pricing cycle in 2005, WRB premium volume increased by 35%.

Management And Corporate Strategy: Providing A Stable Return From The Diversified Insurance Operations To Its Stockholders

We view WRB's management and corporate strategy as a marginal strength to the rating. WRB's corporate strategy focuses on providing a stable return to its stockholders through diversifying its insurance operations. The

consolidated group's corporate strategy, though well-executed (which we measure by its very strong diversified underwriting performance), involves aggressive financial leverage and operating company capitalization in times of business opportunities. Notwithstanding WRB's strong and consistent earnings profile, the willingness to aggressively pursue prospective business opportunities through a somewhat aggressive capital and financial leverage structure increases risk within the organization, particularly if an unforeseen loss should occur.

WRB's senior managers have substantial industry experience. The chairman and founder, William Berkley, created the company in 1967. Using a decentralized management structure, presidents operate the various insurance entities, which function as underwriting units, with oversight from the segment senior vice presidents based at the home office. WRB's corporate strategy is to seek specialized product areas or geographic regions where the insurance subsidiaries can gain a competitive advantage through knowledge-based underwriting and by responding quickly to changing market conditions. Each subsidiary establishes its own pricing practices, which the parent company monitors closely. The successful execution of this is a testament to the company's operational management.

The group has a very strong record of solid performance and astute strategic decision making, which is borne from executive management, the group-level senior vice presidents, and individual operating company presidents disseminating an excellent underwriting risk culture. We believe that WRB's well-established compensation structure, which, to a large degree, is composed of restricted employee stock ownership, bolsters its strong long-term historical underwriting performance. In the face of the next favorable underwriting cycle and the strong growth that current and material production generated from newer startup operations, WRB faces the challenge of sustaining and institutionalizing this culture through a more formal ERM process in addition to its qualitative approaches to risk management that have traditionally gone well for the firm's risk portfolio.

In response to the growing complexity of the enterprise, the insurer recently formalized its ERM practice and dedicated additional resources—an ERM senior vice president (SVP) leading a team of five specialists. An insurance risk management SVP and team, along with an investment SVP at the holding-company level further enhance risk governance and controls. Moreover, dotted-line reporting of actuaries, claims management, and underwriting to the holding company creates a reliable insurance-risk management infrastructure.

However, the company's chairman and CEO, Mr. W.R. Berkley, is actively involved in the detailed oversight and is primarily responsible for the strategic direction of the company and investment. Although the company has succession plans in place, we believe that the loss of Mr. Berkley could have a profound effect on the company's strategic direction.

Enterprise Risk Management: Strong With Strong Risk Controls And Consistently Developing

Enterprise risk management for W.R. Berkley Corp. is viewed as adequate with strong risk controls. WRB's favorable underwriting results highlight its strong risk management culture and insurance-risk controls, which support our view that WRB's enterprise risk management is adequate. WRB continues to dedicate resources to its ERM practices and works to develop the overall ERM framework for the group.

WRB solidly addresses its key risks with strong underwriting fundamentals and qualitative risk management approaches, which is generally helpful for the group's risk portfolio.

The group is well-grounded in sound underwriting fundamentals and focuses on the exposures in which it is most knowledgeable. Part of the firm's risk strategy is to avoid catastrophe risk and to sidestep significant investment risks while concentrating its resources on profitable underwriting of diverse casualty business. It is predominately a low-limit casualty business, which enables the company to minimize its reliance on reinsurance.

Investment-related risk controls seem basic but are commensurate with the complexity of the investment portfolio. The firm chose to take insurance risks while minimizing investment volatility.

Insurance exposures are managed to full maximum loss rather than a probable maximum loss. This conservative, disciplined approach significantly limits dependencies on vendor models and follows sound judgment and experience-driven decisions. The organization is consistent and diligent in maintaining pricing adequacy, and does not jump in and out of products or regions purely on speculation or opportunistic opinion. The firm maintains an extensive cadre of pricing and reserving actuarial staff. There is fluid communication among actuaries, claims staff, and underwriters.

WRB encourages conservative judgment for the reserving process. Reserving decisions are made on the operating-company level, but the peer-review process assures methodology and assumption consistency across the firm. Nevertheless, reserve adequacy remains a considerable source of uncertainty to WRB, particularly if claim costs start to escalate. This high-inflation scenario could coincide with high interest rates, thus eroding the value of the investment portfolio. The firm is contemplating this and other macroeconomic scenarios as part of its financial-planning and emerging risk management process.

WRB is a complex and growing enterprise. This may present an operational challenge, if the organizational structure does not keep up with the complexity and growth. However we believe WRB defines risk appetite and tolerances well, mainly using extreme-event scenarios, and aims to limit potential capital erosion. In addition to enhancing its ERM and strategic decision making, the firm has recently introduced a stochastic internal capital model. Although it is still developing, the models should contribute to a favorable balance of qualitative and quantitative understanding of all risks the organization faces.

We might view the group's ERM as strong if it fully implements the decision-making framework that the internal capital model supports and its strategic risk management structure becomes more diverse, thereby limiting the key-man risk—or dependency on one or few individuals, and associated dependencies. However, if the group's controls and mitigation efforts are not as robust as we thought, it would hurt our view of the firm's ERM effectiveness.

Accounting

WRB is a publicly traded entity subject to SEC filings. In addition, its U.S. insurance company subsidiaries are required to file statutory statements. KPMG audited the GAAP consolidated balance sheets as of Dec. 31, 2010 and 2009, and the related consolidated income statement and changes in shareholders' equity and cash flows for the three years ended Dec. 31, 2010, and expressed an unqualified opinion. Standard & Poor's is unaware of any regulatory inquiry in WRB's financial reporting. The company filed all financial statements, statutory and GAAP, on time.

In our assessment of Berkley's capital adequacy, we replace WRB's tabular and nontabular discounting with our

own measurement of discounting in calculating the company's audited reserves. Because our capital adequacy ratio model includes a time value of money benefit to the company's surplus base, we made the adjustment to avoid giving double credit to capital.

Operating Performance: Soft Pricing Could Pose A Challenge, But Underwriting And Profitability Should Support Performance

WRB's consistently strong and diversified underwriting performance is at the top of its peer group and supports the rating. Given the company's somewhat aggressive financial management for the rating, the operating performance is the primary supporting factor for the rating.

We believe that WRB has strong underwriting standards and earnings capacity. Although the underwriting environment continues to be soft, the overall loss ratio, including weather-related losses in the first half of 2011, is 64.1% and favorable relative to the industry and most of its peers. The GAAP combined ratio was 94.5% in 2010 and 98.8% in first half of 2011 (including unusual weather-related losses in April and May 2011) with about an 80% retention rate in the first six months of 2011, compared with a 78% retention rate in 2010. The group GWP increased by 12% to \$2.52 billion in the first six months of 2011, primarily because of growth in its specialty and international business segments.

In 2010, Berkley reported an increase in its 2010 pretax operating income to \$603 million from \$382 million in 2009, primarily as a result of higher investment income. WRB's return on revenue was also strong at 16.6% at year-end 2010 on a statutory basis.

Table 3

W.R. Berkley Corp.'s Operating Companies--Operating Performance					
(%)	2010	2009	2008	2007	2006
Return on revenue	13.7	11.9	13.3	21.5	19.7
Return on assets excluding all investment gains	4.1	3.3	5.0	7.5	14.4
Return on equity	12.3	9.3	8.5	22.1	41.9
EBIT adjusted/Total equity adjusted	18.0	15.4	23.2	32.7	62.9
EBITDA adjusted/Capital	12.5	11.3	17.0	23.9	48.4
Net investment yield	4.0	4.2	4.2	5.0	9.9
Net loss ratio	60.2	61.4	62.7	59.6	61.0
Net expense ratio	34.3	32.8	30.4	32.8	30.9
Net combined ratio	94.5	94.2	93.1	92.4	91.9

Specialty segment

Although the premiums in the specialty segment declined in 2008 and 2009 because of a soft underwriting environment and the weak economy, management demonstrated its underwriting restraint through its incremental increase in the loss ratio. The segment picked up momentum in 2010 with a 4% increase in GPW and an improved loss ratio of 58.3% from 61.9% in 2009. In second-quarter 2011, the specialty segment net premium earned (NPE) increased 11% compared with same period a year ago. The company had experienced favorable claims frequency rates for its recent accident years since 2004, mainly because of the tightening of terms and conditions of policy coverage agreements. Over the next 12 to 24 months, however, we believe that the company may have fewer favorable reserve releases.

Regional segment

Regional gross premiums decreased by about 6% in 2010 from the prior year. In 2010, premium pricing had stabilized significantly from 2008 and 2009. An increase in favorable loss reserve development contributed to the decline in loss ratios to 60.7% from 61.4% and 65.2%, respectively. The premium pricing stabilization has also reduced the loss ratios in the first half of 2011, excluding weather-related losses. Both a decrease in net written premiums and the build-up of the Berkley North Pacific group in 2010 aided the slight increase in expense ratio for the segment.

Alternative segment

Alternative markets' gross premiums increased by 6% in 2010 from the prior year. The increase in the loss expense ratio in 2010 reflected a decrease in favorable loss reserve development compared with the prior year. However, we believe that the segment's combined ratio is still strong relative to the industry and most of WRB's peers.

Reinsurance segment

Although GPW has fallen by 7% in 2010 as a result of the soft market, the segment has maintained strong underwriting standards, and its loss ratios have decreased to 52.5% from 57.9% in 2009. A modest increase in premium rates and professional liability policies' favorable claims mitigated the decline in premiums through 2010. The slight increase of the expense ratio in 2010 is a result of the reduced premium.

International segment

Although the company has been expanding into new international markets, it has maintained strong underwriting discipline, and the loss ratios have remained relatively consistent throughout 2007 to 2011. The Chilean earthquake losses of \$4 million (less than 1% on the loss ratio) and a reduction in favorable loss reserve development hurt the segment performance in 2010. We expect expense ratios to continue to remain high as the company ramps up its international operations.

Prospective

We believe that although insurance market conditions will continue to challenge WRB's operating performance in 2011 and 2012, the group's solid underwriting performance will fuel a positive operating performance.

Investments And Liquidity: Focuses On Maximizing Long-Term, After-Tax Returns

We view investments and liquidity as strong because the high-quality bonds portfolio contributes to strong liquidity. WRB's risk-management philosophy calls for assuming insurance risk while minimizing investment risk.

As of June 30, 2011, the consolidated group allocated 80% of its investments in fixed-income securities, 6% in cash and cash equivalents, 4% in equity securities, 5% in merger arbitrage, and 7% in other investments. WRB manages the assets for all its subsidiaries with a focus on maximizing long-term, after-tax returns. The average credit quality of the fixed income portfolio is 'AA', with an average duration of 3.5 years at June 30, 2011.

WRB's predominantly focuses its fixed-maturity portfolio on state and municipal holdings (48% as of June 30, 2011), MBS (16%), corporates (21%), U.S. government agency (7%), and foreign governments (8%). The state and municipal holdings are primarily revenue-backed bonds (48%), prerefunded bonds (26%), and general obligation bonds (including leases, 26%). As of June 30, 2011, Standard & Poor's rated 45% of the fixed-income portfolio 'AAA' with 'AA', 'A', and 'BBB' ratings comprising 23%, 16% and 11%, respectively. As of June 30, 2011, WRB's

fixed-income portfolio had gross unrealized gains and gross unrealized losses of \$504 million and \$62.5 million, respectively. The total fixed-maturity portfolio (\$11.3 billion fair value) exceeds the total reserve for losses and loss expenses of \$9.2 billion.

WRB maintains 5% of its invested assets in a trading account focused on merger arbitrage. As of June 30 2011, WRB increased its trading account investment to \$536 million from \$420 million at year-end 2010. Merger arbitrage entails investing in securities of publicly traded companies that are the targets in announced tender offers and mergers. Usually, the change in value is four months or less.

Historically, a growing book of profitable business that generated net operating cash flows of \$1.6 billion in 2008 and \$1.5 billion in 2007 supported the company's liquidity. Although, because of reduced premium volume borne from disciplined underwriting when prices decline, cash flow from operating activities had shrunk to \$316 million in 2009. In 2010, however, it was \$451 million, and in the first half of 2011, the company reported net operating cash flows of \$216 million, which is higher than \$186 million in the first half of 2010. In addition, the company had \$795 million in cash and cash equivalents at June 30, 2011. Its statutory underwriting and operating cash flow ratios remain strong and supportive of the rating at about 100% and 112% at year-end 2010, respectively.

Table 4

W.R. Berkley Corp.'s Operating Companies--Investment Statistics					
(%)	2010	2009	2008	2007	2006
Equity investment	7.2	6.0	7.6	11.1	12.7
Investment-grade bonds	78.1	83.3	77.2	73.9	77.2
Speculative-grade bonds	4.1	0.0	0.0	0.0	0.0
Mortgages and loans	2.6	2.8	3.0	2.5	0.0
Cash and short-term investments	4.7	3.8	9.0	7.1	6.4
Other investment	3.3	4.0	3.1	5.3	3.8
Investments in affiliates	0.0	0.0	0.0	0.0	0.0
Total	100.0	100.0	100.0	100.0	100.0

Prospective

Standard & Poor's expects WRB to maintain its actively managed investment portfolio and for the high-quality fixed-income portfolio to support future obligations. The company will continue to manage and measure assets in terms of duration and diversification at the holding company level. We expect the company, through its prudent underwriting, to be able to continue its strong operating cash flow performance. However, we also believe that with potentially higher reinvestment risk, WRB will find it more difficult to achieve the investment yields it has in the past.

Capitalization

We view capital as a weakness to the rating because WRB manages capital aggressively and opportunistically, though it is prudent. Accordingly, management is willing to temporarily operate with capital that is lower than what we expect for the rating when it perceives opportunities. For 2010, WRB ceded approximately 11% of its premiums to reinsurers, and its net recoverables-to-surplus ratio was 25% on statutory basis. Even though it's lower than what we expect for the rating, we considered Berkley's capitalization to be good at year-end 2010, especially when considering qualitative aspects such as nonmaterial catastrophe exposure, relatively low policy limits, and below

average reinsurance recoverable exposure. We believe that, consistent with the past, Berkley will continue to stress capital in the pursuit of profitable growth opportunities.

Prospective

Standard & Poor's expects WRB to continue to manage low capital adequacy for the rating to take advantage of business opportunities. We believe WRB will also maintain its strategy of maximizing return on capital by using earnings to pursue profitable growth, share repurchases, or other investor measures. Accordingly, there will be periods when capitalization will fall modestly lower than what we expect for the rating on WRB. The strong level of earnings from its highly diversified, well-positioned subsidiaries offsets this weakness. But when WRB allows capital to fall while pursuing growth, Berkley's capital will be less able to withstand volatility from an underwriting standpoint when it is booking materially larger volumes of new business.

Reserves

We believe that WRB's reserving practices are reasonable and adding actuarial talent and improving processes in recent years has enhanced them, thereby reducing the chance of adverse development as in 2004 through 2006 when prior-year reserves increased an aggregate \$509 million. Reserves for more recent years have developed favorably with favorable prior-year reserve developments of \$234 million and \$86 million in 2010 and the first six months of 2011, respectively. Favorable reserve development is mainly because of tighter excess-and-surplus policy contract language, which resulted in lower observed claims frequency for policies underwritten in 2003 through 2007, and fewer miles driven in 2008 and 2009, which resulted in fewer claims for commercial auto policies. WRB's relatively conservative inflation assumption of 5% to 6% on a more-than-three years weighted duration reserve base adds some cushion to its reserve balance. Although WRB has had a favorable development on reserves for recent accident years, it continues to have adverse reserve development in older accident years. We believe that the company may have lower favorable reserve releases over the next 12-24 months.

Reinsurance WRB's strategy of writing relatively low casualty policy limits relative to its GAAP equity base (\$3.9 billion as of June 2011) leads the group to rely less on reinsurance than many of its peers. Limited property exposure further lessens the company's reinsurance requirements. Reinsurance utilization, including servicing carrier business, was about 12% in 2010, 13% in 2009, and 10% in 2008. This nonaffiliated reinsurance utilization ratio is near the lowest in the peer group. Reinsurance recoverables of \$968.3 billion constitute 25% of GAAP equity from a high quality of reinsurers.

Financial Flexibility

We view WRB's financial flexibility as strong and appropriate for the rating category based on its successful access to the equity and debt markets and consistently strong operating performance. However, WRB has aggressively managed its financial leverage. In September 2010, the company issued \$300 million of 5.375% senior notes due 2020 and repaid its \$150 million of 5.125% senior notes upon maturity. Although financial leverage declined to 32.7% as of June 2011 from its December 2005 peak of 37.8%, WRB is willing to temporarily manage its financial leverage to a somewhat aggressive level—up to 35%—when management believes profitable growth opportunities are available. As a result, any unexpected capital shortfall would, more so than for many peers, result in the potential need to access the more difficult equity markets rather than issue a debt or hybrid security. The company's tolerance for relatively high financial leverage and somewhat aggressive capitalization for the rating category is a reflection of its risk profile (low catastrophe exposed profile). However, Standard & Poor's views it as a modest strain on financial flexibility, particularly if its operations were to suffer an unexpected, materially adverse event.

The possibility of increasing its currently low use of reinsurance, as well as a favorable long-term maturity schedule, somewhat offsets this concern. WRB has \$200 million prospective maturities in 2013, \$200 million in 2015, \$450 million in 2019, \$300 million in 2020, \$76 million in 2022, \$625,000 in 2023, and \$250 million in 2037, with \$250 million of subordinated debentures due in 2045. WRB has no short-term debt in the form of commercial paper or bank lines outstanding. Furthermore, the company has strong statutory underwriting and operating cash flows, with 2010 ratios of 100% and 112%, respectively.

Catastrophe exposures in terms of hurricanes and earthquakes are limited, given Berkley's casualty-focused business profile. A 1-in-250-year net aggregate probable maximum loss was less than 5.5% of GAAP equity as of December 2010.

Standard & Poor's expects debt leverage to remain less than 35%, and that fixed-charge coverage will be greater than 5x excluding realized investment and investment fund losses.

Related Criteria And Research

- Holding Company Analysis, June 11, 2009
- Analysis Of Nonlife Insurance Operating Performance, April 22, 2009

Ratings Detail (As Of October 3, 2011)*	
Holding Company: W.R. Berkley Corp.	
Issuer Credit Rating	
Local Currency	BBB+/Stable/--
Preferred Stock (2 Issues)	BBB-
Senior Unsecured (7 Issues)	BBB+
Operating Companies Covered By This Report	
Firemen's Insurance Co. of Washington DC	
Financial Strength Rating	
Local Currency	A+/Stable/--
Counterparty Credit Rating	
Local Currency	A+/Stable/--
Acadia Insurance Co.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
Admiral Indemnity Co.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
Admiral Insurance Co.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--

Ratings Detail (As Of October 3, 2011)* (cont.)	
Berkley Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Berkley National Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Berkley Regional Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Berkley Regional Specialty Ins Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Carolina Casualty Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Clermont Ins Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Continental Western Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Gemini Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Great Divide Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--

Ratings Detail (As Of October 3, 2011)***(cont.)**

Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Key Risk Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Midwest Employers Casualty Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Nautilus Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Preferred Employers Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Riverport Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
StarNet Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Tri State Insurance Co. of MN	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
Union Insurance Co.	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--

Ratings Detail (As Of October 3, 2011)***(cont.)**

Union Standard Lloyds

Financial Strength Rating

Local Currency

A+/Stable/--

Issuer Credit Rating

Local Currency

A+/Stable/--

Domicile

District Of Columbia

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

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