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# W.R. Berkley Corp. And Operating Subsidiaries

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# W.R. Berkley Corp. And Operating Subsidiaries

## Major Rating Factors

### Strengths:

- Very strong operating performance.
- Strong, well-diversified competitive position.
- Strong liquidity.

### Weaknesses:

- Somewhat aggressive historical financial leverage at the holding company.
- Operating company capital levels that are well supportive of the rating, though they may be pressured in the growth phase of the underwriting cycle.

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

## Rationale

The counterparty credit rating on W.R. Berkley Corp. (WRB) and the insurer financial strength ratings on its operating insurance companies (collectively referred to as Berkley) reflect Berkley's very strong operating performance; strong, well-diversified competitive position; and strong liquidity. Offsetting these strengths are WRB's somewhat aggressive historical financial leverage and operating company capital levels that, although currently are well supportive of the rating, have in the past trended below the rating as the companies pursued growth opportunities.

Berkley's pretax income before minority interest of \$359.8 million during the six months ended June 2008 (combined ratio of 91.7% and a pretax return on revenue, or ROR, of 14.9%) though lagging prior year-to-date performance (combined ratio of 87% and a pretax ROR of 19.2%), does remain very strong and consistent with expectations. The modest deterioration in operating performance in the first half of 2008 resulted mainly from the large amount of attritional catastrophe losses in the regional segment and a challenging pricing environment that has particularly affected the reinsurance and specialty segments. The continuation of the diversified insurance operating entities' very strong and consistent performance over the past seven years is a key strength to the rating.

Berkley's competitive position is strong, based on its well-diversified revenue profile, long-standing relationships with producers, economies of scale, and market position. Berkley 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. Berkley's long-term relationships with brokers and agents have allowed it to compete effectively with larger peers.

Liquidity is strong, supported by high-quality fixed maturities and cash equivalents constituting 81% of the investment portfolio and operating cash flows borne from a very strong earnings profile. The average credit quality of the bond portfolio is 'AA', with an average duration of 3.6 years. Notwithstanding an expected third-quarter 2008 other-than-temporary impairment charge that will materially diminish quarterly earnings, WRB's overall portfolio is sound as evidenced by net unrealized losses of \$35.9 million as of June 30, 2008, on a total portfolio of

\$11.8 billion.

Berkley is an aggressive, though prudent, manager of capital. Although capitalization at the operating companies is currently appropriate for the rating level, the pursuit of rapid growth (35% in 2003 and 16% in 2004) to capitalize on favorable pricing and underwriting resulted in capitalization temporarily deteriorating to a level below the rating category before being restored to appropriate levels for the rating in 2005. At the same time, financial leverage at the holding company was high for the rating, with total leverage ranging from 36% to 38% during the three years ended December 2005. Although current capital adequacy and financial leverage (28% as of June 2008) are well supportive of the rating, we believe WRB may continue to stress capital and financial leverage as it pursues growth opportunities, particularly when the underwriting cycle becomes more favorable.

## Factors Specific To Holding Company

Standard & Poor's Ratings Services applies standard notching (one full category) between the operating companies and their holding company, WRB. The three notch difference reflects the holding company's dependence on dividends from its operating subsidiaries and regulators' ability to prohibit those dividends. As of year-end 2007, dividends available from the subsidiaries to WRB without prior regulatory approval totaled \$653 million.

Holding company financial metrics are consistent with the rating, with debt leverage of 22.9% and intermediate hybrid equity leverage of 5.2% as of June 2008. WRB modestly exceeds our debt double-leverage tolerance by \$73 million. Consistent with our criteria, we reduce our view of capital at the operating company level by this amount. Even with this modest adjustment, we view operating company capitalization as strong and well supportive of the rating. WRB's fixed-charge coverage ratio, excluding realized gains/losses, of 12x in 2007 marks the fourth consecutive calendar year of fixed-charge coverage approaching or exceeding the double digits. We view this performance as extremely strong, reflecting WRB's consistent track record of performing at levels above the rating. Although adverse pricing conditions are expected to result in lower earnings and coverage metrics in the next one to two years, 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 opportunities, as evidenced by total financial leverage exceeding 35% in the height of the favorable market cycle in 2005. As demonstrated by currently appropriate capital and financial leverage metrics, the company has a tolerance for leverage variances, with higher and somewhat aggressive tolerances in hard markets and lower tolerances in soft markets. Standard & Poor's views this as a modest strain on financial flexibility, particularly if the company were to experience an unexpected and materially adverse event to its operations at a time of somewhat aggressive financial metrics.

**Table 1**

<b>W.R. Berkley Corp./Financial Statistics</b>					
	<b>--Through second quarter--</b>		<b>--Year ended Dec. 31--</b>		
	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
GAAP interest coverage (EBIT) (x)	11.3	14.7	13.3	12.7	12.4
GAAP fixed-charge coverage (EBIT) (x)	9.3	12.0	11.0	9.3	9.4
Statutory interest coverage (x)	N.A.	6.8	3.0	3.4	3.1
Statutory fixed-charge coverage (x)	N.A.	5.6	2.5	2.5	2.4

**Table 1**

W.R. Berkley Corp./Financial Statistics(cont.)					
Debt leverage (%)	22.9	23.3	21.5	26.2	29.1
Hybrid leverage (%)	5.2	4.8	5.6	11.5	7.0
Financial leverage (%)	28.0	28.1	27.1	37.7	36.1

N.A.—Not available.

**Chart 1**

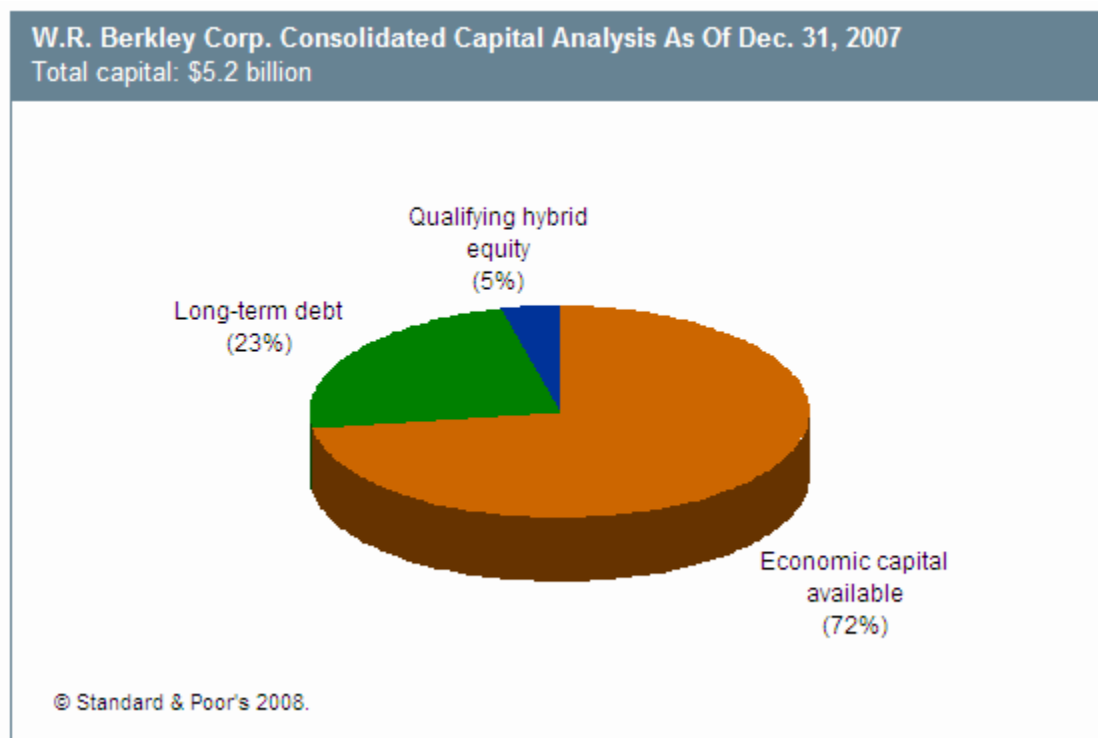
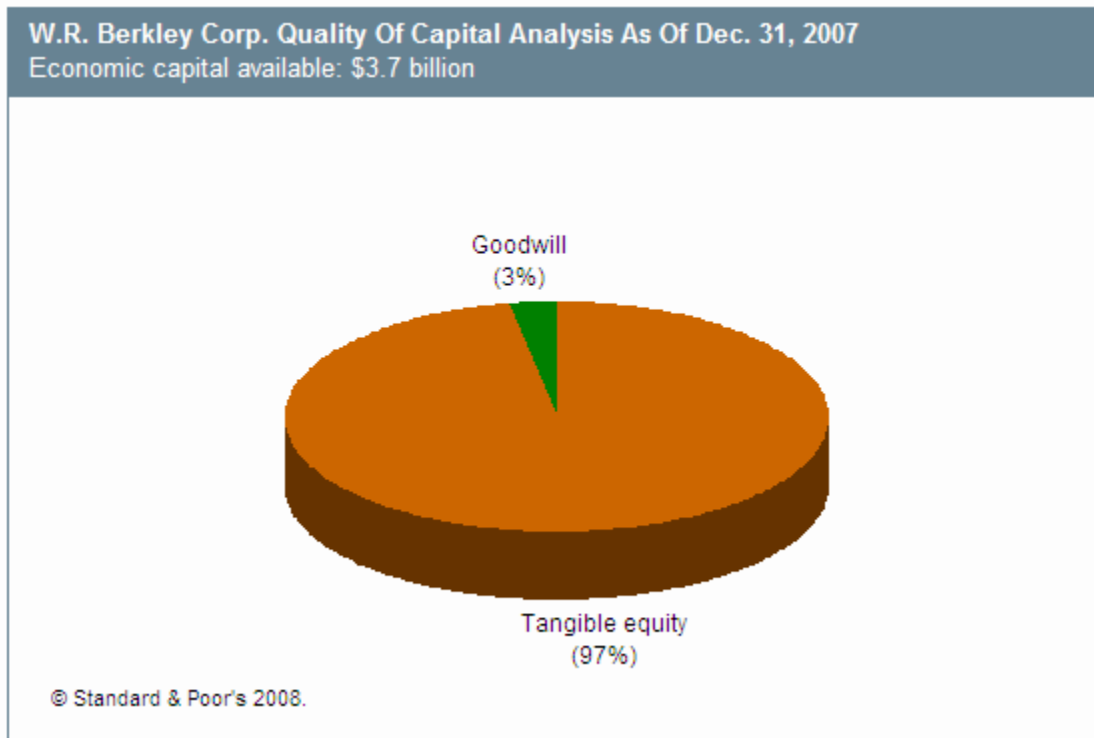


Chart 2



## Outlook

The outlook is stable because the very strong earnings from the solidly positioned, diversified subsidiaries will offset our expectation that Berkley will continue to manage its capital at an aggressive, though prudent, level for the rating. An adverse change to Berkley's very strong earnings profile or a diminished view of its enterprise risk management (ERM) at the operating company level could result in an outlook revision to negative. Alternatively, we could revise the outlook to positive if Berkley improves its ERM to the strong level and if it maintains capital adequacy and financial leverage well into the strong level while sustaining very strong earnings, thereby demonstrating its strong competitive profile.

The Standard & Poor's capital adequacy ratio at the operating company level likely will remain strong and appropriate for the rating, with holding company financial leverage remaining significantly less than 35%. Although we expect difficult market conditions to pressure WRB's top-line and bottom-line operating performance, the company will sustain a very strong operating performance, with a combined ratio well below 95% and fixed-charge coverage, excluding realized investment gain/losses, exceeding 8x.

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

Berkley's competitive position is strong, based on its well-diversified revenue profile, long-standing relationships

with producers, and economies of scale. Berkley's success in recent years booking very strong operating results further demonstrates its competitive strength. In 2007, Berkley was ranked the 18th-largest P/C insurance company and the ninth-largest commercial lines insurer in the U.S. based on net premiums written of \$3.9 billion. The reinsurance operations generated an additional \$682 million in net premiums written in 2007.

Berkley is well diversified by business segment, line of business within each segment, and distribution. In addition, all of these segments--particularly the well-performing specialty and regional segments, which have generated net premium volume of 36% and 29%, respectively, with combined ratios of less than 91% in each year since 2001--are highly profitable. The diversified nature of the group's strongly positioned operating segments is a strength to the rating.

**Table 2**

<b>W.R. Berkley Corp.'s Operating Companies/Business Statistics</b>					
	<b>--Through second quarter--</b>		<b>--Year ended Dec. 31--</b>		
<b>(Mil. \$)</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
Gross premiums written	2,399.9	5,053.2	5,277.0	5,088.0	4,724.1
Year-over-year change (%)	(9.4)	(4.2)	3.7	7.7	11.3
Net premiums written	2,149.1	4,576.0	4,819.0	4,604.6	4,266.4
Year-over-year change (%)	(10.1)	(5.0)	4.6	7.9	16.2
Reinsurance utilization (%)	10.4	9.4	8.7	9.5	9.7
<b>Net premiums by line of business</b>					
Specialty insurance (%)	36	37.3	37.7	39.8	35.1
Alternative markets (%)	15.8	14.3	13.5	14.5	15.0
Reinsurance (%)	11.6	14.9	18.5	15.6	19.3
Regional (%)	29.7	27.7	25.6	26.0	26.5
International (%)	6.9	5.8	4.7	4.1	4.1

### Specialty segment

The specialty segment (36% of consolidated gross premiums written, or GPW, in 2007) has a strong competitive position based on its contribution within the excess and surplus lines and admitted specialty markets (\$1.7 billion of net earned premiums in 2007), specialized products, and long-term relationships with its distributors. Although this business is highly competitive, with net premium volumes declining by more than 15% during the six months ended June 2008, Berkley has a long and established competitive position in this segment and continues to realize very strong industry leading margins while sustaining a strong market presence.

Berkley conducts its specialty business through nine operating units focusing on different customer bases and product offerings.

Admiral Insurance Co. (28% of segment GPW in 2007) 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 (\$29,000 average premium) is through wholesale brokers to middle-market commercial accounts.

Nautilus Insurance Co. (18% of GPW in the segment), though marketing similar products, targets less complex risk (\$3,000 average premium) from significantly smaller clients. Unlike Admiral, Nautilus business is written on a

binding authority basis, or individually underwritten wholesale broker business.

Vela Insurance Services contributed 8% of the specialty segment's GPW in 2007. Vela also focuses on small to midsize accounts and mainly writes contractors and products liability on a primary basis.

Carolina Casualty Insurance Co. (15% of 2007 specialty segment GPW) specializes in transportation insurance for intermediate- and long-haul trucking, as well as various classes of business and public auto risks. The Carolina Casualty business is split between general agent and brokerage channels.

The remaining specialty operating units (31% of the segment's GPW) pursue similarly focused specialty business in the U.S. On a GPW basis, premises operations constituted 38% of 2007 consolidated specialty business, with commercial auto (16%), product liability (12%), professional liability (10%), commercial property (14%), and other (10%) rounding out the book of business.

### **Regional segment**

The regional segment's (29% of 2007 consolidated GPW) competitive position is strong, based on its position within commercial lines, providing products to Berkley's customers primarily in 48 states and the District of Columbia. Leveraging solid agency relationships and a commitment to customer focus, the regional segment has countered larger competitors, as evidenced by this segment's minor 4.5% net premium written decline during the six months ended June 2008. Given WRB's historically very strong profitability, this speaks to the solid diversified competitive presence of this segment. The specific target market of WRB's regional platforms is small to midsize businesses and governmental entities. Business is well diversified by state, with the top five states—Massachusetts (7%), Kansas (6.1%), Texas (6.4%), Pennsylvania (5.8%), and New Hampshire (5.1%)—constituting 30% of direct premium volume in 2007. The next five states contributed an additional 20% of total writings. Commercial multiperil constituted 35% of total business by line in 2007, with commercial auto (26%), workers' compensation (18%), assigned risk plans (6%), and other lines (16%) rounding out the book of business.

### **Alternative segment**

The alternative segment (15% of 2007 consolidated GPW) provides a variety of fee-based (consulting and administrative) services and risk-transfer mechanisms. Midwest Employers Casualty Co. (45% of 2007 gross segment premiums) provides excess workers' compensation to self-insured employers and groups above their self-insured or retention limits. Preferred Employers Insurance Co. (11%) offers primary workers' compensation to owner-managed small employers in California. Berkley Risk Administrators (8%) is a nationwide third-party administrator of P/C insurance claims, policy, and underwriting services. Key Risk Insurance Co. (18%) offers primary workers' compensation principally in North Carolina.

### **Reinsurance segment**

Like its primary operations, BER's reinsurance operations (14% of 2007 consolidated GPW) focus on specialty lines of business, offering reinsurance on an individual basis primarily through facultative reinsurance, as well as treaty reinsurance. The segment writes the majority of its business on behalf of Berkley Insurance Co. (BIC). The reinsurance business originates primarily from brokers, 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: Signet Star (40% of total GPW) focuses on casualty excess-of-loss treaties produced through reinsurance brokers and intermediaries. Facultative ReSources Inc. (17%) specializes in individual certificate and program facultative business produced through brokers. BF Re (11%) is a direct casualty facultative reinsurance underwriting manager.

Berkley also maintains a reinsurance presence in the Lloyd's market that constituted 23% of Berkley's overall reinsurance book in 2007, where it assumes a range of short-tailed lines (including some catastrophe-exposed property) through a Lloyd's syndicate. In 2007, the reinsurance business had a 76%/24% split between casualty and property.

The reinsurance segment has grown by more than 30% since 2002, consistent with management's strategy of selectively pursuing profitable growth as rates increased considerably during this time period. As with Berkley's other segments, we expect underwriting profit considerations to drive growth.

### **International segment**

Berkley's international segment (6% of 2007 consolidated GPW) has operations in Europe (mainly the U.K. and Spain), South America, Asia, and Australia. Berkley writes about \$160 million of casualty business in Europe, primarily professional lines. The company continues to demonstrate a commitment to growing its international books of business. The goal is to establish these operations in the current competitive market and realize growth when market opportunities present themselves. In addition to a solid presence in the U.K. through W.R. Berkley Insurance (Europe), the company has established a South America presence, as evidenced by its position as the 10th-largest P/C insurer in Argentina. In addition, Berkley maintains reinsurance branches in Hong Kong and Australia.

### **Prospective**

Notwithstanding premium declines borne from disciplined underwriting in a highly competitive pricing environment, Berkley's competitive position will remain strong, as evidenced by very strong profitability, while maintaining scale. We expect consolidated net premiums to decline in the low double digits, stemming primarily from material declines in the specialty and reinsurance segments. These segments have been hurt most by competitive pricing pressures, consistent with the current soft stage of the industry underwriting cycle. Standard & Poor's expects business volume in the regional and alternative markets to remain stable, with single-digit declines resulting from pricing rather than from exposure reductions. The international segment will continue to expand in 2008, with growth in 2009 dependent on market conditions.

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

WRB's corporate strategy focuses on providing a stable return to its stockholders through its diversified insurance operations in five P/C markets. The consolidated group's corporate strategy, though well executed (as measured by its very strong diversified operating performance), historically has been aggressive. Berkley manages aggressive financial leverage and operating company capitalization in times of business opportunities. During the height of the favorable market cycle in 2003 through 2005, when WRB aggressively and profitably grew its business, it had financial leverage well in excess of 30%. At the same time, capital at the operating company level, though strong, was below the rating level. Notwithstanding WRB's current conservative profile (strong capitalization, appropriate financial leverage, declining premium volume in response to difficult market conditions) the willingness to aggressively pursue prospective business opportunities through a somewhat aggressive capital and financial leverage structure increases risk within the organization.

Berkley'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. The 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 are monitored closely by the parent company. The successful execution of this is a testament to the company's operational management.

Standard & Poor's recognizes the strong historical track record of astute strategic decision making, as well as the material roles of the group-level senior vice presidents and individual operating company presidents in executing the group's strategic direction. Notwithstanding, we believe that strategic decision making is more concentrated at the executive management level at Berkley than it is at many similarly rated peers. Although the continued development and institutionalization of ERM will address and remediate this concern on a prospective basis, the potential exists that an unforeseen change in executive management, though not detrimental to ongoing operations, could hurt the company's historically successful strategic decision-making processes.

## Enterprise Risk Management: Favorable Underwriting, With A Focus On The Risks And Exposures It Knows Best

Standard & Poor's considers WRB's ERM to be adequate. This is supported by strong insurance risk controls in underwriting, pricing, and cycle management, which all follow a conservative and traditional process. The organization's favorable underwriting results support the effectiveness of these controls.

Risk management is an integral concept to the CEO, and this has been ingrained throughout the organization. The company's operational strategy of focusing on low-limit casualty business (80% below \$1 million, 90% below \$2 million, 99% below \$10 million) enables it to minimize reinsurance (reinsurance utilization was 9.2% in 2007) and to stay focused on risks and exposures where its most knowledgeable.

Part of the company's risk strategy is to avoid significant catastrophe and investment risks while concentrating its resources on the profitable underwriting of a diversified array of casualty business. WRB manages exposures to full maximum loss rather than a probable maximum loss. This conservative approach significantly limits the company's dependency on vendor models.

The ERM process with oversight and coordinated from the corporate home office coincides with the general management of the organization. Risk assessment for insurance is less model dependent than are other commercial carriers, but risk assessment follows a disciplined qualitative approach, in which sound judgment and experience drive most decisions. WRB has a formal economic capital model in development, which likely will be fully implemented in 2009. We view this as an enhancement that, over time, should create a favorable balance of qualitative and quantitative understanding of all risks the company faces.

Notwithstanding the integral role of the company presidents, senior vice presidents, and executive vice president, a lingering concern is key-man risk associated with the highly influential CEO who has successfully guided WRB since inception in 1967. Despite evidence of a decentralized structure, the CEO does appear to have significant influence on the company's risk management, including establishing group-level risk tolerance and making strategic risk decisions. In some cases, this is more pronounced than most other insurers'.

Over time, WRB may be positioned to migrate to strong ERM. However, two factors are necessary to support that

assessment. One is evidence of a fully implemented economic capital model that is ingrained in the culture of the organization and supports strong strategic risk management. The other is continued evidence of a broad and diverse strategic decision-making structure that limits the key-man risk and associated dependencies.

We believe WRB is unlikely to experience losses outside of what is normal for its traditional risk areas.

## Accounting

WRB is a publicly traded entity subject to SEC filings. In addition, its insurance company subsidiaries are required to file statutory statements. KPMG audited the GAAP consolidated balance sheets as of Dec. 31, 2007, 2006, and 2005, and the related consolidated income statement and changes in shareholders' equity and cash flows for the three years ended Dec. 31, 2007, expressing an unqualified opinion. Standard & Poor's is unaware of any regulatory inquiry in Berkley's financial reporting. The company filed all financial statements, statutory and GAAP, on a timely basis.

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 statutory 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. In addition, certain publicly traded investments, with the exception of ownership of holding company stocks that are classified as affiliated on Berkley's statutory statements, have been reclassified as unaffiliated common stock, and we have applied the related capital charge to our capital model.

## Operating Performance: Difficult Pricing Will Pose A Challenge, But Underwriting And Profitability Should Support Performance

Berkley's consistently very strong and diversified operating performance is at the top of its peer group and is a significant strength to the rating. Given the company's somewhat aggressive capital management for the rating, the operating performance is the primary supporting factor for the rating and outlook.

**Table 3**

<b>W.R. Berkley Corp.'s Operating Companies/Operating Statistics</b>						
<b>(Mil. \$)</b>	<b>--Through second</b>	<b>--Year ended Dec. 31--</b>				
	<b>quarter--</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
Total revenue (excluding realized gains/losses)		2,602.4	5,538.7	5,385.2	4,979.6	4,463.9
Underwriting gain or loss		79.9	353.3	380.0	320.5	253.8
Pretax income (before minority interest and excluding realized gains)		387.9	1,042.7	978.9	753.3	590.2
Net income (before minority interest)		268.8	746.7	702.2	548.0	441.5
Pretax operating return on revenue (%)		14.9	18.8	18.2	15.1	13.2
Pretax operating return on equity (%)		10.5	30.3	33.5	32.2	34.6
Loss ratio (%)		62	59.6	61.0	62.4	63.0
Expense ratio (%)		29.7	28.5	27.0	26.9	27.4
Combined ratio (%)		91.7	88.1	88.0	89.3	90.4

**Table 3**

<b>W.R. Berkley Corp.'s Operating Companies/Operating Statistics (cont.)</b>					
Net cash flow from operating activities	405.3	1,479.7	1,564.0	1,719.8	1,619.7
Net cash flow from investing activities	(161.3)	(1,047.5)	(1,165.4)	(2,355.8)	(2,282.6)
Net cash flow from financing activities	(583.4)	(244.2)	(342.7)	376.9	163.5

**Historical**

Operating performance has improved steadily over the past several years. Pretax income before minority interest increased to \$989 million in 2006 (combined ratio of 88%) from \$770 million in 2005 (combined ratio of 89.3%) and \$639 million in 2004 (combined ratio of 90.4%). In this three-year period, the reinsurance and international segments did not perform as strongly as the other business segments, producing an average combined ratio of 100.8% and 94.4%, respectively. The alternative markets segment showed good improvement in 2006, lowering the combined ratio to 75.6% from more than 91% in 2004 and 2003.

**Current performance**

Berkley's 2007 pretax income before minority interest of \$1.1 billion (combined ratio of 88%, pretax ROR of 19%) marked the continuation of very strong performance from previous years. In 2006, the results were \$989 million, 88%, and 18%, respectively. These very strong results incorporated prior-year reserve releases of \$106 million in 2007 and reserve additions of \$27 million in 2006.

Berkley's pretax income before minority interest of \$359.8 million during the six months ended June 2008 (combined ratio of 91.7%, pretax ROR of 14.9%) though lagging prior year-to-date performance in the same period of 2007 (combined ratio of 87%, pretax ROR of 19.2%), does remain very strong and consistent with expectations. The modest deterioration in operating performance in the first half of 2008 is mainly attributed to the large amount of attritional catastrophe losses in the regional segment and challenging pricing that has particularly affected the reinsurance and specialty segments.

**Prospective**

Berkley's operating performance in 2008 will be pressured from a top-line and bottom-line prospective by challenging pricing. However, we believe that, although Berkley's overall profitability will decline, underwriting performance and overall profitability will remain a key strength to the rating. Specifically, we expect underwriting performance to be well above industry averages, with a combined ratio of less than 95%. This is particularly impressive given the long-tail casualty nature of WRB's book of business. In addition, we expect a pretax ROR well in excess of 15%.

**Investments And Liquidity: Focuses On Maximizing Long-Term, Aftertax Returns**

We view investments and liquidity as strong, based on high-quality bonds contributing to strong liquidity.

As of year-end 2007, the consolidated group allocated its investments as follows: fixed-income securities, 74%; equities, 15%; cash and cash equivalents, 7%; and other investments, 4%. WRB manages the assets for all its subsidiaries with a focus on maximizing long-term, aftertax returns. The holding company's investment strategy also entails diversification of risk to preserve principal values. The average credit quality of the bond portfolio is 'AA', with an average duration of 3.6 years.

Table 4

<b>W.R. Berkley Corp.'s Operating Companies/Investment Statistics</b>					
<b>(Mil. \$)</b>	<b>--Through second quarter--</b>		<b>--Year ended Dec. 31--</b>		
	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
Invested assets	12,726	13,188	12,012.3	10,378.3	8,341.9
Year-over-year change (%)	0.5	9.79	15.74	24.4	28.7
Net investment income	298.4	672.7	586.1	404.0	291.3
Net investment yield (%)	4.6	5.3	5.2	4.3	3.9
Realized capital gains or losses	(28.10)	14.9	10.0	17.2	48.3
Total yield (%)	4.6	5.4	5.3	4.5	4.6
Net investment income to net premiums earned (%)	13.6	14.4	12.5	9.1	7.2
Shareholders' equity (including minority interest)	3,281.9	3,605.2	3,365.8	2,588.4	2,155.9
<b>Portfolio composition (% of invested assets)</b>					
Bonds (including mortgage-backed securities)	79.2	76.3	76.2	81.8	76.4
Common stocks	9.4	9.7	12.5	9.7	8.3
Other investments	6.5	6.7	5.1	2.1	4.2
Cash and cash equivalents	4.8	7.2	6.2	6.5	11.2

Berkley maintains a portion of its invested assets in a trading account focused on merger arbitrage. Berkley has increased its trading account investment to \$855 million (6.4% of total invested assets) as of year-end 2007 from \$783 million (7% of invested assets) at the end of 2006. Merger arbitrage is the business of 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.

In 2007, Berkley acquired two fixed-based operators, which each provide services to the general aviation market. As wholly owned investees, these investments flow through the revenue and expense lines of WRB's income statement. In 2007, revenues associated with these investments totaled \$102.8 million, with corresponding expenses of \$96.4 million.

Notwithstanding an expected third-quarter 2008 other-than-temporary impairment charge that will materially diminish quarterly earnings, WRB's overall portfolio is sound as evidenced by net unrealized losses of \$35.9 million on a total portfolio of \$11.8 billion as of June 2008.

Liquidity is supported by a growing book of profitable business that has generated net operating cash flows of \$1.5 billion in 2007, \$1.6 billion in 2006, and \$1.7 billion in 2005. However, because of reduced premium volume borne from disciplined underwriting in a declining price environment, cash flow from operating activities declined by 36.4% in the first six months of 2008 to \$405 million, relative to the same period in 2007. Cash and invested assets of \$395 million at the parent company as of year-end 2007 compares with \$89 million in interest expense recorded in 2007. The subsidiaries have dividend capacity of \$653 million that is available without prior regulatory approval.

### Prospective

Standard & Poor's expects Berkley to maintain its actively managed investment portfolio, and the high-quality, fixed-income portfolio will support future obligations. The company will continue to manage and measure assets in terms of duration and diversification at the holding company level.

## Capitalization: Aggressive, Though Prudent, Capital Management

Berkley is an aggressive, though prudent, manager of capital. Accordingly, management is willing to temporarily operate with capital that is below the rating level when it perceives opportunities. Although capital is appropriate for the rating, the pursuit of rapid growth (35% in 2003 and 16% in 2004) in response to favorable pricing and underwriting resulted in historical capital levels below the rating category. 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 Berkley to continue managing capital adequacy at an appropriate level and to maintain its strategy of maximizing return on capital by applying earnings to the pursuit of profitable growth, share repurchases, or other investor measures. Accordingly, there will be periods when capitalization will fall to or marginally below the rating level. The strong level of earnings from its highly diversified, well-positioned subsidiaries offsets this weakness. But it is important to note that when WRB is stressing capital while pursuing high levels of 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

Although Standard & Poor's rating incorporates the belief that reserves are appropriate, the material development of 1998 to 2002 accident-year reserves raises a modest concern that those periods could continue to generate adverse development. Before calendar-year 1999, Berkley managed reserves very conservatively, and Standard & Poor's considered reserves redundant. From 1999 to 2001, however, the company's reserving was deficient, resulting in reserve shortfalls, which was somewhat consistent with the industry. Subsequently, management booked prior-year reserve additions of \$295 million, \$187 million, and \$27 million in calendar-years 2004, 2005, and 2006, respectively. Reserves for the most recent accident years (2004 to 2006) have thus far developed favorably, as evidenced by \$106 million of favorable reserve development in calendar-year 2007. This addresses a modest concern regarding whether WRB appropriately reserved for the material growth pursued during this period.

### Reinsurance

WRB's strategy of writing low casualty policy limits (80% less than \$1 million, 90% less than \$2 million, 99% for less than \$10 million) relative to its capital base (\$3.6 billion as of December 2007) results in less reliance on reinsurance than many of its peers. The avoidance of property exposures further lessens the company's reinsurance requirements.

Reinsurance utilization, including servicing carrier business, was 9.4% in 2007, 8.6% in 2006, and 9.5% in 2005. This nonaffiliated reinsurance utilization ratio is near the lowest in the peer group. Reinsurance recoverables of \$905 million constitute 25% of GAAP equity.

## Financial Flexibility: Good, But Strained By Tolerance For Somewhat High Financial Leverage

Standard & Poor's views WRB's financial flexibility as good and appropriate for the rating category based on its successful accessing of the equity and debt markets and very strong fixed-charge coverage of 12x and 9.3x in 2007 and in the first half of 2008, respectively. However, WRB has been aggressive in managing its financial leverage.

Although financial leverage declined to 28% as of June 2008 from 36% as of December 2005, 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. This concern is offset somewhat by the possibility of increasing its currently low use of reinsurance, as well as a favorable long-term maturity schedule. Prospective maturities consist of \$1 million in 2009, \$150 million in 2010, \$2 million in 2012, \$200 million in 2013, \$200 million in 2015, \$150 million in 2019, \$76 million in 2022, \$12 million in 2023, \$7 million in 2035, 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.

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% of GAAP equity as of December 2007.

Standard & Poor's expects financial leverage (debt plus preferred to total capital) to remain at less than 35%, with double leverage at less than 120%, and that fixed-charge coverage will remain very strong (greater than 8x).

<b>Ratings Detail</b> (As Of September 17, 2008)*	
<b>Holding Company: W.R. Berkley Corp.</b>	
Issuer Credit Rating	
Local Currency	BBB+/Stable/--
Preferred Stock (2 Issues)	BBB-
Senior Unsecured (6 Issues)	BBB+
<b>Operating Companies Covered By This Report</b>	
<b>Acadia Insurance Co.</b>	
Financial Strength Rating	
Local Currency	A+/Stable/--
Counterparty Credit Rating	
Local Currency	A+/Stable/--
<b>Admiral Indemnity Co.</b>	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
<b>Admiral Insurance Co.</b>	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--

<b>Ratings Detail</b> (As Of September 17, 2008)* <b>(cont.)</b>	
<b>Berkley Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Berkley Regional Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Berkley Regional Specialty Ins Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Carolina Casualty Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Clermont Ins Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Continental Western Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Firemen's Insurance Co. of Washington DC</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Gemini Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Great Divide Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--

<b>Ratings Detail</b> (As Of September 17, 2008)* <b>(cont.)</b>	
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Key Risk Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Midwest Employers Casualty Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Nautilus Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Preferred Employers Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Riverport Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>StarNet Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Tri State Insurance Co. of MN</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Union Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--

<b>Ratings Detail</b> (As Of September 17, 2008)* <b>(cont.)</b>	
<b>Union Standard Insurance Co.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Union Standard Lloyds</b>	
Financial Strength Rating	
<i>Local Currency</i>	A+/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A+/Stable/--
<b>Related Entities</b>	
<b>W.R. Berkley Insurance (Europe) Ltd.</b>	
Financial Strength Rating	
<i>Local Currency</i>	A/Stable/--
Issuer Credit Rating	
<i>Local Currency</i>	A/Stable/--
<b>Domicile</b>	Maine

\*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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