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Best's Rating and Report Updates for HOUSTON CASUALTY COMPANY

Best's Rating of A+ g (Superior) Financial Size Category of XIV (\$1.5 Billion to \$2 Billion)

Rating Category (Superior): This rating is assigned to companies that have, in our opinion, a superior ability to meet their ongoing obligations to policyholders. A.M. Best assigns each letter rated (A++ through D) insurance company a **Financial Size Category (FSC)**, which is designed to provide a convenient indicator of the size of a company based on reported policyholders' surplus and conditional or reserve funds.

The objective of **Best's rating system** is to provide an opinion of an insurer's financial strength and ability to meet ongoing obligations to policyholders. Our opinions are derived from the evaluation of a company's balance sheet strength, operating performance and business profile as compared to Best's quantitative and qualitative standards. View our [Best's Rating System and Procedures](#) for more information.

While Best's Ratings reflect our **opinion** of a company's financial strength and ability to meet its ongoing obligations to policyholders, they are **not a warranty**, nor are they a recommendation of a specific policy form, contract, rate or claim practice. View our [entire notice](#) for complete details.

The rating symbols "A++", "A+", "A", "A-", "B++", and "B+" are registered certification marks of the A.M. Best Company, Inc.

Note: The above information reflects the most recent Best's Rating for this company, which may have been released subsequent to the creation of the following AMB Credit Report - Insurance Professional.

AMB Credit Report - Insurance Professional provides detailed business overview, extensive financial data and analytical commentary, product and geographic information, company history, as well as the rationale supporting the financial strength rating assigned by A.M. Best. These reports are updated on a regular basis based on input and analysis performed throughout the year.

Report Revision Date - 07/12/2009 *

The **Report Revision Date** * represents the last significant material change made to this report. Other non-material changes may have been made to this report subsequent to this date, but are not reflected in the report revision date. The AMB Credit Report - Insurance Professional below was created based on the following dates.

Rating and Commentary ¹	Financial ²	General Information ³
Best's Rating: 07/30/2008	Time Period: 1st Quarter - 2009	Corporate Structure: N/A
Rating Rationale: 07/30/2008	Last Updated: 06/24/2009	States Licensed: 07/17/2009
Report Commentary: 07/12/2009	Status: Quality Cross Checked	Officers and Directors: 07/13/2009

***Note:** The **Rating and Commentary** ¹ date outlines the most recent updates to the Company's Rating, Rationale, and Report Commentary for key rating and business changes. Report commentary may include significant changes to Business Review, Financial Performance/Earnings, Capitalization, Investment/Liquidity, or Reinsurance sections of the report. The **Financial** ² date reflects the current status of the financial tables found within the body of the Report, including whether the data was loaded as received or had been run through our quality control cross-check process. The **General Information** ³ date covers key areas that may have changed such as corporate structure, states licensed or officers and

directors.

AMB Credit Report - Insurance Professional for HOUSTON CASUALTY COMPANY

Ultimate Parent: HCC Insurance Holdings, Inc

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AMB#: 03286

NAIC#: 42374

Ultimate Parent#: 58391

FEIN#: 74-2195939

Report Revision Date: 07/12/2009

BEST'S FINANCIAL STRENGTH RATING

Based on our opinion of the consolidated Financial Strength of the property/casualty members of Houston Casualty Group, which operate under a group structure, each group member is assigned a Best's Financial Strength Rating of A+ (Superior). The company is assigned the Financial Size Category of Class XIV, which is the Financial Size Category of the group.

RATING RATIONALE

The following text is derived from the report of Houston Casualty Group.

Rating Rationale: The rating reflects Houston Casualty Group's ("the group") sustained profitability and solid level of capitalization, while also recognizing the financial flexibility and support provided by its publicly traded parent, HCC Insurance Holdings, Inc. (HCC). The rating is also indicative of the group's near-term earnings prospects considering HCC's strong position in the specialty admitted and non-admitted market segments. Partially offsetting these positive rating factors is HCC's historically above-average ceded leverage, and the additional risk caused by increasing net premium retention levels. The rating outlook reflects A.M. Best's expectation for continued underwriting and operating profitability over the near term.

The rating is supported by the group's conservative underwriting, investment and loss reserving strategies that have led to its long-term operating profitability, while also being the primary driver for its considerable balance sheet strength. Over the past several years, the group's underwriting and operating results have consistently been outstanding. Much of HCC's success stems from the group's well-defined, specialty lines business strategy and its optimum utilization of reinsurance. This strategy has led to an above-average ceded leverage position, although this leverage has been declining in recent years as the group has increased its net premium retention. Additionally, the group's utilization of high-quality reinsurers, and its proactive approach to monitoring the quality of its recoverables somewhat tempers A.M. Best's concern over ceded leverage. The rating also recognizes HCC's growth over the past five years via an expansion in the diversified financial products segment comprised of professional liability and surety coverage, and its resulting impact on net underwriting leverage. The group's overall capitalization, although remaining solid, had weakened somewhat over the last few years due to the level of premium growth and commensurate growth in related liabilities, before improving markedly in 2007, the result of another excellent year

of earnings production. As expected, underwriting leverage has stabilized during the most recent calendar years as a more than commensurate level of surplus appreciation has offset net premium growth. The group also remains exposed to large catastrophe losses due to its property and energy lines of business. On a net basis, catastrophe exposure is significantly moderated by the group's purchase of catastrophe reinsurance.

Best's Financial Strength Rating: A+ g

Outlook: Stable

FIVE YEAR RATING HISTORY

<u>Date</u>	Best's <u>FSR</u>
07/30/08	A+ g
04/15/08	A+ g
01/04/07	A+ g
11/22/06	A+ gu
06/09/06	A+ g
06/28/05	A+ g
06/29/04	A+ g

KEY FINANCIAL INDICATORS

Period <u>Ending</u>	Statutory Data (\$000)		
	Direct Premiums <u>Written</u>	Net Premiums <u>Written</u>	Pretax Operating <u>Income</u>
2004	563,332	471,045	33,920
2005	474,513	499,452	7,331
2006	409,185	485,571	175,955
2007	383,293	424,862	172,199
2008	402,027	371,997	239,246
03/2008	79,550	92,289	32,125
03/2009	80,814	67,542	26,998

Period <u>Ending</u>	Statutory Data (\$000)		
	Net <u>Income</u>	Total Admitted <u>Assets</u>	Policy- holders' <u>Surplus</u>
2004	18,526	1,663,676	604,394
2005	4,655	2,235,101	812,520
2006	160,833	2,520,418	952,083
2007	136,605	2,781,997	1,260,208
2008	179,850	2,845,690	1,345,252
03/2008	15,892	2,844,804	1,317,165
03/2009	21,998	2,917,498	1,411,886

_____ Profitability _____ Leverage _____ Liquidity _____

Period <u>Ending</u>	Comb. <u>Ratio</u>	Inv. Yield <u>(%)</u>	Pretax ROR <u>(%)</u>	NA Inv <u>Lev</u>	NPW <u>to PHS</u>	Net <u>Lev</u>	Overall Liq <u>(%)</u>	Oper. Cash- flow <u>(%)</u>
2004	96.9	3.1	8.1	-1.5	0.8	2.4	166.1	224.5
2005	105.9	2.5	1.5	14.1	0.6	2.3	164.9	317.3
2006	82.3	4.3	35.4	18.8	0.5	2.1	165.2	206.9
2007	80.1	3.2	38.0	14.7	0.3	1.5	185.1	134.0
2008	76.3	5.4	60.1	2.6	0.3	1.4	194.6	147.7
5-Yr Avg	88.6	3.9	27.9	...	...	...	...	...
03/2008	85.8	XX	35.2	XX	0.3	1.5	188.3	156.4
03/2009	93.8	XX	31.4	XX	0.2	1.3	197.3	104.6

(*) Data reflected within all tables of this report has been compiled from the company-filed statutory statement. Within several financial tables of this report, this company is compared against the Surplus Lines Composite.

BUSINESS REVIEW

The following text is derived from the report of Houston Casualty Group.

The insurance companies comprising the HCC Insurance Group provide group life, accident and health, aviation, property, marine, energy, directors' and officers' liability, professional liability, surety and other specialty lines coverages through the group's lead carrier, Houston Casualty Company (HC) and its affiliates. HC's operation includes those of a branch office in London, England.

The group's business is produced directly and through independent agents, brokers and third party administrators on a worldwide basis. HCC Insurance Holdings, Inc.'s (HCC) [NYSE: HCC] affiliated underwriting agencies act on behalf of both unaffiliated and affiliated insurance companies to provide insurance underwriting management and claim administration services while its reinsurance and insurance brokers provide a variety of additional services such as marketing, placing, consulting on and servicing risks for their clients. Aviation coverage is marketed to offshore operations, corporations, cargo operations, commuter airlines, governments and private aircraft owners on both a domestic and international basis. Facilities are currently dedicated to the handling of aircraft hull and liability insurance. In addition to conventional corporate and personal aircraft, the group covers specialty types, such as sport and antique airplanes, amphibians and seaplanes.

HCC provides accident and health coverages that are marketed directly through unaffiliated agents, brokers and third-party administrators. Property coverage is provided to large multinational corporations through HC's London branch office. The London branch also underwrites marine hull and liability coverage for ocean-going vessels, as well as onshore and offshore energy coverage for large oil companies and drilling contractors. Many of the policy forms are manuscript and tailored to meet the needs of the insured. Assumed reinsurance principally consists of accident and health reinsurance coverage, facultative aviation, and property and energy reinsurance issued by local companies in order to satisfy licensing requirements. Directors' and officers' liability and professional liability insurance is written through acquired underwriting agencies. Surety operations are consolidated within HCC Surety Group via American Contractors Indemnity Company (ACIC), United States Surety Company (USSC), Pioneer General Insurance Company (Pioneer General),

Seguros y Reaseguros S.A. (HCCE), HCC International Insurance Company PLC (HCCI) and U.S. Specialty Insurance Company (USSIC).

In January of 2004, HCC sought to increase its specialty lines platform via the acquisition of Surety Associates Holdings Company, Inc., the parent company of ACIC. ACIC specializes in court, specialty contract, license and permit, and bail bonds. In February of 2005, HCC acquired USSC via the purchase of USSC Holdings, Inc., the privately held parent company of USSC. USSC is a Maryland-domiciled carrier specializing in writing surety bonds for small-to medium-sized contractors. In December of 2005, HCC purchased MIC Life Insurance Corporation, a Delaware-domiciled company specializing in medical stop-loss business. HCC continued to expand its surety platform in 2007 through the acquisition of Colorado-based Pioneer General, a specialty underwriter specializing in bail and civil bonds, and in 2009 through the acquisition of Surety Company of the Pacific (SCOP) which specializes in California contractors' license and permit bonds. SCOP was merged into ACIC.

Workers' compensation coverage had been written by the group through USSIC, but during 2001, management decided to exit this line of business due to loss ratio and expense issues that were adversely impacting profitability. In 2001, the affiliated underwriting agencies writing workers' compensation and aviation business were consolidated with USSIC's operations. In December 1999, HCC completed the acquisition of Centris, a leading provider of medical stop-loss coverage through Centris Life Insurance Company (Centris Life) and U.S. Benefits. Subsequently, HCC contributed Centris Life to HC and renamed it HCC Life Insurance Company (HCC Life). Following the acquisition of the Centris Group, HCC became one of the largest providers of medical stop-loss coverage in the United States. HCC currently markets medical stop-loss coverage through Avemco Insurance Company (AIC) and HCC Life. Since 2003, the company continued transferring medical stop-loss business from AIC to HCC Life. Employers purchase the medical stop-loss coverage to help limit their exposure under self-insured health plans. In 2002, HCC Specialty Insurance Company (HCCSpl) was also established as an Oklahoma-domiciled subsidiary of AIC. HCCSpl's purpose is to allow HCC to write surplus lines business in Texas that HC cannot write since it is a Texas-domiciled insurer.

HCC supplements the activities of its risk-bearing companies with underwriting agencies and brokers who write on behalf of its insurance carriers and, in certain situations, other non-affiliated companies. These organizations generate fee-service income and profit commissions for the group while bearing no insurance risk. The principal agencies operating within HCC are Covenant Underwriters, Ltd. (Covenant), HCC Global Financial Products (HCCG), HCC Indemnity Guaranty Agency (HCCIG), HCC Specialty Underwriters, Inc. (HCCSU), and Professional Indemnity Agency, Inc. (PIA). The underwriting agencies specialize in the various lines of business written by the group's insurance carriers.

HCC has made numerous strategic transactions in recent years that have furthered its overall business strategy. In June of 2006, the company acquired Novia Underwriters, Inc., an underwriting agency based in Indianapolis, Indiana that specializes in medical stop-loss insurance. Novia's business has since been absorbed into Perico Life Insurance Company (PLIC). The following month the company acquired G.B. Kenrick & Associates, Inc. a Michigan-based underwriting agency specifically focused on public entity insurance. During the fourth quarter of 2006, HCC acquired the assets of the Health Products division of Allianz life Insurance Company of North America. This entity's business include medical stop-loss and medical excess insurance. HCC acquired MultiNational Underwriters (MNU) in January, 2008. MNU is an underwriting agency based in Indianapolis, Indiana. In November and December 2008 HCC acquired Cox Insurance Group, a medical stop-loss

underwriting agency whose business was absorbed by PLIC and two small underwriting operations whose business was absorbed by PIA.

Previously, in 2005, HCC acquired the remaining 66% of De Montfort Group Limited that it did not own. The key operating subsidiary of De Montfort Group was DMI, a provider of surety and credit insurance in the United Kingdom, allowing the group to further enhance its diversified financial product platform and its geographic base. In 2005, DMI was renamed HCC International Insurance Company PLC. Late in 2005, the company acquired Perico, Ltd., a medical stop-loss insurance underwriting agency domiciled in St. Louis, Missouri, and MIC Life Insurance Corporation (MIC), a Delaware-domiciled company. MIC was renamed Perico Life Insurance Company and was re-located to Missouri. In 2002, HCC acquired St. Paul Espana located in Madrid, Spain. This company provides directors' and officers' liability, professional liability and surety coverage utilizing a very experienced management team. St. Paul Espana now operates as HCC Europe.

2008 BUSINESS PRODUCTION AND PROFITABILITY (\$000)

Product Line	Premiums Written		% of Total NPW	Pure Loss Ratio	Loss & LAE Reserves
	Direct	Net			
Oth Liab CM	226,526	215,417	57.9	25.2	488,446
Aircraft	24,590	31,774	8.5	54.4	34,487
Ocean Marine	89,219	30,644	8.2	60.3	108,370
Oth Liab Occur	...	18,588	5.0	44.7	53,017
Com'l MultiPeril	...	17,645	4.7	54.3	21,061
Credit	14,253	13,196	3.5	43.9	11,345
Group A & H	13,690	7,600	2.0	3.2	309,284
Inland Marine	14,997	1,971	0.5	32.1	1,841
All Other	18,752	35,161	9.5	51.0	90,498
Totals	402,027	371,997	100.0	36.7	1,118,349

Geographical breakdown of direct premium writings (\$000): California, \$66,808 (16.6%); Louisiana, \$56,289 (14.0%); Texas, \$27,109 (6.7%); New York, \$24,001 (6.0%); Florida, \$15,810 (3.9%); 49 other jurisdictions, \$179,572 (44.7%); Canada, \$293 (0.1%); Aggregate Alien, \$32,144 (8.0%).

FINANCIAL PERFORMANCE

The following text is derived from the report of Houston Casualty Group.

Overall Earnings: On a five-year basis, the group's pre-tax and after-tax returns substantially surpass the average produced by the industry composite. This level of performance is driven by the group's underwriting discipline, expense ratio advantage and the sizeable income garnered from its investment portfolio of over \$3.4 billion. Despite overall market softening that has caused margin compression in recent years, the group has focused on specific lines of business it feels still offer profit potential. These more desirable lines of business have included the group's core aviation and accident and health segments, along with the more newly emphasized surety and professional liability lines of business.

Following a few years where calendar year profits were somewhat lessened by catastrophe-driven

losses, operating results for the last two years have benefited from relatively benign catastrophe activity. Though these events added points to the group's combined ratio, overall results have remained very profitable. Increased net investment income has also helped drive the improving profits. A small amount of adverse reserve development has had a very minimal, limiting impact on operating profits.

Competitive market pressures in recent years have compressed the group's profit margins on certain lines of business. Aggressive competition has led to the group placing less emphasis on certain lines of business while focusing on increased opportunities and more favorable profit margins in other lines of business. This has also led to increased retentions. Management has historically been able to limit the impact of pricing pressures on its bottom-line during periods of extreme competition through the increased utilization of reinsurance, primarily facultative placements. Reserve redundancies have also had a favorable impact. Substantial growth in the group's net invested asset base has fueled a commensurate increase in net investment income, further augmenting calendar year operating earnings. A.M. Best believes the group will continue to generate solid earnings despite market softening in some areas because of its diversification and ability to focus on lines of business less impacted by current market pressures. Considering the group's successful history in managing the cycle and its steadfast application of conservative operating fundamentals, A.M. Best believes operating results will remain favorable.

PROFITABILITY ANALYSIS

Period Ending	Company				Industry Composite			
	Pretax ROR (%)	Return on PHS(%)	Comb. Ratio	Oper. Ratio	Pretax ROR (%)	Return on PHS(%)	Comb. Ratio	Oper. Ratio
2004	8.1	12.0	96.9	88.7	14.9	11.2	94.4	83.1
2005	1.5	9.5	105.9	97.6	18.8	12.0	93.8	80.4
2006	35.4	10.2	82.3	65.2	33.2	18.3	80.7	65.6
2007	38.0	25.6	80.1	63.8	38.9	17.6	79.3	62.0
2008	60.1	15.3	76.3	42.1	24.4	-0.1	95.0	76.1
5-Yr Avg	27.9	15.5	88.6	72.2	26.5	11.5	88.2	72.9
03/2008	35.2	XX	85.8	64.8	XX	XX	XX	XX
03/2009	31.4	XX	93.8	75.4	XX	XX	XX	XX

Underwriting Income: Over the last five years, the group's underwriting performance has been very strong as evidenced by a combined ratio during that period that is comfortably better than that of the industry composite. A distinct loss ratio advantage, relative to the composite, has led to the well above-average historical underwriting performance. Solid results in core lines of business, partially offset by less favorable performance on the discontinued lines of business, drives the long-term favorable underwriting results.

The group has produced a net underwriting profit for six consecutive years, with the substantial profits being realized during the last two years in particular. This period of strong results has been produced despite the fact HCC has negotiated various reinsurance commutations, leading to the recording of additional losses and loss adjustment expenses as a result of the discount related to the commutations, primarily for the discontinued, assumed accident and health class of business. Unfavorable loss reserve development on the accident & health line, principally stemming from the

commutations, and to a lesser extent, adverse development on the commercial multiple peril line of business negatively impacted the still strong underwriting results. The group's combined ratio has historically benefited from a large amount of ceding commission, largely offsetting commissions paid on direct and assumed business. Increasing net retentions, however, have tempered the positive impact of ceding commissions in recent years. A.M. Best expects HCC's long-held underwriting discipline to allow the group to sustain the favorable underwriting and operating results even as segments of the market face greater price competition.

UNDERWRITING EXPERIENCE

Year	Net Undrw Income (\$000)	Loss Ratios			Expense Ratios			Div. Pol.	Comb Ratio
		Pure Loss	LAE	Loss & LAE	Net Comm	Other Exp.	Total Exp.		
2004	-833	66.5	2.9	69.4	22.6	4.8	27.5	...	96.9
2005	-33,067	71.4	4.5	75.9	23.3	6.7	30.1	...	105.9
2006	90,950	51.5	4.7	56.2	20.9	5.1	26.1	...	82.3
2007	98,128	43.4	8.6	52.0	20.7	7.4	28.1	...	80.1
2008	101,864	36.7	11.3	48.0	22.0	6.2	28.2	...	76.3
5-Yr Avg	...	54.4	6.3	60.6	21.9	6.0	28.0	...	88.6
03/2008	12,742	47.1	9.7	56.8	XX	XX	28.9	...	85.8
03/2009	11,103	54.9	7.8	62.7	XX	XX	31.0	...	93.8

Investment Income: The group's increased premium level, higher retentions, the increase in the payout period for claims due to the writing of more longer-tail business, and the impact of reinsurance commutations have combined to produce improved operating cash flows in recent years. These cash flows have driven growth in both the invested asset base and net investment income. The group's invested asset portfolio is predominately concentrated in high-quality fixed-income securities, with an emphasis on municipal bonds, asset-backed and mortgage-backed securities, corporate bonds and to a lesser extent, treasury securities. The predominant portion of the group's investment leverage stems from its common stock holdings of affiliated companies and will remain as such given the group's business model and related business strategies. A minimal amount of equity holdings are maintained, particularly in comparison to the composite. Overall, HCC maintains relatively conservative investment leverage.

The average maturity of the fixed-income portfolio has consistently been maintained at approximately five to six years. Over the past five years, the group's investment portfolio has generated an investment yield that is slightly below that of the industry composite, as is its average return on invested assets over that same time period.

INVESTMENT INCOME ANALYSIS (\$000)

Year	Company		
	Net Inv Income	Realized Capital Gains	Unrealized Capital Gains
2004	34,373	4,254	42,544
2005	40,312	10,453	62,519
2006	85,123	31,236	-71,188

2007	73,895	12,319	146,358
2008	136,045	-7,584	18,953
03/2008	19,132	111	40,318
03/2009	15,782	728	28,899

Year	Company			Industry Composite	
	Inv Inc Growth (%)	Inv Yield (%)	Total Return (%)	Inv Inc Growth (%)	Inv Yield (%)
2004	-17.2	3.1	7.4	5.3	3.7
2005	17.3	2.5	7.2	19.0	3.8
2006	111.2	4.3	2.2	28.4	4.3
2007	-13.2	3.2	10.5	13.8	4.4
2008	84.1	5.4	5.9	3.5	4.4
5-Yr Avg	34.3	3.9	6.6	13.3	4.2
03/2008	XX	XX	2.4	XX	XX
03/2009	XX	XX	1.7	XX	XX

INVESTMENT PORTFOLIO ANALYSIS

Asset Class	2008 Inv Assets (\$000)	% of Invested Assets		Annual % Chg
		2008	2007	
Long-Term bonds	1,724,891	66.1	59.5	14.9
Stocks	0	0.0	1.9	-99.9
Affiliated Investments	696,142	26.7	25.8	7.0
Other Inv Assets	188,791	7.2	12.8	-41.6
Total	2,609,824	100.0	100.0	3.4

2008 BOND PORTFOLIO ANALYSIS

Asset Class	% of Total Bonds	Mkt Val to Stmt Val (%)	Avg. Maturity (Yrs)	Class		Struc. Secur. (%)	Struc. Secur. (% of PHS)
				1 - 2 (%)	3 - 6 (%)		
Governments	6.0	2.6	1.1	100.0	...	...	...
Other	67.7	2.2	6.6	100.0	...	8.3	7.5
Corporates	26.4	-3.2	3.9	100.0	...	27.6	9.7
Total all bonds	100.0	0.8	5.6	100.0	...	12.9	17.1

CAPITALIZATION

The following text is derived from the report of Houston Casualty Group.

The considerable appreciation in the group's policyholders' surplus has predominantly been driven by

operating earnings, capital contributions from the parent company and both realized and unrealized gains. Surplus growth has been constrained somewhat recently by dividends paid to the parent and the capital contributions have decreased in the last few calendar years. Excellent operating results in recent years coupled with capital contributions from the parent holding company have enabled capitalization to adequately support the group's growth in premiums written.

The group has produced strong earnings via increased earned premium from its increasing net retentions of recent years. This is a solid indication that the group has effectively seized opportunities to generate revenue on business where market competition remains reasonable and favorable profit margins still exist.

Over the past several years, the group's significant growth, particularly during the 2001-2004 hard-market period, led to slightly weakened risk-adjusted capitalization by the end of that period. However, the group's capital position has always remained supportive of its rating, as measured by Best's Capital Adequacy Ratio (BCAR). The decline in risk-adjusted capitalization reflected both significant growth in net premium volume along with commensurate growth in net loss reserves and ceded reinsurance recoverables. Despite these increases, premium and loss reserve leverage measures remain on par with or slightly conservative, relative to the industry composite, primarily due to the impact of the parent company capital contributions.

Until recently, the strong cash flow of HCC has historically been enough to cover its operating and dividend requirements. As agencies have been combined with insurance companies, there has been a need to take dividends from HCC's insurance company subsidiaries. A.M. Best does not anticipate the level of dividends paid by the group's insurance companies to the parent to materially weaken the capitalization of these subsidiaries.

CAPITAL GENERATION ANALYSIS (\$000)

<u>Year</u>	Source of Surplus Growth		
	Pretax Operating <u>Income</u>	Total Inv. <u>Gains</u>	Net Contrib. <u>Capital</u>
2004	33,920	46,798	95,791
2005	7,331	72,972	146,900
2006	175,955	-39,952	18,464
2007	172,199	158,676	1,207
2008	239,246	11,370	-84,175
5-Yr Total	628,650	249,864	178,187
03/2008	32,125	40,429	72
03/2009	26,998	29,627	72

<u>Year</u>	Source of Surplus Growth		
	Other, Net of <u>Tax</u>	Change in <u>PHS</u>	PHS Growth <u>(%)</u>
2004	18,419	194,928	47.6
2005	-19,077	208,126	34.4
2006	-14,904	139,563	17.2

2007	-23,958	308,125	32.4
2008	-81,396	85,044	6.7
5-Yr Total	-120,916	935,786	...
03/2008	-15,669	56,957	4.5
03/2009	9,937	66,634	5.0

QUALITY OF SURPLUS (\$000)

Year	Year-End PHS	% of PHS			Dividend Requirements		
		Cap Stk/Contrib. Cap.	Other	Un-assigned Surplus	Stockholder Divs	Div to POI (%)	Div to Net Inc. (%)
2004	604,394	66.5	...	33.5	...	...	...
2005	812,520	67.6	...	32.4	...	...	...
2006	952,083	59.6	...	40.4	...	...	...
2007	1,260,208	45.5	...	54.5	...	...	...
2008	1,345,252	42.7	...	57.3	-85,000	35.5	47.3
03/2008	1,317,165	43.5	...	56.5	...	...	...
03/2009	1,411,886	40.7	...	59.3	...	...	...

LEVERAGE ANALYSIS

Year	Company				Industry Composite			
	NPW to PHS	Reserves to PHS	Net Lev	Gross Lev	NPW to PHS	Reserves to PHS	Net Lev	Gross Lev
2004	0.8	1.0	2.4	4.9	0.7	1.0	2.3	3.8
2005	0.6	1.2	2.3	4.2	0.6	1.0	2.3	3.8
2006	0.5	1.2	2.1	3.4	0.6	1.0	2.2	3.5
2007	0.3	0.9	1.5	2.3	0.5	0.9	2.0	2.9
2008	0.3	0.8	1.4	2.1	0.5	1.0	2.0	3.0
03/2008	0.3	0.9	1.5	XX	XX	XX	XX	XX
03/2009	0.2	0.8	1.3	XX	XX	XX	XX	XX

Current BCAR: 227.1

PREMIUM COMPOSITION & GROWTH ANALYSIS

Period Ending	DPW		GPW	
	(\$000)	(% Chg)	(\$000)	(% Chg)
2004	563,332	16.3	927,909	2.0
2005	474,513	-15.8	833,566	-10.2
2006	409,185	-13.8	738,596	-11.4
2007	383,293	-6.3	664,564	-10.0
2008	402,027	4.9	586,431	-11.8
5-Yr CAGR	...	-3.7	...	-8.4

5-Yr Change	...	-17.0	...	-35.5
03/2008	79,550	0.3	140,258	-8.0
03/2009	80,814	1.6	120,425	-14.1
Period	NPW		NPE	
<u>Ending</u>	<u>(\$000)</u>	<u>(% Chg)</u>	<u>(\$000)</u>	<u>(% Chg)</u>
2004	471,045	11.5	420,427	32.6
2005	499,452	6.0	485,539	15.5
2006	485,571	-2.8	496,968	2.4
2007	424,862	-12.5	453,470	-8.8
2008	371,997	-12.4	398,042	-12.2
5-Yr CAGR	...	-2.5	...	4.7
5-Yr Change	...	-11.9	...	25.6
03/2008	92,289	-8.7	91,356	-19.5
03/2009	67,542	-26.8	86,045	-5.8

Reserve Quality: From a calendar year and an accident year perspective, the group has reported favorable loss reserve development in recent years. The commutation of a large amount of reinsurance recoverables in 2003, 2005 and 2006 related to discontinued accident and health reinsurance business and a strengthening of the reserves related to that business in 2004 negatively impacted primarily accident years 1998-2002. Excluding the impact of the commutations, prior year reserve development would have been relatively flat if not favorable, as has historically been the case. The group's lead company, HC, has borne the brunt of the adverse reserve development, specifically related to its discontinued accident and health reinsurance business. The exit from the workers' compensation line of business several years ago, with the exception of minimum premium workers' compensation business, also led to recorded deficiencies in earlier years. The lines of business reporting more favorable loss reserve development include property, aviation, professional liability and surety lines of business as well as business assumed under a program with an unaffiliated insurance company. Absent the negative impact of additional reinsurance commutations, A.M. Best expects the group's reserve development pattern to continue being reflective of historical norms over the near term.

LOSS & ALAE RESERVE DEVELOPMENT: CALENDAR YEAR (\$000)

Calendar Year	Original Loss Reserves	Developed Reserves Thru 2008	Develop. to Orig.(%)	Develop. to PHS (%)	Develop. to NPE (%)	Unpaid Reserves @12/2008	Unpaid Resrv. to Dev.(%)
2003	364,934	445,074	22.0	19.6	140.4	348,585	78.3
2004	586,434	582,053	-0.7	-0.7	138.4	431,153	74.1
2005	943,965	853,643	-9.6	-11.1	175.8	554,411	64.9
2006	1,151,441	1,046,345	-9.1	-11.0	210.5	689,182	65.9
2007	1,148,496	1,081,216	-5.9	-5.3	238.4	886,389	82.0
2008	1,109,281	1,109,281	...	...	278.7	1,109,281	100.0

LOSS & ALAE RESERVE DEVELOPMENT: ACCIDENT YEAR (\$000)

Original	Developed	Develop.	Unpaid	Acc Yr.	Acc Yr.
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Accident Year	Loss Reserves	Reserves Thru 2008	to Orig.(%)	Reserves @ 12/2008	Loss Ratio	Comb Ratio
2003	158,816	132,446	-16.6	66,427	50.0	76.1
2004	214,291	166,587	-22.3	82,568	50.1	77.6
2005	309,469	247,751	-19.9	123,258	58.4	88.5
2006	252,220	233,003	-7.6	134,771	53.1	79.2
2007	227,559	237,825	4.5	197,207	59.3	87.4
2008	222,892	222,892	...	222,892	64.5	92.8

Reinsurance Utilization: Maintaining sufficient reinsurance to support the catastrophe portion of its portfolio, as well as limiting its exposure in any one class of business, is an integral part of the group's business strategy. Various domestic and foreign reinsurers are utilized in order to limit the group's credit risk to any particular reinsurer. In addition, management has positioned the group to be able to increase the utilization of reinsurance as market conditions warrant, while maintaining a solid balance sheet to support increased retention of premium when reinsurance capacity lessens. A specific reinsurance program is structured for each line of business. Since the beginning of 2002, the group has significantly reduced its ceded business, going from ceding almost two-thirds of its gross book of business, to approximately 20%. This strategic change has been undertaken to increase retentions, capitalize on the rising rates and improved market conditions, and manage reinsurance costs.

Despite the reduction, the utilization of reinsurance to mitigate the group's exposure to any one event leaves it exposed to the impact of changes in the reinsurance sector, including but not limited to pricing behavior, credit risk and dispute risk. As such, management remains highly attuned to activity in the reinsurance market sector seeking to ensure that the group remains aligned with financially strong reinsurance partners. The focus on maintaining solid partnerships has led to the commutation of recoverables when circumstances determined it to be the best strategic option.

The group's total reinsurance recoverables, specifically those related to unpaid and incurred but not reported (IBNR) losses, have increased historically because of the growth in gross writings and the effect of catastrophe losses, principally hurricanes. A.M. Best anticipates that the level of reinsurance recoverables will likely decline modestly as reinsurance recoverables related to catastrophes are collected.

CEDED REINSURANCE ANALYSIS (\$000)

Year	Company				Industry Composite		
	Ceded Reins Total	Business Retention (%)	Rein Rec to PHS (%)	Ceded Reins to PHS (%)	Business Retention (%)	Rein Rec to PHS (%)	Ceded Reins to PHS (%)
2004	1,515,672	50.8	175.2	250.8	43.5	103.4	144.1
2005	1,546,438	61.0	149.2	190.3	42.7	111.9	147.0
2006	1,198,756	66.2	99.3	125.9	45.6	90.4	123.1
2007	1,033,688	64.5	63.0	82.0	45.2	70.4	95.6
2008	1,019,242	64.0	59.8	75.8	45.8	74.8	99.6

2008 REINSURANCE RECOVERABLES (\$000)

Paid & Unpaid	Unearned	Other	Total Reins
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	<u>Losses</u>	<u>IBNR</u>	<u>Premiums</u>	<u>Recov*</u>	<u>Recov</u>
US Affiliates	388	388
Foreign Affiliates	1,879	44	21,391	-2,832	20,482
US Insurers	151,933	115,586	44,350	151	312,020
Pools/Associations	45	...	...	3	48
Other Non-US	264,949	149,437	57,469	403	472,258
Total (ex US Affils)	418,806	265,067	123,210	-2,275	804,808
Grand Total	419,194	265,067	123,210	-2,275	805,196

* Includes Commissions less Funds Withheld

INVESTMENT LEVERAGE ANALYSIS (% OF PHS)

Year	Company						Industry Composite	
	Class 3-6 <u>Bonds</u>	Real Estate/ Mtg.	Other Invested Assets	Common Stocks	Non-Affl Inv. Lev.	Affil Inv.	Class 3-6 <u>Bonds</u>	Common Stocks
2004	...	...	3.1	-4.6	-1.5	49.0	1.5	18.7
2005	...	...	9.6	4.5	14.1	47.4	1.6	17.7
2006	0.3	...	12.3	6.1	18.8	53.0	1.0	18.6
2007	0.2	...	10.6	3.9	14.7	51.6	0.9	17.3
2008	...	...	2.6	0.0	2.6	51.7	2.8	10.5

LIQUIDITY

The following text is derived from the report of Houston Casualty Group.

Overall Liquidity: The group maintains a sound liquidity position as evidenced by current and overall liquidity ratios that are on par with industry composite averages. Increased emphasis on shorter-term bonds in the last few years has helped maintain the sound liquidity, as has the positive impact of reinsurance commutations on cash holdings. The level of invested assets has increased by almost four times since year-end 2001, thereby offsetting similar growth in total liabilities stemming from higher loss reserves and a larger unearned premium balance. Operating cash flow, driven by increased premiums collected, has risen significantly in recent years. Historically, the group's adequate liquidity position has been derived from consistent operating cash flow and contributed capital from the parent holding company with solid investment income also contributing.

In October 2007, parent HCC Insurance Holdings, Inc., increased its existing \$300 million bank credit facility to \$575 million. The facility expires in December 2011. There was \$220 million outstanding on this facility as of December 31, 2008. In September of 2007, HCC announced its intent to redeem all of its outstanding 2.00% convertible exchange notes in October, increasing the \$40.0 million balance outstanding on the bank facility to \$210.0 million to fund the principal payments on the notes. Previously, in late May of 2006, the parent company filed for a new \$1 billion universal shelf registration, to replace the \$750 million shelf previously in place. This shelf allows HCC to issue debt, stock, or any other subordinated debt type of security and helps provide the group with great financial flexibility.

LIQUIDITY ANALYSIS

Year	Company				Industry Composite			
	Quick Liq (%)	Current Liq (%)	Overall Liq (%)	Gross Agents Bal to PHS(%)	Quick Liq (%)	Current Liq (%)	Overall Liq (%)	Gross Agents Bal to PHS(%)
2004	34.9	104.3	166.1	26.9	36.5	131.3	159.1	12.9
2005	36.7	114.9	164.9	18.9	32.6	133.3	158.2	13.5
2006	23.1	107.4	165.2	12.6	36.8	142.5	161.0	12.3
2007	25.2	124.9	185.1	7.8	33.7	148.8	168.1	10.5
2008	18.5	131.2	194.6	9.4	30.3	144.2	165.4	9.6
03/2008	XX	126.9	188.3	8.2	XX	XX	XX	XX
03/2009	XX	131.7	197.3	8.9	XX	XX	XX	XX

CASH FLOW ANALYSIS (\$000)

Year	Company			Industry Composite			
	Underw Cash Flow	Oper Cash Flow	Net Cash Flow	Underw Cash Flow (%)	Oper Cash Flow (%)	Underw Cash Flow (%)	Oper Cash Flow (%)
2004	248,162	275,093	153,745	217.8	224.5	207.5	203.1
2005	355,168	373,978	46,536	341.9	317.3	149.5	157.0
2006	271,444	273,644	-161,832	230.5	206.9	158.1	159.7
2007	86,579	138,229	-7,372	124.2	134.0	146.6	144.2
2008	75,298	170,052	-92,310	124.4	147.7	121.9	133.6
03/2008	44,680	43,509	-35,565	180.7	156.4	XX	XX
03/2009	-9,053	4,036	34,158	88.9	104.6	XX	XX

HISTORY

The company was incorporated under the laws of Texas on December 9, 1980, as International Indemnity Company of Texas and began business on June 18, 1981. The name was changed to Houston Casualty Company on May 26, 1983.

Capital paid-up at year-end was \$5,000,000 consisting of 5,000,000 shares of common stock at a par value of \$1 per share. Authorized capital stock at year end was 10,000,000 shares.

MANAGEMENT

The company is ultimately wholly owned by HCC Insurance Holdings, Inc., a publicly held insurance and insurance-related services holding company traded on the NYSE under the symbol HCC. Administration of the company's affairs is under the direction of Michael J. Schell, Chief Executive Officer and Executive Vice President of HCC Insurance Holdings, Inc.

Officers: President and Chief Executive Officer, Michael J. Schell; President, Barry Cook (London Branch); Chief Operating Officer, Nick Hutton-Penman (London Branch); Chief Financial Officer, Brendan Merriman (London Branch); Chief Underwriting Officer, Michael Onslow (London Branch); Executive Vice Presidents, Michael J. Donovan, Edward H. Ellis, Jr., John N. Molbeck, Jr.; Senior Vice President and Actuary, Annette J. Goodreau; Senior Vice Presidents, Mark A. Buechler,

Brian E. Duffy, Duane R. Dyckman, Christopher M. Lewis, Carl R. Nederman, Mark P. Reynolds, Mark P. Rickert, Randy D. Rinicella; Vice President and Chief Financial Officer, Stephen P. MacDonough; Vice President and Secretary, James L. Simmons; Vice President and Treasurer, Hamendra P. Ojha; Vice Presidents, Christopher D. Bonnett, Sharon L. Brock, Jackie S. Kellems, Joycelyn M. Ray, Deborah L. Riffe, Christopher S. Throckmorton (Chief Pricing Actuary); Treasurer, Rowland Hughes (London Branch); Controller, Chris Tlucek.

Directors: Edward H. Ellis, Jr., Stephen P. MacDonough, John N. Molbeck, Jr., Hamendra P. Ojha, Pamela J. Penny, Randy D. Rinicella, Michael J. Schell.

REGULATORY

An examination of the financial condition was made as of December 31, 2003 by the Insurance Departments of Delaware and Texas. The 2008 annual independent audit of the company was conducted by PricewaterhouseCoopers, LLP. The annual statement of actuarial opinion is provided by John F. Gibson, FCAS, MAAA, PricewaterhouseCoopers, LLP.

TERRITORY

The company is licensed in Texas. Credit is allowed for reinsurance as a licensed reinsurer in New Hampshire. It also operates on a surplus lines or non-admitted basis in the District of Columbia, Guam, Northern Mariana Islands, Puerto Rico, U.S. Virgin Islands, AL, AK, AZ, AR, CA, CO, CT, DE, FL, GA, HI, ID, IL, IN, IA, KS, KY, LA, ME, MD, MA, MI, MN, MS, MO, MT, NE, NV, NJ, NM, NY, NC, ND, OH, OK, OR, PA, RI, SC, SD, TN, UT, VT, VA, WA, WV, WI and WY.

REINSURANCE

The following text is derived from the report of Houston Casualty Group.

Reinsurance is maintained on a quota share and excess of loss basis with a separate program maintained for each line of business. Catastrophe coverage is purchased for property, marine, and energy business that is exposed to natural disasters and aviation for ground accumulation. Facultative reinsurance is also purchased when deemed appropriate.

BALANCE SHEET (\$000)

<u>ADMITTED ASSETS</u>	<u>12/31/2008</u>	<u>12/31/2007</u>	<u>2008 %</u>	<u>2007 %</u>
Bonds	1,724,891	1,501,491	60.6	54.0
Common stock	0	49,091	0.0	1.8
Cash & short-term invest	79,747	172,057	2.8	6.2
Other non-affil inv asset	88,896	133,644	3.1	4.8
Investments in affiliates	687,076	641,154	24.1	23.0
Real estate, offices	9,066	9,601	0.3	0.3
Total invested assets	2,589,676	2,507,038	91.0	90.1
Premium balances	169,750	157,288	6.0	5.7
Accrued interest	20,148	17,580	0.7	0.6

All other assets	66,116	100,091	2.3	3.6
Total assets	2,845,690	2,781,997	100.0	100.0
<u>LIABILITIES & SURPLUS</u>	<u>12/31/2008</u>	<u>12/31/2007</u>	<u>2008 %</u>	<u>2007 %</u>
Loss & LAE reserves	1,118,349	1,155,555	39.3	41.5
Unearned premiums	199,146	225,190	7.0	8.1
Conditional reserve funds	38,414	19,000	1.3	0.7
All other liabilities	144,530	122,044	5.1	4.4
Total liabilities	1,500,438	1,521,789	52.7	54.7
Capital & assigned surplus	574,004	573,179	20.2	20.6
Unassigned surplus	771,248	687,028	27.1	24.7
Total policyholders' surplus	1,345,252	1,260,208	47.3	45.3
Total liabilities & surplus	2,845,690	2,781,997	100.0	100.0

SUMMARY OF 2008 OPERATIONS (\$000)

<u>STATEMENT OF INCOME</u>	<u>12/31/2008</u>	<u>FUNDS PROVIDED FROM OPERATIONS</u>	<u>12/31/2008</u>
Premiums earned	398,042	Premiums collected	384,126
Losses incurred	146,064	Benefit & loss related pmts	169,629
LAE incurred	45,162	LAE & undrw expenses paid	139,199
Undrw expenses incurred	104,951	Undrw cash flow	75,298
Net underwriting income	101,864	Investment income	140,995
Net investment income	136,045	Other income/expense	1,343
Other income/expense	1,337	Pre-tax cash operations	217,636
Pre-tax oper income	239,246	Income taxes pd (recov)	47,584
Realized capital gains	-7,584	Net oper cash flow	170,052
Income taxes incurred	51,812		
Net income	179,850		

INTERIM BALANCE SHEET (\$000)

<u>ADMITTED ASSETS</u>	<u>03/31/2009</u>
Cash & short term invest	113,905
Bonds	1,774,016
Common stock	718,311
Other investments	48,725
Total investments	2,654,957
Premium balances	173,991
Reinsurance funds	44,123

Accrued interest	19,280
All other assets	25,147
Total assets	2,917,498

LIABILITIES & SURPLUS 03/31/2009

Loss & LAE reserves	1,124,217
Unearned premiums	180,643
Conditional reserve funds	26,792
All other liabilities	173,960
Total liabilities	1,505,613

Capital & assigned surp	574,028
Unassigned surplus	837,858
Policyholders' surplus	1,411,886

Total liabilities & surplus	2,917,498
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INTERIM INCOME STATEMENT (\$000)

	Period Ended <u>3/31/2009</u>	Period Ended <u>3/31/2008</u>	Increase/ <u>Decrease</u>
Premiums earned	86,045	91,356	-5,311
Losses incurred	47,253	43,031	4,222
LAE incurred	6,729	8,874	-2,145
Underwriters expenses incurred	20,961	26,709	-5,748
Net underwriting income	11,103	12,742	-1,639
Net investment income	15,782	19,132	-3,350
Other income/expenses	113	251	-138
Pre-tax operating income	26,998	32,125	-5,127
Realized capital gains	728	111	617
Income taxes incurred	5,728	16,344	-10,616
Net income	21,998	15,892	6,105

INTERIM CASH FLOW (\$000)

	Period Ended <u>3/31/2009</u>	Period Ended <u>3/31/2008</u>	Increase/ <u>Decrease</u>
Premiums collected	72,415	100,072	-27,656
Benefit & loss related pmts	48,529	18,872	29,657
Undrw expenses paid	32,939	36,520	-3,581
Underwriting cash flow			

	-9,053	44,680	-53,733
Investment income	18,812	20,365	-1,553
Other income/expense	113	251	-138
Pre-tax cash operations	9,872	65,296	-55,423
Income taxes pd (recov)	5,836	21,787	-15,951
Net oper cash flow	4,036	43,509	-39,472

The Financial Strength Rating opinion addresses the relative ability of an insurer to meet its ongoing insurance obligations. The ratings are not assigned to specific insurance policies or contracts and do not address any other risk, including, but not limited to, an insurer's claims-payment policies or procedures; the ability of the insurer to dispute or deny claims payment on grounds of misrepresentation or fraud; or any specific liability contractually borne by the policy or contract holder. A Financial Strength Rating is not a recommendation to purchase, hold, or terminate any insurance policy, contract, or any other financial obligation issued by an insurer, nor does it address the suitability of any particular policy or contract for a specific purpose or purchaser. In arriving at a rating decision, A.M. Best relies on third-party audited financial data and/or other information provided to it. While this information is believed to be reliable, A.M. Best does not independently verify the accuracy or reliability of the information. For additional details, see A.M. Best's Terms of Use at www.ambest.com/terms.html

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