

2007

**Hiscox Ltd
Report and
Accounts**

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— **“Our ambition remains to be a highly respected international specialist insurance and reinsurance company, built on a balance between volatile international catastrophe business and more steady local and regional business.”**

Robert Hiscox
Chairman

Corporate highlights

Financial

Record pre-tax profits up 18% to £237.2m (2006: £201.1m)
Gross premiums written up 6.5% to £1,198.9m (2006: £1,126.2m)
Group combined ratio improves to 84.4% (2006: 89.1%)
Earnings per share on profit after tax up 16.1% to 48.4p (2006: 41.7p)
Final dividend 8p per share (2006: 7p) making 12p for the full year, an increase of 20% (2006: 10p)
Return on equity 28.8% (2006: 28.9%)
Active capital management

Operational

Excellent year for Hiscox Global Markets – profits increased to £155.6m (2006: £90.7m)
Hiscox UK and Hiscox Europe – good top line growth of 13.7% to £302.3m (2006: £265.8m) with profits of £21.8m (2006: £33.1m) despite the impact of Windstorm Kyrill and the UK floods
Hiscox International – another successful year with profits up 33.2% to £69.1m (2006: £51.9m)
Hiscox USA – acquired American Live Stock, a major milestone towards building a strong US domestic business
Regional business relatively stable in the softening market with good growth prospects

20%
increase
in dividend

12p
dividend
for 2007

Group key performance indicators

	2007	2006
Gross premiums written (£m)	1,198.9	1,126.2
Net earned premiums (£m)	965.2	888.8
Profit before tax (£m)	237.2	201.1
Earnings per share (p)	48.4	41.7
Total dividend per share for year (p)	12.0	10.0
Net asset value per share (p)	209.5	173.2
Shareholders' equity (£m)	824.3	682.1
Group combined ratio (%)	84.4	89.1
Return on equity (%)	28.8	28.9



Robert Hiscox

After a record result in 2006, I am delighted to announce a further record in 2007. We took full advantage of the strong rates for international reinsurance in London and Bermuda, added some gearing from our sidecar 'Panther', and with disciplined underwriting, skilful avoidance of various market losses and some help from Mother Nature, were handsomely rewarded. Our regional businesses in the UK, Europe and the USA continued to grow, with the UK making a good profit despite the storms and floods. Our strategy of growing stable regional businesses will now become more valuable as some international rates fall following two years with relatively light catastrophes.

Results

The result for the year ended 31 December 2007 was a record profit of £237.2 million (2006: £201.1 million). Gross written premium income increased 6.5% to £1,198.9 million (2006: £1,126.2 million) with net earned premium increasing 8.6% to £965.2 million (2006: £888.8 million). This was despite a weak dollar exchange rate persisting throughout 2007. The combined ratio was 84.4% (2006: 89.1%). Earnings per share on profit after tax increased 16.1% to 48.4p (2006: 41.7p) and net assets per share rose 21% to 209.5p per share (2006: 173.2p). Return on equity was 28.8% (2006: 28.9%).

£237.2m

record profit before tax

Dividend and capital management

In March 2007, the Board proposed a total dividend of 12p for 2007. Subject to shareholders' approval, we will pay a final dividend of 8p (2006: 7p) making a total distribution for the year of 12p (2006: 10p) an increase of 20%. This will be paid on 17 June 2008 to shareholders on the register on 16 May 2008. Our dividend policy going forward is to increase the dividend year-on-year as we believe a growing income is well received by shareholders and a main plank of equity investment.

This year's record result has generated additional capital at a time when we have reduced the 2008 capacity of our Lloyd's Syndicate 33 by 20%. On top of the annual dividend of around £50 million, we have announced a buy-back of our shares to treasury of up to £50 million and repayment of debt of £50 million, making an effective capital repayment of £150 million.

Our business needs capital to support underwriting and to build the network of regional businesses. We have made regular small

Dividend and capital management continued

acquisitions but prices have been driven very high. If the sub-prime crisis and the competitive insurance conditions reduce the profitability and the expectations of some attractive businesses we will need capital to be able to buy if the right opportunity arises.

Review of the year

Our ambition remains to be a highly respected international specialist insurance and reinsurance company, built on a portfolio balanced between volatile international catastrophe business and more steady local and regional business. During the last year we made significant progress in strengthening the Group.

As usual I will highlight some salient points of the year under review and leave Bronek Masojada to report in more detail.

2007 was another cracking year for the international catastrophe exposed business. It always sounds easy in retrospect to write a book of catastrophe business when the catastrophes have not occurred, but it isn't. It requires extremely careful analysis of exposures and sensible purchase of reinsurance, combined with the ability to secure shares of the most attractive business.

This the Global Markets team in London and the Bermuda team did extremely well.

handling combined with slick operations to build a profitable book such as ours. Our direct business which offers household and small commercial policies, is nearing critical mass and profitability. The income rose by 72% and the number of policies to 54,000, aided by the advertising campaigns which also helped sell policies through brokers and strengthen the brand.

Hiscox Europe increased premium income by 25% and had a third year of profit despite losses from Windstorm Kyrill which bodes well for the future as we increase our product range.

Hiscox USA established a firm foothold and the acquisition of the American Live Stock Insurance Company, now renamed Hiscox Insurance Company Inc., will give us the ability to market our policies on an admitted basis in addition to the surplus lines basis using Hiscox Syndicate 33 at Lloyd's.

Hiscox Guernsey had another brilliant year.

The market

The insurance cycle is alive and definitely kicking and it would appear that some insurers are, as usual, suffering from rapid and severe memory loss. (How can they forget 2005 when years of premiums were wiped out?) Rates are reducing rapidly in obvious

Our strategy of growing stable regional businesses will now become more valuable.

2007 was a year of good progress on the regional side of the business. Hiscox UK made a profit despite being assaulted by Windstorm Kyrill in January and floods in June and July.

The household book lost money but enhanced its reputation by excelling in the management of claims. Household insurance is thought by the majority of buyers to be a commodity purchase – all policies are the same so it is only price that matters. It is extraordinary that people who would normally never buy the cheapest will cover the risk of losing their most precious assets with a cheap and often unread policy. Well you find out how good your policy is when you have a claim, and we set out to prove that a Hiscox policy is altogether better – and I believe that we succeeded.

The commercial side of Hiscox UK showed the benefit of balance and its superb underwriting profits kept UK profitable. It has built up an excellent book in the small professional businesses area with intelligent cover and efficient processes. There is less competition for small risks which require a distinct skill in underwriting and claims

areas where there are large premiums to be competed for and the lust for non-catastrophe exposed business is turning underwriting discipline to jelly. I sometimes wonder whether underwriters who have made a 10% profit and then reduce rates by 10% think they are going to make 9%, instead of the obvious NIL. Any management, including the management of Lloyd's, who sees a rising income in an area of falling rates ought to ask serious questions. It was disappointing to see the capacity of Lloyd's reducing only 2% for 2008 (an actual increase at constant exchange rates) when most of the seasoned underwriters like us were reducing by 20%.

Sub-prime crisis

After a period of grace during which the banks had re-established a reputation for financial discipline, control of risk and expertise in passing that risk off to others (and insurers were widely assumed to have taken the risk off them), there is a measure of *schadenfreude* in their current turmoil. Critics have wondered why the insurance industry has been unable to quantify its losses almost immediately after major catastrophes, telling us that the banks can

mark to market every night and know their exact exposure at any time. Not so, it would appear. It is a serious crisis, the full extent of which I do not think we have yet seen. In our underwriting books we have a very limited exposure which we have reserved fully. I comment on our investment portfolios below.

Investments

The end of 2007 (and the beginning of 2008) has been a challenging period for investing. However, our policy of focusing on high quality, short duration bonds has kept us away from the structured products that have done so much damage in the financial world. We have a negligible exposure to certain sub-prime securities, all of which remain AAA rated.

At the end of last year we reduced our equity exposure from 10% of overall funds to 7.8% and that has helped during the weak market in early 2008. We expect opportunities to emerge from the current turbulence and a more normal relationship between risk and reward to return.

People

We have continued to seek, recruit, train and motivate the best people. There is a spirit which pervades throughout all our offices which is made up of a desire to do an excellent job with drive,

Our regional businesses are showing healthy growth. We believe that we have demonstrated that our household policies give superior cover backed by great service. Our specialist commercial policies have a strong following in their markets and have much further to go. We have built many advantages into our business over the last few years which will benefit us greatly in the years to come. Our residence in Bermuda gives us considerable strategic advantages and a more global perspective. Our international spread of offices lead to business opportunities not available to us before, and give our staff increased choices in their careers. We have a great group of people with a wide range of skills in international and regional business with a network of offices and contacts throughout the world. The market may be testing in the next few years but we have been building towards this moment and I am confident that we will prosper.

Robert Hiscox
Chairman
3 March 2008



**Direct to customer
income up by
72%**

efficiency and integrity. I think that because of this customers want to do business with Hiscox. I am very grateful to everyone at Hiscox for what they have built over the last few years culminating in the excellent results over the last two.

The future

We are building a long-term business and our senior management have experience of several down-cycles. We have spent 15 years investing considerable money in building an international network to distribute our specialist products. This will mitigate the effect of this part of the cycle.

Our Global Markets and Bermuda businesses are most affected by the cycle and they will let those with short memories take the business off them if the price is not right. There is still plenty of good business at fair prices so they have budgeted to make a good profit in 2008. Reinsurance prices are relatively firm, so those who are reducing insurance premiums to unrealistic levels will be squeezed by expensive reinsurance and less income to pay losses.



Beornat Mosogóla

Our Chairman Robert Hiscox has always advised us to 'advance to the sound of gunfire, retreat when the Sirens call'. In 2007 we followed this advice. Significant parts of our business advanced, particularly in reinsurance in London and Bermuda, but also in our smaller ticket businesses in the UK, USA and Europe.

The result of this has been a record level of controlled gross written premium, record profits on both an absolute and per share basis and a 20% increase in dividend per share. We are also hearing the Sirens of a market in downturn and in 2008 we will retreat tactically. Across the Group market conditions are becoming tougher but with variability in pricing trends by line of business. Our business strategy has long been set to take account of this environment. We are shrinking significantly in the areas such as international big ticket business where we see most pressure on pricing, shrinking moderately in areas like reinsurance which are less affected, and expanding in the US, UK and European domestic markets where our specialist focus protects us from the extremes of market competition.

Group performance

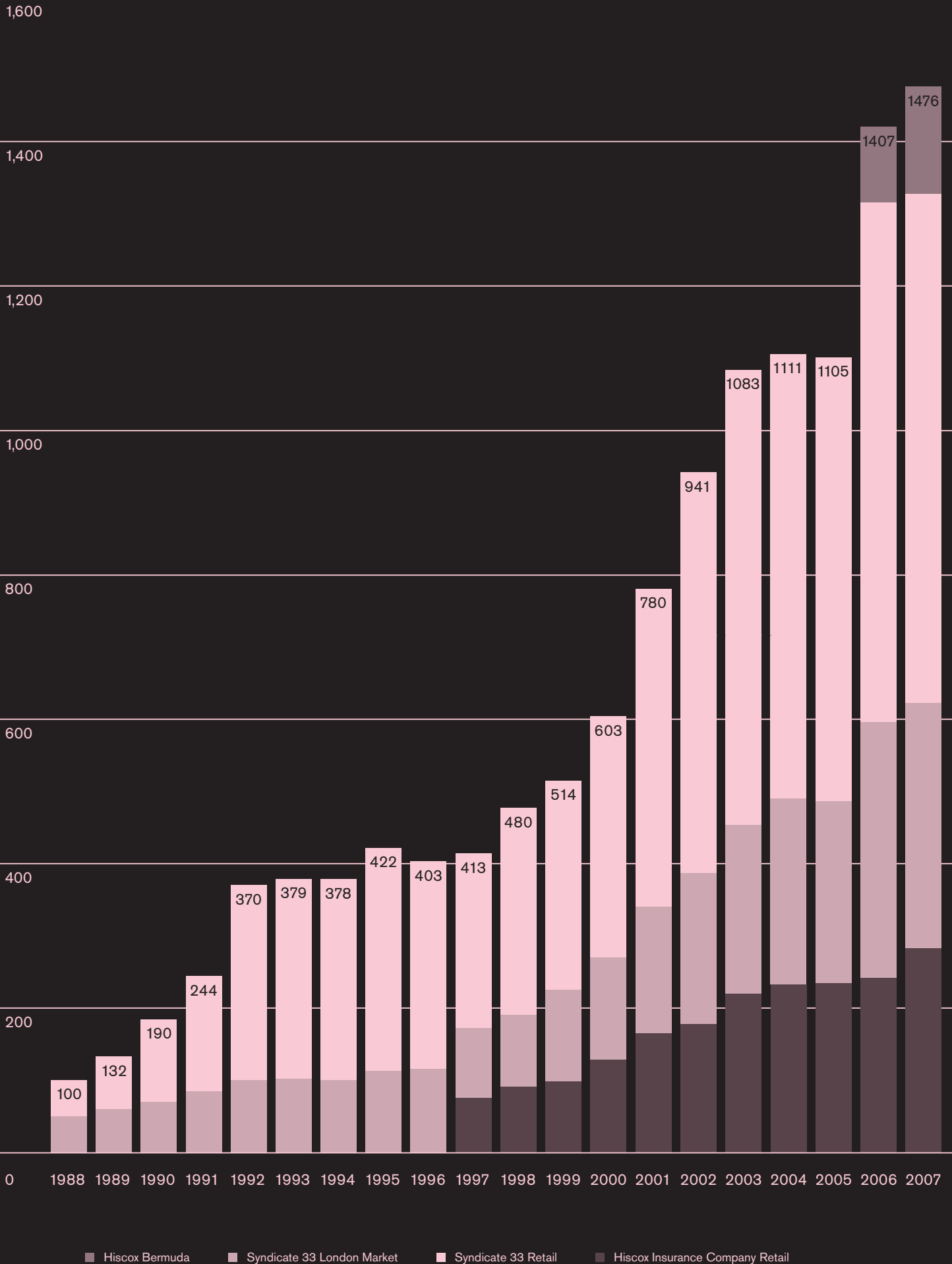
The pre-tax profit for the year was £237.2 million (2006: £201.1 million). Gross written premium grew to £1,198.9 million, an increase of 6.5% (2006: £1,126.2 million), which equals £3.04 per share (2006: £2.86). Earnings per share are 48.4p (2006: 41.7p). Return on equity was 28.8% (2006: 28.9%). Dividends per share have increased 20% to 12p per share (2006: 10p). This excellent performance was achieved despite losses of £68 million from the catastrophes which affected our business.

Hiscox is most well known for its expertise in the high net worth arena, but it is our balance of business that gave us the flexibility to deliver this record result while still investing in the future. The decision to expand in reinsurance in both London and Bermuda, combined with a strong performance in big ticket international business, generated record returns and we invested in both our UK direct business and the USA.

84.4%
Group combined
ratio

£1,198.9m

Gross premiums written up by 6.5%



■ Hiscox Bermuda ■ Syndicate 33 London Market ■ Syndicate 33 Retail ■ Hiscox Insurance Company Retail

Hiscox Global Markets

Hiscox Global Markets underwrites a mix of bigger ticket international business where the Lloyd's licences provide market access, and smaller ticket specialty business which comes to London for both historic and relationship reasons. Richard Watson led it to a stunning year. Gross written premiums were £676.5 million (2006: £709.1 million) and profits surged to £155.6 million (2006: £90.7 million). The combined ratio improved to 81.7% (2006: 90.1%). The growth in profits was due to an excellent performance by the reinsurance, property and specialty teams. Our marine and global errors and omissions (E&O) teams all made solid contributions.

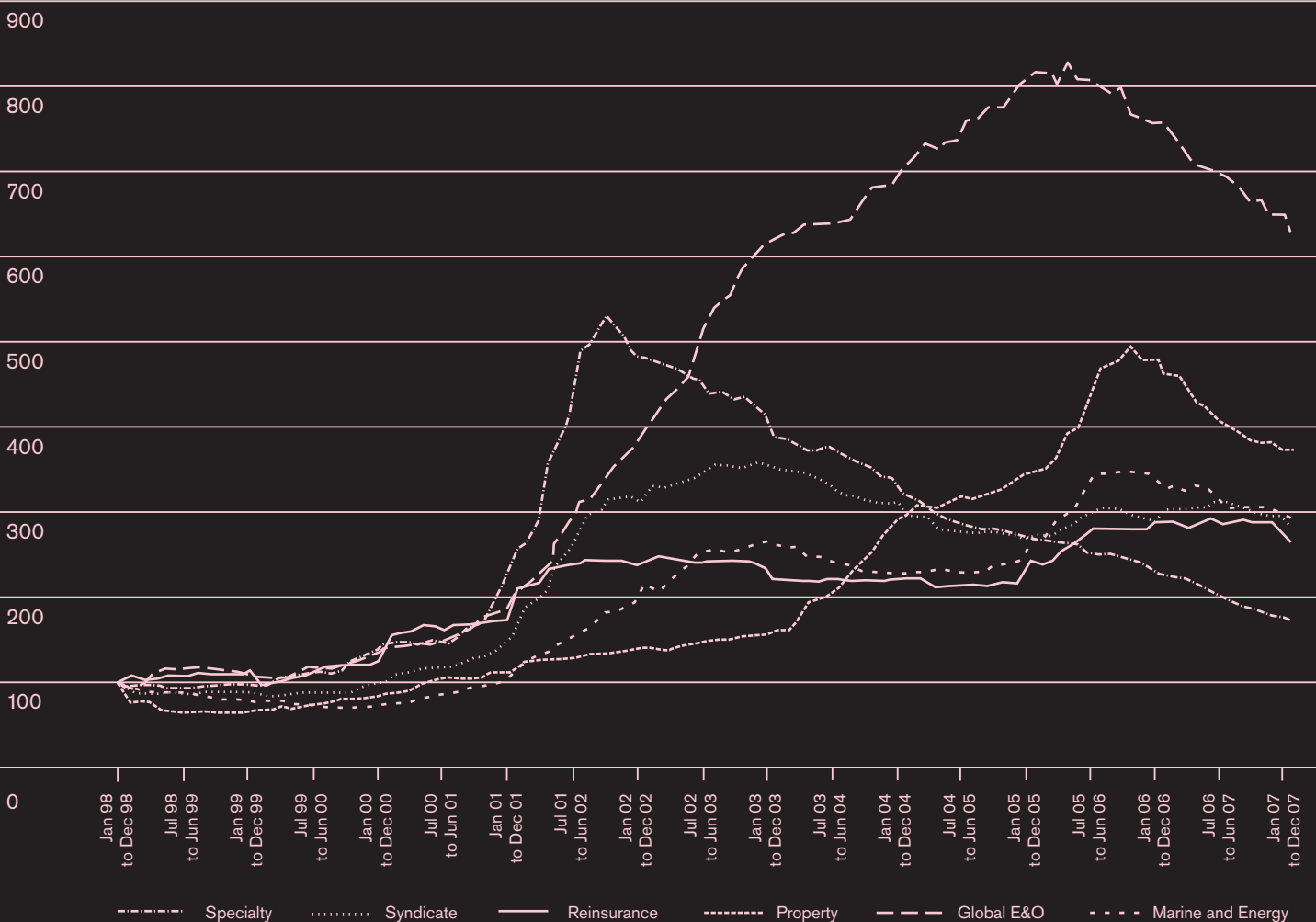
The reinsurance area expanded significantly in the year, with the added capacity of a special purpose re-insurer Panther Re, which was capitalised by WL Ross & Co. Growth in a year that turned out to have very few insured natural catastrophes has been a major contributor to the Group's growth in profits. In October last year Panther Re and Syndicate 33 agreed that their successful reinsurance partnership covering the 2007 year of account would not be renewed for 2008. We commuted our contract with Panther Re in January 2008 in a deal which brought benefits to both parties. In place of Panther Re we created the smaller Cougar Syndicate at Lloyd's which is capitalised by a mix of individual and Corporate Names. Initially set up for one year, Cougar Syndicate has a capacity of £34.6 million. Although we expect our reinsurance writings to reduce as rates are easing, we will write enough well-rated business to satisfy both Cougar and ourselves.

The property team underwrite all of our catastrophe exposed primary property and property binder business. They had a good year as modest expansion and few losses led to a significant profit contribution. We have moved the reinsurance protections of this business towards a quota share structure, creating partnerships to share both risk and reward.

Under the specialty banner we bring together a range of areas such as bloodstock, contingency, kidnap and ransom, terrorism, personal accident and political risks. The division had an almost static top line but improved combined ratios led to a good performance.

£155.6m
Hiscox Global Markets
pre-tax profit

Hiscox Global Markets rating index Index level (%)



£69.1m

**Hiscox
International
pre-tax profit**

It is the specialty division which provides a fair degree of balance of non-correlated business to Hiscox Global Markets and the Group, so it is an area we will cherish as market conditions deteriorate.

The marine area saw a reduction in overall premium written as we responded to declining rates, particularly in upstream energy. Combined ratios remained good, but the smaller level of income led to slightly lower profitability overall.

Our global errors and omissions division was created from the merger of our technology, media and telecommunications teams and our global professional indemnity teams. Bigger ticket professional indemnity is an area where many catastrophe-focused players are expanding – seeking illusory 'non-correlating' business – forgetting that it is only worth doing if it remains profitable. The division has shown great discipline, shrinking in those areas where rates are under most pressure, allowing it to deliver a good result. We remain committed to the area, particularly its more specialist niches, and will expand when the rates return to better levels.

Hiscox Global Markets has invested in building underwriting teams outside London. We have established hubs in Paris and in New York to give brokers greater choice in the way they access Hiscox. As well as business which comes to London, we can also serve those brokers who, for whatever reason, decide to place their business in their local market.

At Hiscox we have regarded front line underwriters as our 'fighter pilots'; but just like real pilots, their tools are becoming ever more sophisticated and a greater range of skills need to be brought to bear before a risk is underwritten. Over the last several years we have invested significantly in our modelling capability with a focus on both aggregate management and risk pricing. This year we recruited a further three pricing actuaries to expand our strong analytical team. We believe that the enhanced transparency and greater understanding that the analytics give us, when combined with real management action, will make us more effective in dealing with the softer market that lies ahead.

As announced in late 2007, we expect Hiscox Global Markets to shrink by at least 20% in 2008 as we remain committed to our goal of seeking profit over volume.

Hiscox International

Hiscox International comprises our business in Bermuda, the USA and Guernsey. It had another successful year. Gross written premium grew to £220.2 million (2006: £151.3 million) and the combined ratio 75.4% (2006: 62.7%). Profits grew to £69.1 million (2006: £51.9 million). This improvement was driven by a good performance in each business.

Hiscox Bermuda had a great year. Robert Childs led his team to expand their external reinsurance book by 60% to £148.7 million (2006: £93.0 million). This expansion, coupled with a year of low loss frequency, generated a combined ratio of 56.7% and allowed the profits to flow. In 2008 we expect the business to shrink as the team shows the same discipline in softer markets as it did in expanding at the right time.

Hiscox Guernsey had another good year under the leadership of Steve Camm and Rob Davies. Gross written premium remained virtually flat at £49.1 million (2006: £48.6 million). Profits remained strong. Our Guernsey team continues to drive the expansion of our worldwide kidnap and ransom business. During the year we acquired a portfolio of this business from AON, which is made up of Latin American risks from third party intermediaries. We also recruited another team based in New York. These two teams will build our relationships with local retail brokers – injecting a stronger growth element into this business.

Hiscox USA had a step change in size this year. Led by Ed Donnelly, premiums grew 130% to £22.4 million (2006: £9.7 million). Our team expanded to 88 people. During the year we acquired the American Live Stock Insurance Company. It contributed £3 million to this year's business.

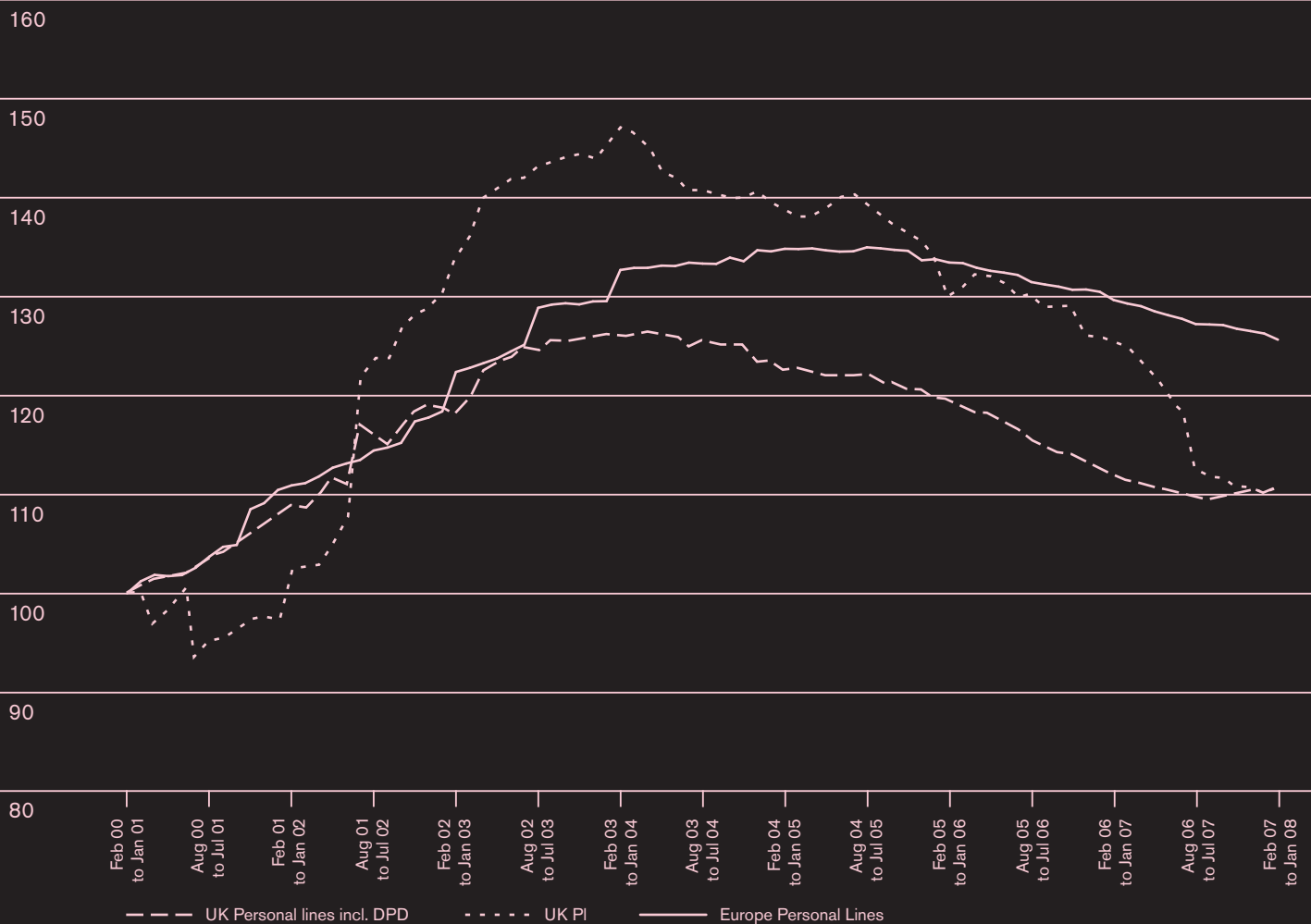
Hiscox Global Markets

	2007 £m	2006 £m
Gross premiums written	676.4	709.1
Net premiums earned	552.2	567.5
Profit before tax	155.6	90.7
Combined ratio	81.7%	90.1%

Hiscox International

	2007 £m	2006 £m
Gross premiums written	220.2	151.3
Net premiums earned	164.6	93.5
Profit before tax	69.1	51.9
Combined ratio	75.4%	62.7%

Hiscox UK and Hiscox Europe rating index Index level (%)



We have renamed it Hiscox Insurance Company Inc. and will use it as our admitted market platform for the USA. This represents a major milestone in our desire to build a strong US domestic platform. We will retain its profitable animal mortality business and will continue to use the American Live Stock brand in this specialist area. We now have four offices supporting our USA domestic operations in Armonk, Chicago, Manhattan and Geneva, Illinois. In time, we aim to acquire additional businesses or teams who can support the growth of our US domestic business.

Hiscox UK and Hiscox Europe

Despite challenging conditions our businesses in both the UK and Europe delivered good top line growth with gross premiums written increasing by 13.7% to £302.3 million (2006: £265.8 million). Aggregate profits fell to £21.8 million (2006: £33.1 million), and the combined ratio was 98.2% (2006: 96.2%) reflecting the impact of Windstorm Kyrill and the UK floods.

Hiscox UK, led by Steve Langan, produced profits despite several catastrophe events. It has grown gross written premiums 10.7% to £229.2 million (2006: £207.1 million) though profits have fallen to £17.2 million (2006: £32.4 million). The decline has been due to the impact of Windstorm Kyrill, the UK floods in June and July and further investment in our UK marketing campaign. UK property rates had been low for some time and, in part due to the impact of the floods, we are now seeing rates firm. Our marketing campaign continues to show returns. Brand awareness almost trebled in 18 months and

customer numbers for the direct business grew to 54,000. The professions and specialty commercial area focuses on knowledge-based businesses employing 250 or fewer staff. Over several years we have developed specific products for firms active in this sector and are building our market presence. This year we began marketing these liability and property products to firms employing ten or fewer staff via the internet. These smaller firms increasingly use the internet to purchase insurance and Hiscox is able to serve their specialist needs. One of the consequences of the UK floods and Windstorm Kyrill has been the need to restructure Hiscox UK's reinsurance programme as it is no longer economic to continue unchanged. In 2008 we have decided to increase the deductible on our catastrophe programme to £10 million from its previous level of £1 million.

Hiscox Europe, led by Marc van der Veer, produced a fourth year of profits and growth. Gross written premiums grew 24.5% to reach £73.1 million (2006: £58.7 million) and profits increased to £4.6 million (2006: £0.7 million). The profit improvement includes the benefit of a stronger Euro exchange rate, but even excluding this we are ahead year-on-year. This was achieved despite some serious losses as a result of Windstorm Kyrill. During the year we opened an office in Hamburg and in 2008 we opened another in Bordeaux. We remain committed to growth in the territories where we are currently active. Europe has very good loss ratios, and it is through growth and efficiency gains that we expect profits to improve.

£17.2m
Hiscox UK
pre-tax profit

£4.6m
Hiscox Europe
pre-tax profit

£100.8m
Investment return

Hiscox UK and Hiscox Europe

	UK	2007 £m Europe	UK	2006 £m Europe
Gross premiums written	229.2	73.1	207.1	58.7
Net premiums earned	190.3	58.0	178.3	49.5
Profit before tax	17.2	4.6	32.4	0.7
Combined ratio	98.8%	96.2%	92.0%	106.6%

Claims

Two years ago we appointed Jeremy Pinchin as Group Claims Director. Since then, Jeremy has been working in a systematic way with the senior claims team to enhance our claims promise. We have been investing in the operational and technical robustness of our claims function given the growth of key business areas and increased geographic spread. The claims team's work was put to the test this year and they passed with flying colours. In the UK, we received many plaudits for the outstanding service which we gave to many policyholders following the UK floods. Across the Group, claims staff often work in tough situations to return our policyholders to normality as soon as possible. They enhance our reputation of paying valid claims fast.

Operations and IT

As our business grows and develops our IT infrastructure becomes ever more central to our operations. In order to increase our operational resilience to external physical events we moved all the Group's core infrastructure to external data centres in suburban London and Paris during 2007.

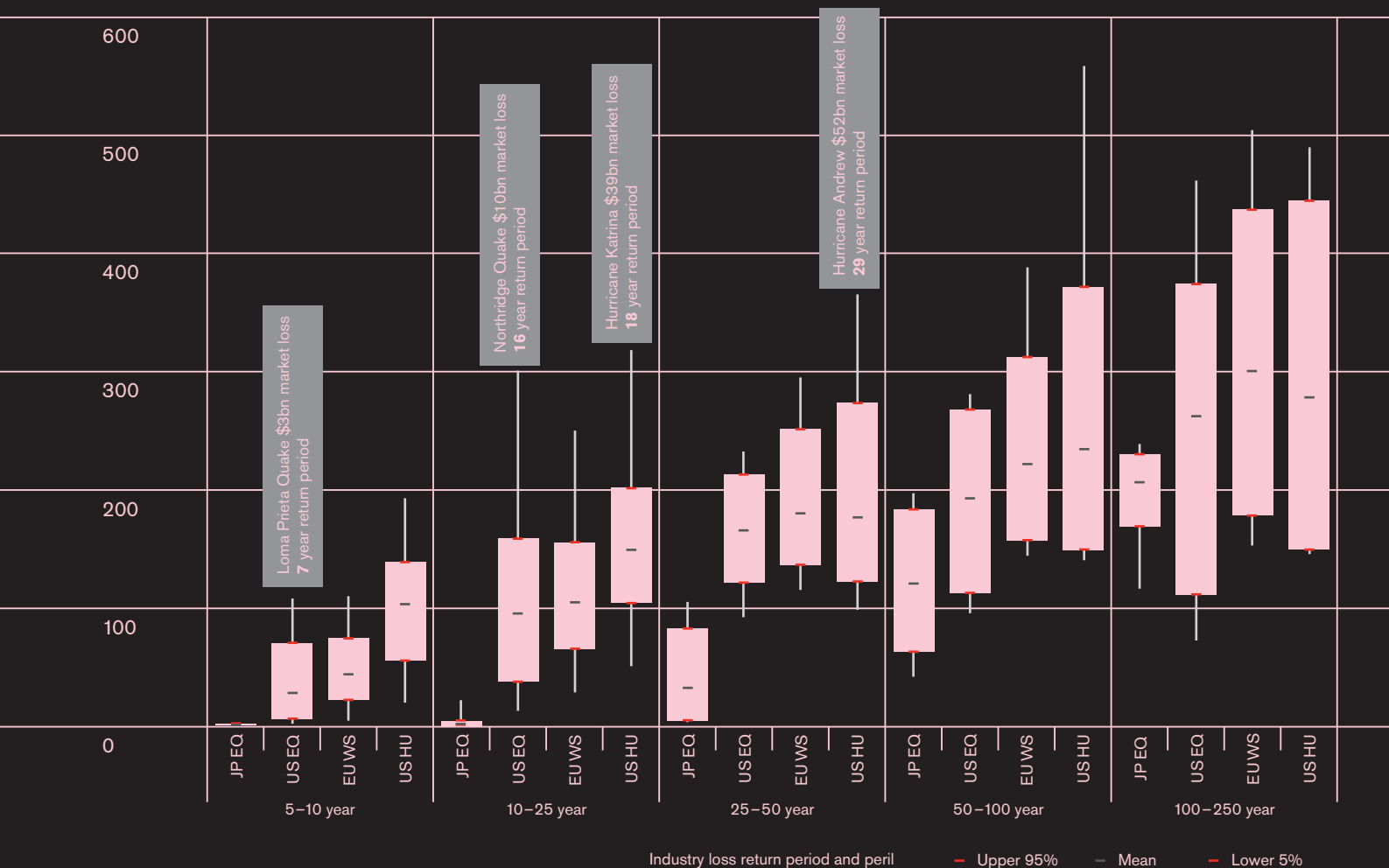
During 2008 we will begin a significant project to migrate our systems onto a new operating platform allowing us to discard older technologies and move to a single system across the Group. The project, which will take around three years and cost £25 million, will enhance operational efficiencies by providing easier access to risk data. The system is designed to support any future growth the Group may experience.

Investments

Invested assets in the Group grew to £2.05 billion (2006: £1.74 billion). Investment income grew to £100.8 million (2006: £78.5 million), a return of 5.4% (2006: 4.6%) on average funds. We have managed to avoid the worst damage from the sub-prime crisis affecting the world. We remain predominantly invested in cash and short duration bonds and have more than sufficient liquidity to meet most eventualities. As the world faces this unprecedented situation we are certain that opportunities will arise. We have made an initial investment in corporate bonds with lower credit ratings than our customary AAA, with a duration of up to five years. We are prepared to hold the bonds purchased to maturity accepting the mark to market volatility as we believe the returns will be more attractive with this approach.

During the course of the year we accepted an offer from the management of Hiscox Investment Management to purchase a majority of the shares of this business. They have renamed themselves HIM Capital and we wish them well in their venture. We retain access to the knowledge of Alec Foster, HIM Capital's Chairman and the overseer of our Group funds for many years, under a consultancy contract. David Astor has succeeded Alec as our in-house overseer of the third party fund managers who have day-to-day responsibility for investing our funds.

Boxplot and whisker diagram of Hiscox Ltd net loss (USD) Hiscox Ltd losses (millions USD)



The chart above shows the variability in net loss the Group expects from individual losses of a given industry loss size.

Balance sheet

Net assets per share grew to 209.5p per share (2006: 173.2p) and tangible net assets grew to 199.3p per share (2006: 164.8p). On the financing front we had a quiet year. We considered issuing longer term debt but the market turmoil that began in the summer made this inadvisable. Our healthy profits and measured growth have led us to consider our own optimal balance sheet structure. The need to have a taut balance sheet has to be balanced against the inevitable increase in exposure to external shocks as the insurance pricing cycle turns. We believe we have struck the right balance in the £100 million capital management programme which we announced in December. £50 million will be spent buying back shares in the market and a further £50 million will be spent repaying debt. In addition, we will be returning almost £50 million to shareholders this year through our dividend. At the end of February 2008 we have spent £14.1 million buying back 5.4 million shares into treasury. The average price paid was 258.7p per share.

People

Hiscox's performance is the result of the efforts of all of our staff. My thanks go to them all, including underwriters and business developers who grew our business at the right price, claims staff who deliver our promise and IT and operations who hold the business together (sometimes with few resources and dated systems). Many went the extra mile to make this result a reality.

Hiscox is committed to continue to equip our staff with the skills required for the changing times. In the year ahead there will be greater emphasis on training for underwriting in a soft market, adapting broker

relationship management to the market and continuing with our leadership development programmes. We feel that if our staff have the best skills, they will deploy them to their own and the business benefit.

Current trading

In our planning process we assumed that rates in the big ticket area would be most under pressure, followed by reinsurance with the specialty and retail businesses being least affected. These assumptions caused us to announce an anticipated 20% reduction in premiums underwritten by Hiscox Global Markets, with Hiscox Bermuda following this lead. To date, renewals have largely met our initial price expectations other than in large property and energy risks. Here price reductions have exceeded our plans and we have revised down our expectations in these areas. We have seen good progress in our retail business areas.

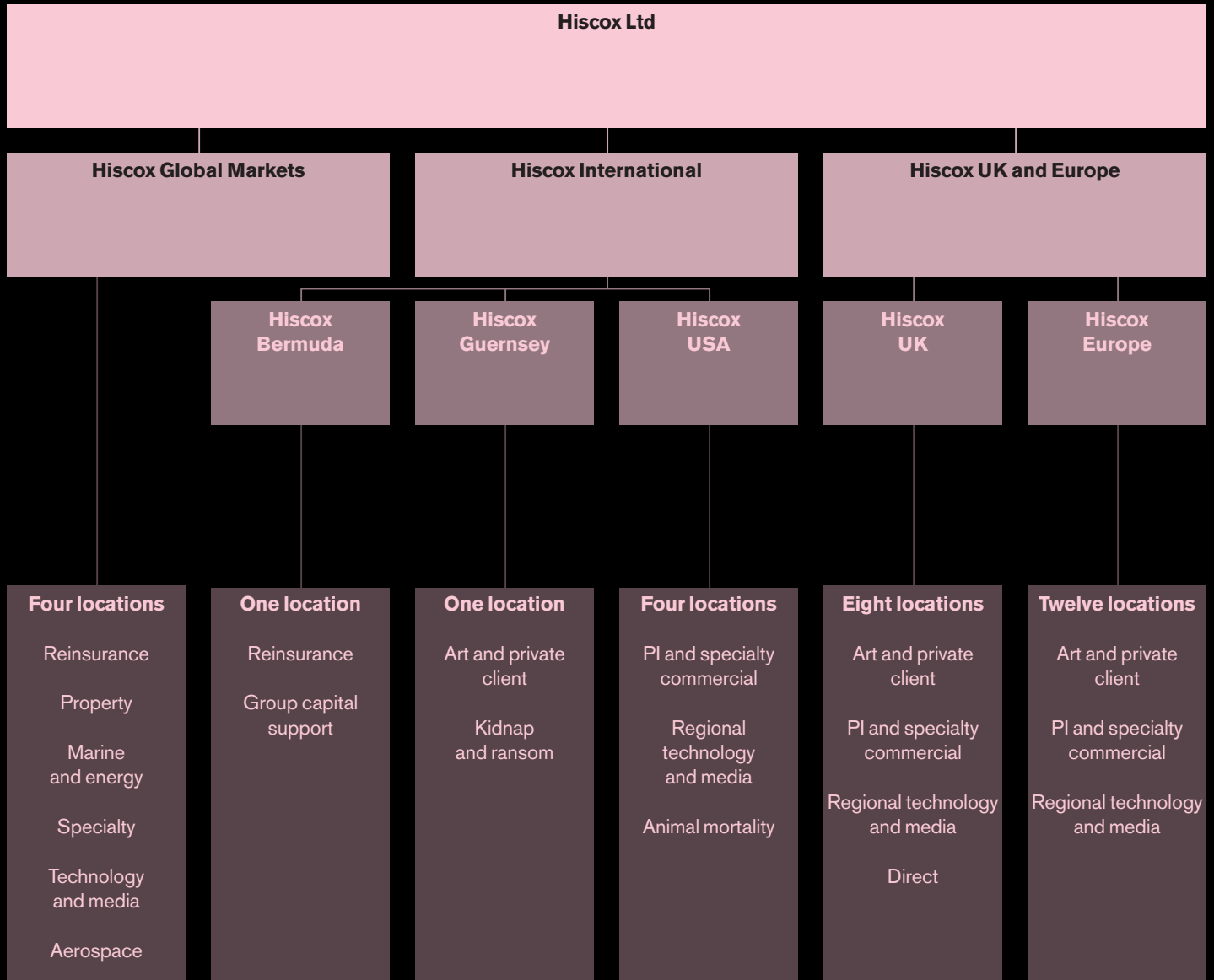
Conclusion

Over the past decade we have built Hiscox from a largely Lloyd's- and London-focused insurance business to a global business with a specialty focus active in multiple regions of the world. This achievement stands us in good stead as we enter a tougher pricing environment. We will continue to balance our retail and volatile risks, giving us the resilience and firepower to respond to the crises and opportunities which will inevitably emerge, to the benefit of the business and its owners.

Bronek Masojada
Chief Executive
3 March 2008

— **Business overview**

Hiscox is now an international insurance Group with a spread of global and regional businesses.



Hiscox Global Markets

Hiscox Global Markets

underwrites insurance and reinsurance business across the world. It uses Lloyd's broker network, licences and coinsurance capability to share in some of the world's largest and most complex risks. Hiscox Global Markets has also developed distribution through hub offices in Paris, New York and San Francisco to access smaller or more sophisticated specialist risks in their local markets such as technology, media and kidnap and ransom.

Highlights

Pre-tax profit £155.6 million (2006: £90.7 million) and a combined ratio of 81.7% (2006: 90.1%)

Panther Re – successful sidecar transaction

Continued focus on risk selection, pricing and aggregation

Security

Syndicate 33 has an A (Excellent) from A.M. Best and uses Lloyd's security, A+ (Strong) from Standard & Poor's and A (Excellent) from A.M. Best.



Richard Watson
Managing Director, Hiscox Global Markets

Joined Hiscox in 1986 as a Political Risk Underwriter. Appointed Managing Director of Hiscox Global Markets in October 2005.

Hiscox UK and Hiscox Europe

Hiscox UK and Hiscox Europe

underwrite local specialty insurance from 20 different regional centres across Europe. Business is sourced mainly through local brokers. There are two main product streams covering:

- the personal property of wealthy individuals, including fine art; and
- the liability and property of professional or advisory and service-led businesses.

Hiscox UK also underwrites executive household, small professional risks and event cover marketed direct to the consumer.

Highlights

Profit despite UK floods £21.8 million (2006: £33.1 million)

Excellent claims performance during floods enhanced brand with customers

Hiscox UK good top line growth in core areas: Art and Private Client, Professions and Specialty Commercial, Technology Media and Telecoms and Direct

25% growth in Hiscox Europe

Security

Hiscox Insurance Company Limited has an A- (Excellent) from A.M. Best and A- (Strong) from Standard & Poor's. Syndicate 33 has an A (Excellent) from A.M. Best and uses Lloyd's security, A+ (Strong) from Standard & Poor's and A (Excellent) from A.M. Best.



Steve Langan
Managing Director, Hiscox UK

Joined in 2005 as Managing Director of UK Retail and Group Marketing Director. Previously Managing Director of Diageo's Italian subsidiary.



Marc van der Veer
Managing Director, Hiscox Europe

Joined in May 2005. Previously headed up directors and officers' liability underwriting, Continental Europe for XL Capital.

Hiscox International

Hiscox International consists of Hiscox Guernsey, Hiscox Bermuda and Hiscox USA.

Highlights

£69.1 million pre-tax profit (2006: £51.9 million) and a combined ratio of 75.4% (2006: 62.7%)

Milestone for Hiscox USA, acquisition of American Live Stock gives access to admitted licences

Hiscox Bermuda had an excellent year despite Windstorm Kyrill, UK floods and California fires

Hiscox Bermuda

Hiscox Bermuda opened in 2005 and underwrites a significant property reinsurance account, predominantly catastrophe and risk excess of loss business and some internal reinsurances.

Security

Hiscox Insurance Company (Bermuda) Limited has an A- (Excellent) from A.M. Best.

Hiscox Guernsey

Hiscox Guernsey has been operating since 1998 and offers a range of products including fine art insurance and kidnap and ransom protection.

Security

Hiscox Insurance Company (Guernsey) Limited has an A- (Excellent) from A.M. Best.

Hiscox USA

Hiscox USA opened in March 2006 and underwrites errors and omissions, kidnap and ransom and terrorism for smaller to medium-sized businesses. American Live Stock Insurance Company underwrites animal mortality insurance.

Security

Syndicate 33 has an A (Excellent) rating from A.M. Best and uses Lloyd's security, A+ (Strong) from Standard & Poor's and A (Excellent) from A.M. Best.



Robert Childs
Chief Underwriting Officer
Chief Executive Officer of Hiscox Bermuda
Chairman of Hiscox USA

Joined Hiscox in 1986. Active Underwriter of Syndicate 33 from 1993 to 2005. Chief Underwriting Officer of the Group for seven years.



Steve Camm
Managing Director, Hiscox Guernsey

Joined Hiscox in 1994 as a Kidnap and Ransom Underwriter. Appointed Underwriting Director of Hiscox Guernsey in December 1998.



Ed Donnelly
President, Hiscox USA

Joined Hiscox in 2005. Previously Senior Vice President at Professional Indemnity Agency, a subsidiary of HCC Insurance Company.

Hiscox locations

Hiscox has 27 offices in 13 countries. Most of these offices service local businesses and individuals with local Hiscox products. These smaller premium products include insurance for higher value homes as well as specialist liability and property risks for professional businesses.

Customers from all parts of the globe place their more complicated or larger business with Hiscox through the Lloyd's and Bermudian insurance markets. In these markets we underwrite a variety of risks from reinsurance and terrorism to contingency.

As local insurance providers become more sophisticated, more business is being underwritten locally. In order to improve broker access to our products, Hiscox Global Markets have opened new offices in New York, Paris and San Francisco. These offices use existing relationships and underwriting expertise to access business that would not be placed in the traditional markets.

Creation of the Hiscox offices

1901	London
1993	Paris
1994	Munich
1998	Guernsey, Leeds
1999	Amsterdam
2000	Birmingham, Glasgow
2001	Brussels, Dublin
2002	Maidenhead
2003	Colchester
2004	Madrid
2005	Bermuda
2006	Armonk, Bristol, Cologne, Lisbon, Lyon, Manhattan, San Francisco, Stockholm
2007	Chicago, Geneva, Hamburg, Manchester
2008	Bordeaux

UK

Birmingham
Bristol
Colchester
Glasgow
Leeds
London
Maidenhead
Manchester

Europe

Amsterdam
Bordeaux
Brussels
Cologne
Dublin
Guernsey
Hamburg
Lisbon
Lyon
Madrid
Munich
Paris
Stockholm

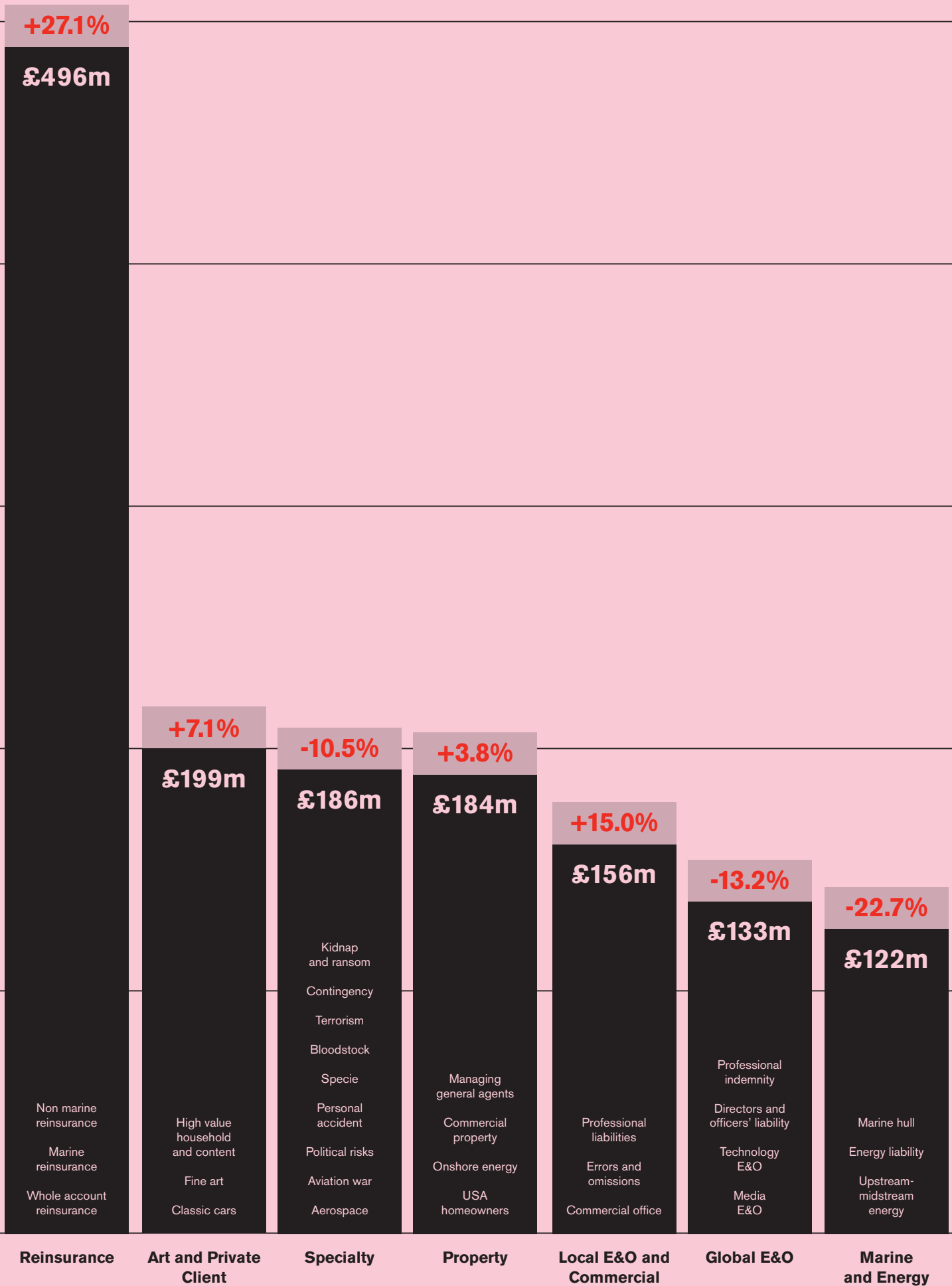
USA

Armonk
Chicago
Geneva
Manhattan
San Francisco

Bermuda

Hamilton





— **Claims at Hiscox**

**We are determined
to make our claims
service better than
the competition.**

Since 2005 the claims team has been working in a systematic way to build upon the operational and technical robustness of our claims function. This has allowed us to maintain high standards given the growth of key business areas and increased geographical spread.

Focus on UK floods

The UK floods in June and July were devastating for those affected and it was a huge event for the industry. Hiscox's claims volume doubled during July, testing our service levels and that of our suppliers. Our claims underwriters, loss adjusters and disaster recovery specialists pulled out all the stops, responding to our clients' difficulties with speed and sensitivity. The ABI predicted the industry would settle 40% of flood claims by the end of 2007. Hiscox had settled over 59% of claims. We expect to have less than ten open claims by July 2008.

Fast and effective

It took 13 minutes for flood waters to rise from three inches to two feet in our customer's Georgian house in North Hampshire. The deluge was beyond the capacity of nearby drains and the failure of the area's pumping station complicated matters. Sewage flooded our customer's kitchen, conservatory, study and the ground floor of an office. Hiscox's loss adjuster arrived the next morning to assess the damage, with the disaster recovery company arriving in the afternoon to remove carpets, sanitise hard areas and start the important drying process with industrial blowers. Our customer said:

“We were very impressed with the service – a loss adjuster was appointed promptly and spent a lot of time on our property. Decisions were made quickly, which I think is important because the longer it takes, the worse the damage will be.”

**Hiscox
pays valid
claims fast**

£452m
paid out in claims
in 2007

— Claims at Hiscox continued

— Feedback on Hiscox from customers affected by the UK floods

“The total service was very professional, very prompt and eased the trauma we felt. Many thanks.”

“The floods brought us great distress. Life became quite fraught and the only salvation in all this was Hiscox. Within 24 hours we were in the hands of a professional team, your staff, the loss adjuster and the salvage team. We soon realised that help and advice was only a phone call away.”

“Best insurance process I have ever been through.”

“Courteous staff. Prompt processing of claim. Fast payment. Very pleased with service.”

Those few Hiscox customers who were still out of their houses at Christmas were sent a hamper. One customer responded with a poem.

**“When life takes a turn
for the dampers,
When house dwellers
turn into campers,
When your council has brains,
As clogged as its drains,
Thank God for Hiscox’s hampers.”**

— Flood risk – a Climatologists view

“We recognise climate change is likely to increase flood risk and our business is preparing for this with increased analysis and modelling of potential risks. We have seen the massive impact that flood has on our customers and the economy. Sadly, some of it could be prevented. The Government needs to raise flood plain management in its list of priorities.”

**Matthew Swann
Hiscox Climatologist**



“Hiscox had faith in me and were determined to fight this to the end.”

Graeme McLagan

Focus on technology and media claims

The Hiscox approach to technology and media claims sets us apart from the competition. Our claims underwriters aim to get under the skin of our customers' business. The team uses its in-depth knowledge of industry risks to help prevent or minimise any problems before they arise. This partnership approach means our claims staff often go beyond the policy commitment to help the insured.

Standing by our policyholders

When freelance journalist Graeme McLagan wrote his book *Bent Coppers: The Inside Story of Scotland Yard's Battle Against Police Corruption*, he and his publishers knew it would be controversial. They were not expecting to be in court for the next four years facing accusations of libel from an ex-police officer backed by the Police Federation. When others would have walked away, Hiscox provided expertise and encouragement. Working with specialist media lawyers, the team was determined to stand by the publisher. The result: The Orion Publishing Group won a landmark ruling in the law of libel by the Court of Appeal which ruled that journalist Graeme McLagan acted responsibly when he researched and wrote the book.

“We felt the High Court had erred in the case. We could also see that there was an important point of law to be defended and winning would have a positive impact on all of our clients engaged in investigative journalism.”

Andrew Sellers
Head of UK and International Technology and Media Claims at Hiscox



— The Hiscox brand

We want customers to reach for a Hiscox policy and be confident that we will deliver great service when they need it most.

**Ambition:
Great underwriting
Superb service
Powerful brand**

“We understand our customers and know they are sophisticated and demanding. The message behind the Hiscox brand is that we will always try to exceed those demands with exceptional service.”

**Steve Langan
Managing Director, Hiscox UK
Group Marketing Director**



Over the last two years Hiscox has spent £23 million on marketing, promoting Hiscox as an insurer you can have confidence in by focusing on our claims record.

The resulting campaigns have been highly regarded and set Hiscox among international brands like Procter and Gamble, British Airways and Tesco.

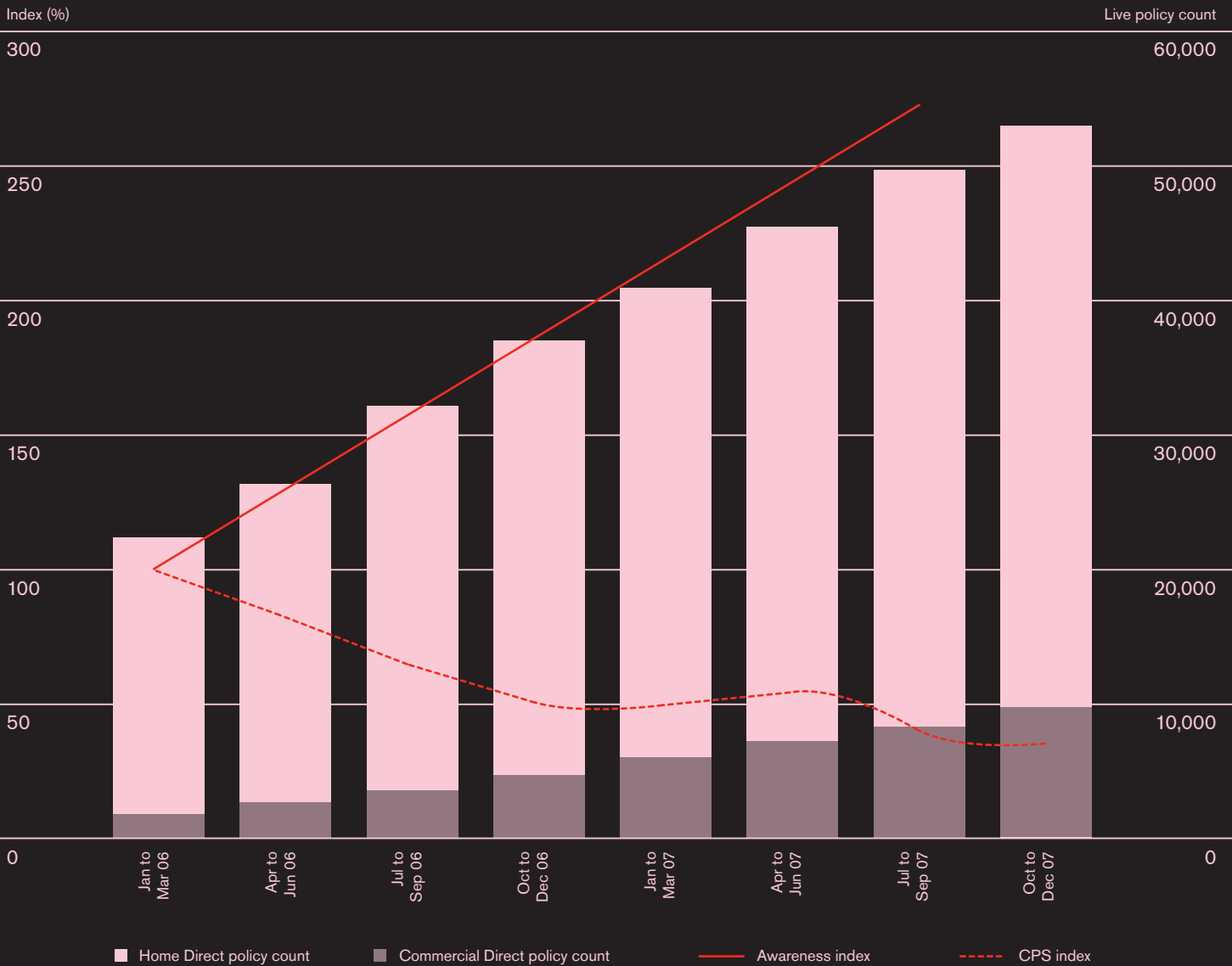
Winners of the Brand Extension category at the 2007 Marketing Society Awards

'Best Use of Data for a Financial Product' in the 2007 Data Strategy Awards

'Best Financial' and 'Innovation' awards in the 2006 Direct Response Intelligence Awards

The Hiscox brand continued

Hiscox Direct Direct marketing cost per sale (CPS), total awareness growth and policy count



Hiscox has a 5* rating (the highest possible) from Defaqto, the independent market researchers, for the most comprehensive cover for its 505 and 506 UK home and contents policies. Our 606 home and contents policy has a Premier rating (the highest possible) from Defaqto for high net worth products.

In 2007 Hiscox was the recipient of the following broker voted awards for the Insurance Times:

- Personal Lines Insurer of the Year
- Commercial Lines Insurer of the Year
- Lloyd's Syndicate of the Year





X3

**Brand awareness
in the UK almost
trebled in two years**

— The people at Hiscox

**We want our customers
to experience Hiscox as:**

**Intelligent not intellectual,
bold not arrogant, thought
provoking not patronising,
different not standard,
straightforward not users
of jargon, positive not pushy,
contemporary not stuffy,
sophisticated not superior.**

“The behaviour and performance of Hiscox employees is what will set us apart from other insurers. Our ambition is to attract and develop extraordinary people.”

Amanda Brown
Group Human Resources Director

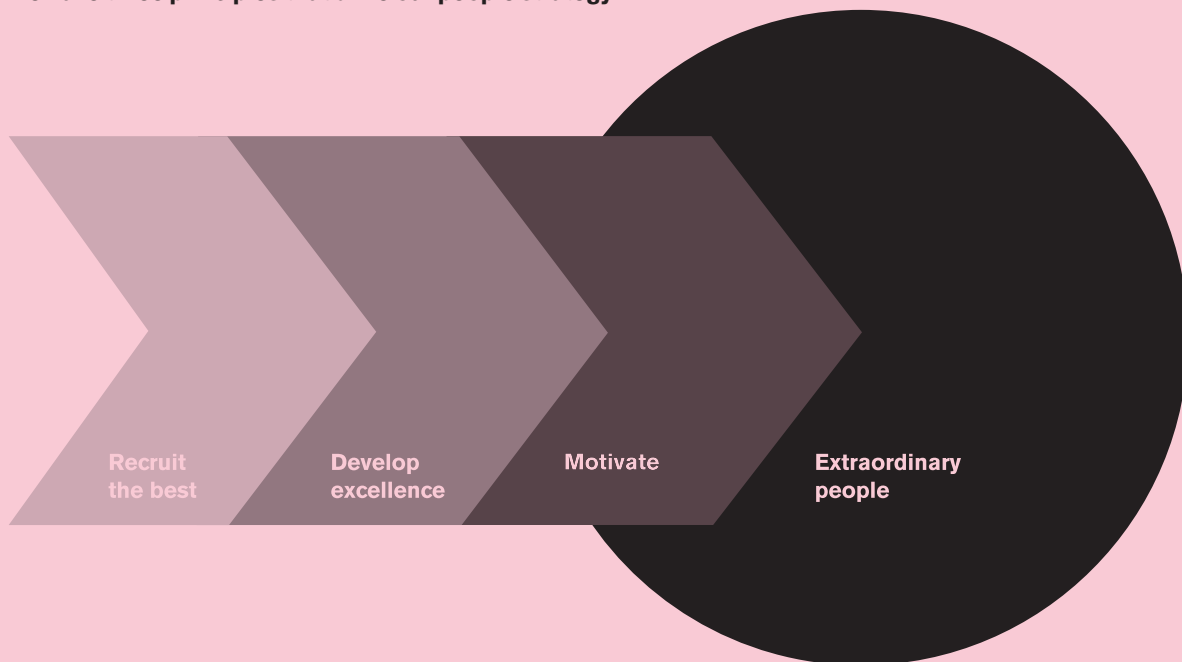


90%

of staff, in an independent employee survey, said they were proud to work at Hiscox

The people at Hiscox continued

We have three principles that drive our people strategy

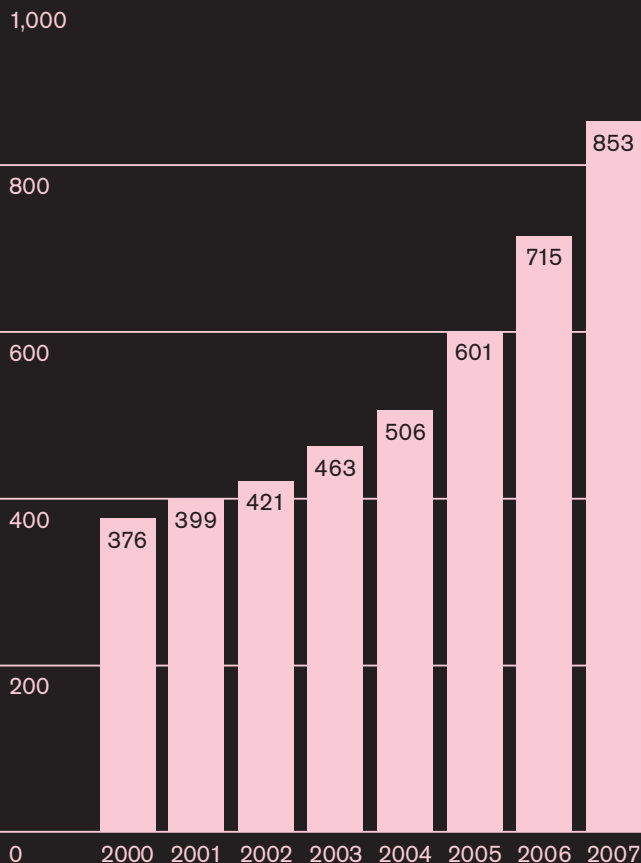


Recruit the best

Where possible, Hiscox aims to recruit internally.

In 2007 one third of new appointments were internal promotions or referrals from current employees. Hiscox has an extremely thorough recruitment process. The average number of candidates seen per hire in 2007 was eight.

Head count growth Total number of staff as at 31 December



“Hiscox is a demanding, challenging client who embraces ‘out of box’ thinking and as a result is able to attract and integrate the best candidates regardless of background. This is not a wood-panelled or long-lunch environment but one which is open, meritocratic, robust, challenging, fast moving and fun.”

Andrew Simpson
Partner and Head of Financial Services Practice
Whitehead Mann LLP

Develop excellence

Hiscox has a unique underwriting training programme developed by very experienced Hiscox underwriters. The training aims to reinforce Hiscox's underwriting standards and covers:

- profitable underwriting;
- learning the lessons of history; and
- approaching every risk with a restless curiosity.

198 underwriters completed this core training programme during 2007. This includes 81% of underwriters from our new businesses in Bermuda and the US.

As the business grows the leadership challenge is being shared with more and more people.

It is a special focus of Hiscox to develop the right kind of leadership skills using and sharing the wealth of experience that exists in the Group. During 2007, 45 people completed the extraordinary leadership training programme.

“During training, it is always interesting and useful to speak to people from other countries. We learn a lot. I guess it is one of Hiscox’s advantages.”

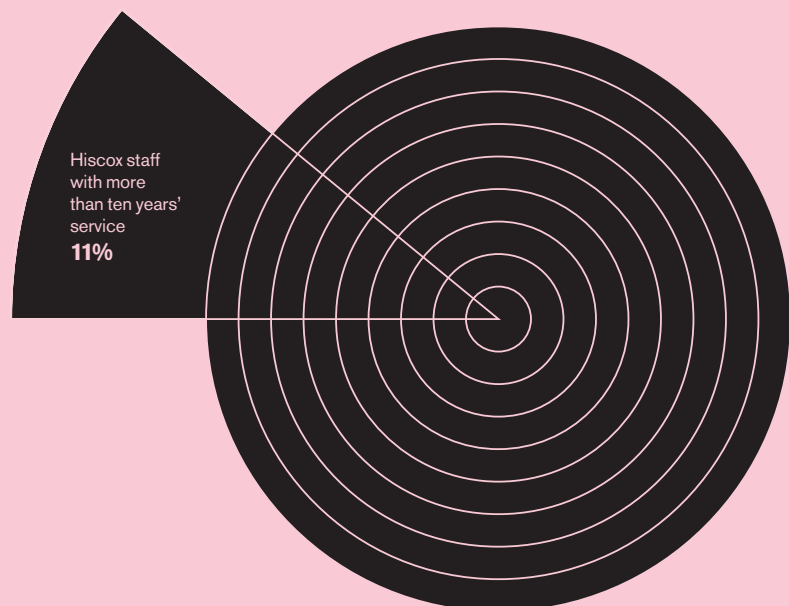
David Viera
Special Risks Underwriter
Hiscox France

Motivate

Having attracted and trained the best people we can find, it is then essential to keep them motivated and thriving in their various roles.

The Hiscox Partnership

One of the motivators to senior people who have contributed significantly to the success of the Group is to be appointed a Hiscox Partner. The Hiscox Partnership is comprised of up to 5% of the total number of staff. The Partnership is informed of all the strategic decisions and facts and figures of the Group, which enables those senior people to influence the direction and performance of the Group. In 2007 nine new partners joined the team.



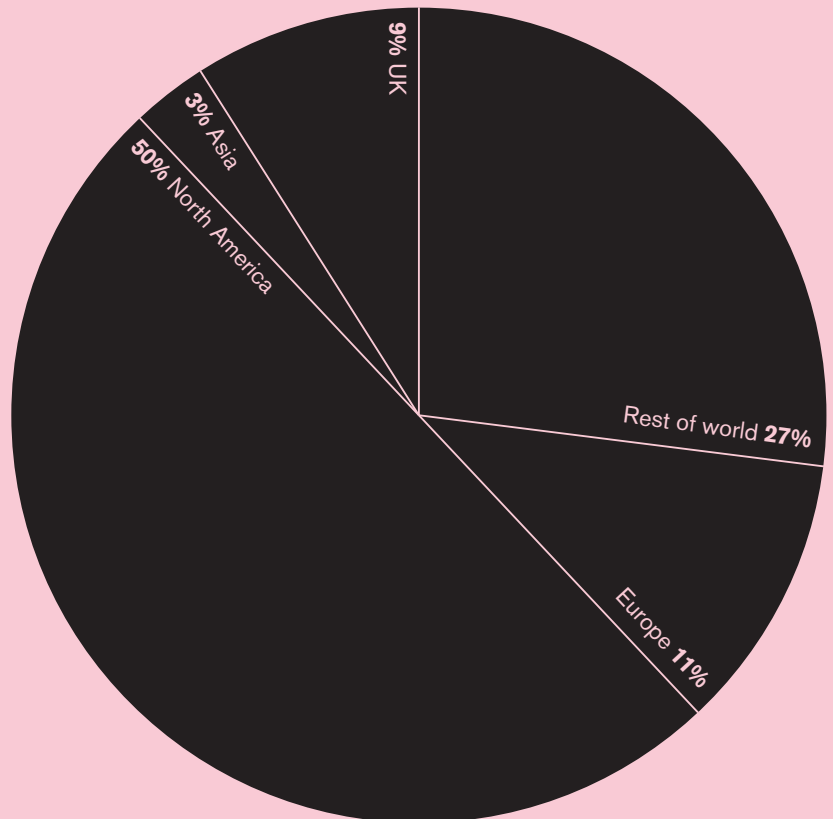
Insurance carriers

Syndicate 33

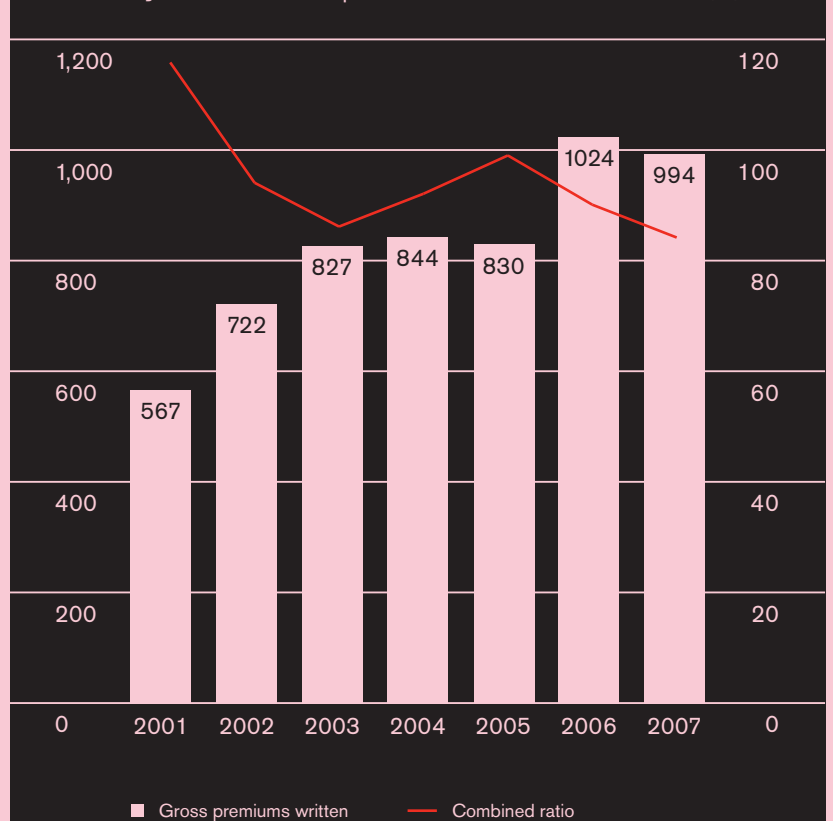
Hiscox can trace its origins in the Lloyd's Market to 1901. Today, Hiscox Syndicate 33 is one of the largest composite syndicates at Lloyd's, and has an A.M. Best syndicate rating of A (Excellent). Syndicate 33 underwrites a mixture of reinsurance, major property and energy business, as well as a range of specialty lines including contingency, technology and media risks among others. The business is mainly property-related short-tail business; there is little exposure to aviation or motor business. Syndicate 33 trades through the Lloyd's worldwide licences and rating. It also benefits from the Lloyd's brand. Lloyd's has an A (Excellent) rating from A.M. Best and A+ (Strong) from Standard & Poor's. The geographical and currency splits are shown on the right. One of the main advantages of trading through Lloyd's is the considerably lower capital ratios that are available due to the diversification of business written in Syndicate 33 and in Lloyd's as a whole. Syndicate 33 has a capital requirement ratio of approximately 50% of Syndicate capacity. The size of the Syndicate is increased or reduced according to the strength of the insurance environment in its main classes. At present, Hiscox owns approximately 72.6% of the Syndicate, with 27.4% being owned by third party Lloyd's Names. Hiscox receives a fee and a profit commission of approximately 17.5% on the element it does not own.

The chart below shows the performance of Syndicate 33 for the last seven years.

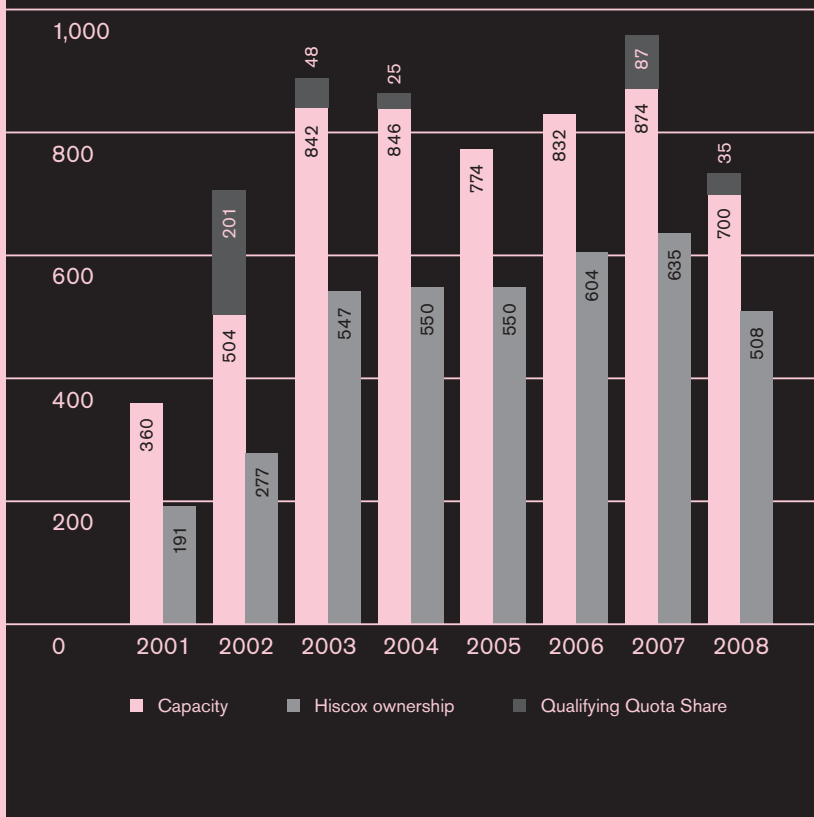
Syndicate 33 2007 Gross premiums written geographical split (%)



Syndicate 33 Gross premiums written and combined ratio (%)



Syndicate 33 Capacity and Hiscox ownership (£m)



Panther Re

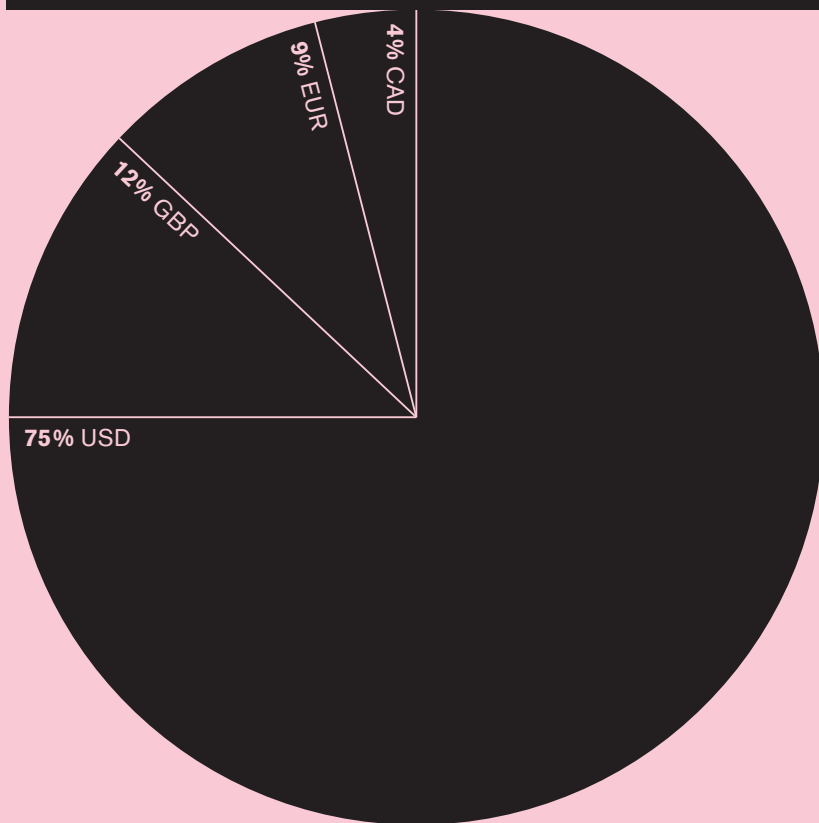
In December 2006, Hiscox announced a market-leading sidecar transaction, which broke new ground within the Lloyd's Market. Hiscox, in conjunction with WL Ross as lead investor, and Goldman Sachs as financial adviser and lead arranger, created the sidecar, Panther Re, which was the first sidecar in the Lloyd's market. A 'sidecar' is a limited-life insurance company, formed to give its investors access to the insurance market, and its cedants access to capital. The quota share arrangement that Syndicate 33 entered into with Panther Re enabled Syndicate 33 to write more of the favourably rated reinsurance business available during 2007. Panther Re's sole activity is the quota share arrangement it entered into with Syndicate 33 for 2007, under which it took a 40% pro-rata share of the Syndicate's property catastrophe reinsurance business. In return Syndicate 33 received a ceding commission and a profit commission.

\$360 million was raised in conjunction with Goldman Sachs and WL Ross to capitalise Panther Re. Hiscox has no equity interest in Panther Re. Panther Re wrote gross premiums of approximately \$160 million in 2007. The sidecar is not controlled by the Group and is not consolidated in the Group's financial statements.

Panther Re and Hiscox Syndicate 33 have agreed that the successful reinsurance partnership between Panther Re and Syndicate 33 covering the 2007 year of account will not be renewed for the 2008 year of account.

Cougar Syndicate

Cougar Syndicate has been set up for 2008 with a capacity of £34.6 million and is wholly backed by external Names. The Syndicate is taking a pure year account quota share of Syndicate 33's international property catastrophe reinsurance account under a limited tenancy agreement initially for a one-year period only. Management is provided by Hiscox Syndicates Ltd.



Syndicate 33 2007 Gross premiums written currency split (%)

Hiscox Insurance Company

Hiscox purchased Hiscox Insurance Company Limited in 1996, in keeping with its aim of diversifying its activities outside of Lloyd's and writing a focused book of regional specialist risks. The Group has reshaped the Company's original portfolio to concentrate on high value household and smaller premium professional indemnity business. Hiscox Insurance Company has licences throughout Europe. It is the primary insurance vehicle used by the UK and mainland Europe offices for their business.

The success of the reshaped portfolio can be seen in the chart below. Hiscox Insurance Company Limited has achieved average compound growth in gross premiums written of 14.2% from 1997 to 2007, despite discontinuing almost all of its original business. It has also significantly improved its combined ratio.

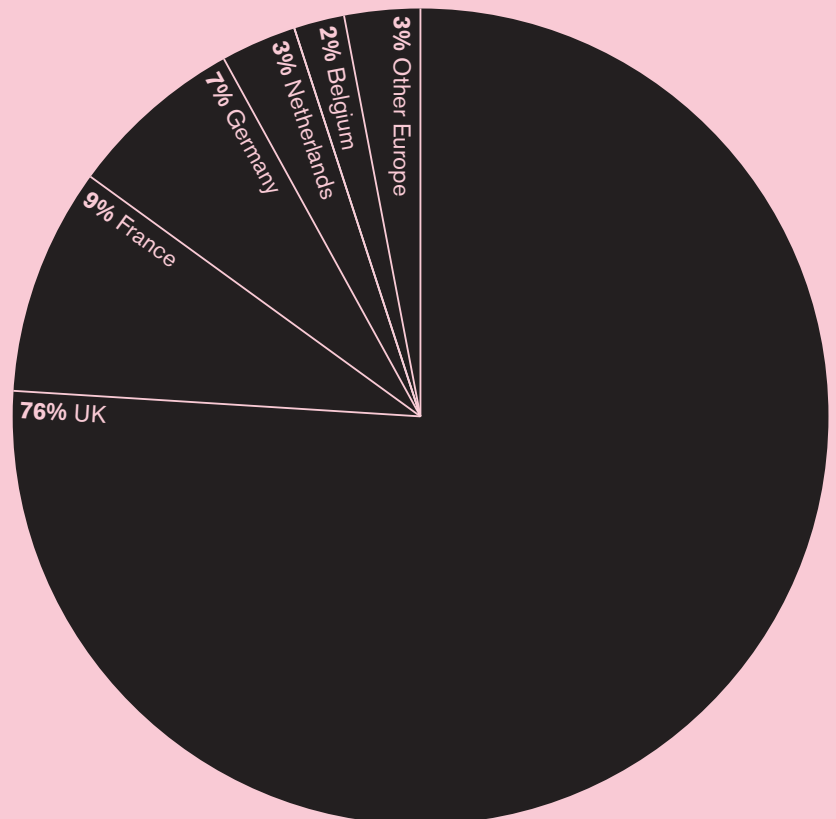
Hiscox Insurance Company Limited continues to be rated A- (Excellent) by A.M. Best and A- (Strong) by Standard & Poor's. At the end of 2007, net assets exceeded £126 million.

Hiscox Insurance Company (Guernsey)

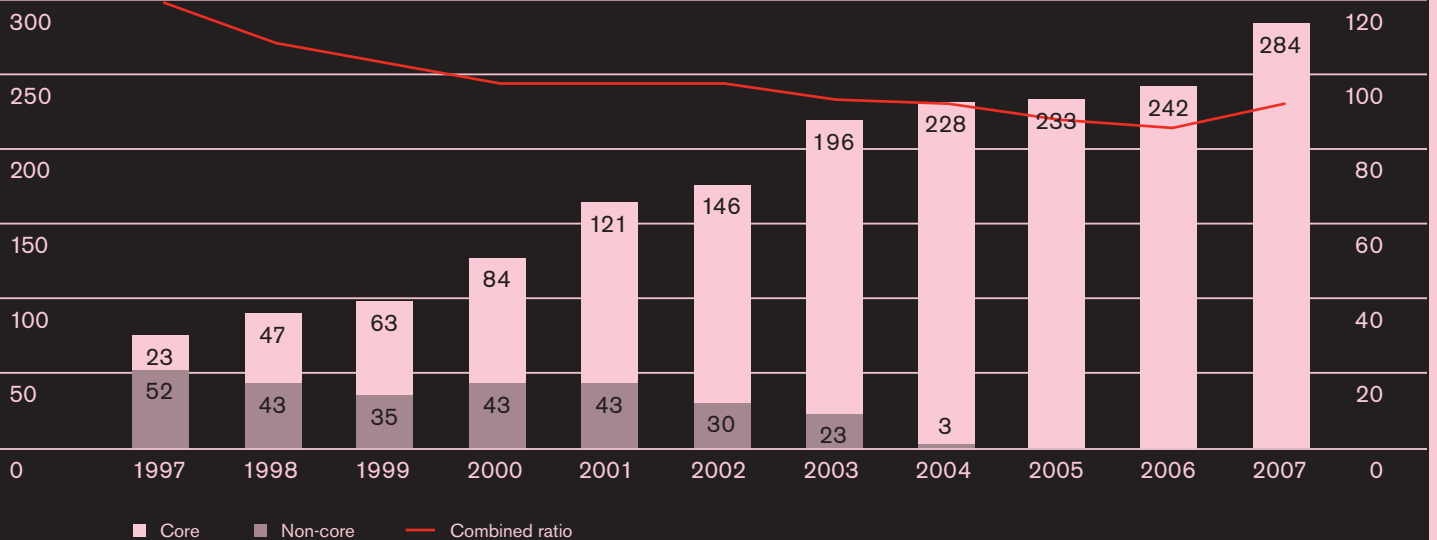
Formed by Hiscox in 1998, Hiscox Insurance Company (Guernsey) Limited writes mainly kidnap and ransom and fine art insurance. Its gross premiums written since inception are shown in the chart opposite. Hiscox Guernsey has an A- (Excellent) rating from A.M. Best.

Hiscox Insurance Company Limited

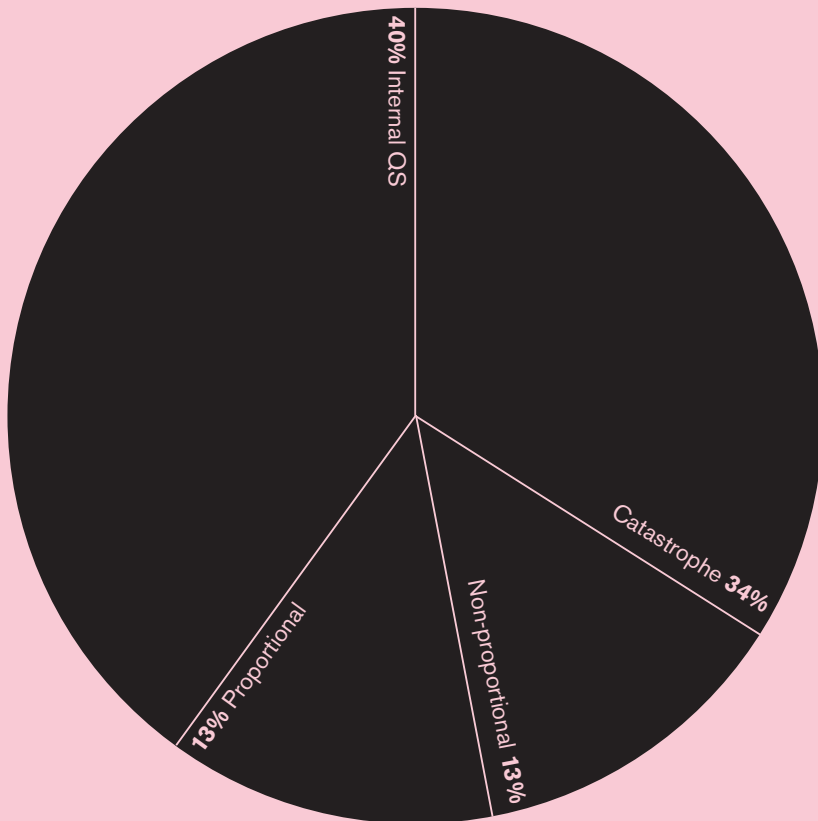
Gross premiums written geographical split by origin (%)



Hiscox Insurance Company Limited Gross premiums written (£m) and combined ratio (%)



Hiscox Insurance Company (Bermuda) Limited
Gross premiums written by class (%)



Hiscox Insurance Company (Bermuda)

Formed by Hiscox in late 2005, Hiscox Insurance Company (Bermuda) Limited completed its first full year of business in 2006. Initially capitalised at \$500 million, it has access to reinsurance business shown to the growing Bermudian market and has also become a vehicle for intergroup reinsurance. Hiscox Bermuda has an A- (Excellent) rating from A.M. Best. At the end of 2007, net assets were \$760.7 million.

American Live Stock

In July 2007 the Group announced the acquisition of ALTOHA, Inc. an insurance holding company and its subsidiaries American Live Stock Insurance Company, the premier live stock insurer in the US, and Harding & Harding, Inc. the affiliated insurance agency. ALTOHA and its subsidiaries are based in Geneva, Illinois and have 25 staff.

American Live Stock Insurance Company is an admitted insurance company with licences in all 50 US states. Its insurance is also available internationally in Australia and South Africa. Its main business is animal mortality insurance for cattle and horses, although farmowners cover is also provided in certain areas. American Live Stock Insurance Company has changed its name to Hiscox Insurance Company Inc. An affiliated agency, Harding & Harding, Inc. has changed its name to American Live Stock Inc. and places all of its business with Hiscox Insurance Company Inc.

Hiscox Insurance Company (Guernsey) Limited Gross premiums written (\$m)



Invested assets in the Group grew to £2.05 billion (2006: £1.74 billion). The investment returns, excluding derivative positions, grew by 28% to £100.8 million (2006: £78.5 million) in the last year due in part to an increase in the Group assets as a result of positive cash flows.

Hiscox has a policy of focusing on high quality, short duration bonds. This has reduced the impact of market volatility witnessed in the second half of the year. We have negligible direct exposure to sub-prime residential mortgage backed securities, which lie at the root of the current market dislocation and all of which remained AAA rated at 31st December 2007. Despite the market conditions, the collateral underlying the mortgage backed and asset backed securities in our US dollar portfolio continues to perform in line with expectations. Similarly our holdings of corporate bonds have seen spreads widen but we expect to recoup any mark to market losses by holding the bonds to maturity. Indeed, we see good value in certain areas of the corporate bond market and expect to add to our holdings. In the last quarter of 2007 we reduced our equity exposure from 10% of overall funds to 7.8% and that has helped during the weak market in early 2008.

Investment policy

The investment policy is designed to maximise returns within the overall risk appetite of the Group. The overriding philosophy with the Group's assets is not to lose money or to put at risk the Group's capacity to underwrite.

Technical funds, the investments held for the payment of future claims, are primarily invested in high quality bonds and cash. The high quality and short duration of these funds allows the Group to meet its aim of paying valid claims quickly. These funds are maintained in the currency of the insurance policy to reduce foreign exchange risk.

Due to the short tail nature of the Group's insurance liabilities, the aim is not to match the duration of the assets and liabilities precisely. Benchmarks are instead set for the fixed income fund managers which approximate the payment profile of the claims as well as providing the managers with some flexibility to enhance returns.

A proportion of the Group's assets are allocated to riskier assets, principally equities. Here, it is the Group's philosophy to take a long-term view in search of acceptable risk adjusted returns. The proportion of the Group's funds invested in risk assets will depend on the outlook for investment and underwriting markets. An allocation within the risk assets is made to less volatile, absolute return strategies. This balances the desire to enhance returns against the need to ensure capital is available to support underwriting throughout any downturn in financial markets.

Group financial performance

The Group achieved a profit before tax of **£237.2 million** in 2007 (2006: **£201.1 million**). Earnings per share were **48.4p** (2006: **41.7p**). The post-tax return on shareholders' equity was **28.8%** (2006: **28.9%**). The underwriting performance of each reporting segment is detailed below.

The net asset value grew to **£824.3 million** from **£682.1 million** driven by profitable contributions from each of the segments. Net asset value per share grew to **209.5p** from **173.2p**.

28.8%
Post-tax return
on equity

Hiscox Global Markets performance

Hiscox Global Markets comprises the results of Syndicate 33, excluding Syndicate 33's fine art, UK regional events coverage, non-US household business and the underwriting result of Hiscox Inc. It includes the results of the larger retail technology and media (TMT) business written by Hiscox Insurance Company Limited.

- Gross premiums written decreased by 4.6% on the prior year. The weaker Dollar to Pound Sterling translation rate obscures real underlying growth in gross premiums written activity of approximately 2%.
- Global Market's reinsurance outwards costs have grown by approximately **£46.2 million**. This is attributable to the Panther Re sidecar arrangement which has taken cedings from the Group of approximately **£54 million**.
- Net premiums written decreased to **£524.7 million** from **£603.6 million**.
- Investment income increased to **£46.6 million** (2006: **£33.1 million**) as continued strong cash generation led to a rise in the average level of assets under management in the Syndicate and interest rates remained at good levels.
- The strong profit before tax increased to **£155.6 million** (2006: **£90.7 million**) following the benign hurricane season experienced this year.
- The combined ratio fell to **81.7%** (2006: **90.1%**).

Group financial performance

	Global Markets 2007	UK and Europe 2007	International 2007	Corporate Centre 2007	Total 2007	Global Markets 2006	UK and Europe 2006	International 2006	Corporate Centre 2006	Total 2006
Gross premiums written (£m)	676.4	302.3	220.2	–	1,198.9	709.1	265.8	151.3	–	1,126.2
Net premiums written (£m)	524.7	265.0	185.2	–	974.9	603.6	234.4	137.4	–	975.4
Net premiums earned (£m)	552.2	248.3	164.6	–	965.2	567.5	227.8	93.5	–	888.8
Investment result (£m)	46.6	18.4	23.9	10.8	99.7	33.1	19.3	16.4	36.7	105.5
Profit/(loss) before tax (£m)	155.6	21.8	69.1	(9.3)	237.2	90.7	33.1	51.9	25.4	201.1
Claims ratio (%)	44.3	45.6	40.1	–	44.0	55.7	41.3	17.5	–	49.3
Expense ratio (%)	37.4	52.6	35.3	–	40.4	34.4	54.9	45.2	–	39.8
Combined ratio (%)	81.7	98.2	75.4	–	84.4	90.1	96.2	62.7	–	89.1
					2007					2006
Financial assets and cash excluding derivative assets (£m)					2,050.6					1,743.1
Other assets (£m)					849.7					914.9
Total assets (£m)					2,900.3					2,658.0
Net assets (£m)					824.3					682.1
Net asset value per share (p)					209.5					173.2
Net tangible asset value per share (p)					199.3					164.8
Adjusted number of shares in issue (m)					393.4					393.7

Hiscox UK and Hiscox Europe

	UK 2007	Europe 2007	Total 2007	UK 2006	Europe 2006	Total 2006
Gross premiums written (£m)	229.2	73.1	302.3	207.1	58.7	265.8
Net premiums written (£m)	202.8	62.2	265.0	182.8	51.6	234.4
Net premiums earned (£m)	190.3	58.0	248.3	178.3	49.5	227.8
Investment result (£m)	15.9	2.5	18.4	15.4	3.9	19.3
Profit before tax (£m)	17.2	4.6	21.8	32.4	0.7	33.1
Claims ratio (%)	45.5	45.2	45.6	39.0	50.2	41.3
Expense ratio (%)	53.3	51.0	52.6	53.0	56.4	54.9
Combined ratio (%)	98.8	96.2	98.2	92.0	106.6	96.2

Hiscox UK performance

Hiscox UK comprises business written by Hiscox Insurance Company Limited in the UK and Ireland. It also includes the results of Syndicate 33's fine art, UK regional events coverage and non-US household business, together with income and expenses arising from the Group's retail agency activities in the UK. It excludes the results of the larger retail TMT business written by Hiscox Insurance Company Limited and the Irish surety business.

- Gross premiums written increased by 10.7% due to increased income from all core lines of business, especially in the direct business and professional and specialty commercial lines.
- Net premiums written increased by 10.9% from £182.8 million to £202.8 million.
- Investment income remained steady at £15.9 million (2006: £15.4 million). Exposure to equity holdings has weighed slightly on relative performance this year versus last.
- Profit before tax of £17.2 million (2006: £32.4 million) was lower than the prior period following the additional marketing and growth related expenses and also due to losses from Windstorm Kyrill and the UK floods.
- The net claims ratio increased to 45.5% (2006: 39.0%). The June and July floods, although well covered by low-level reinsurance coverages, still cost the business approximately £7.5 million net.
- The expense ratio increased to 53.3% (2006: 53.0%) in part due to increased marketing costs.
- The combined ratio increased to 98.8% (2006: 92.0%) due mainly to the effects of the UK floods.

Hiscox Europe performance

Hiscox Europe comprises business written in mainland Europe by Hiscox Insurance Company Limited and the Irish surety business. It also includes the results of Syndicate 33's European fine art, European regional events coverage and European household business, together with the income and expenses arising from the Group's retail agency activities in Continental Europe.

- Europe's gross premiums written has grown by 24.5% as a result of good underlying growth in all established European territories, most notably Holland and France, together with an increase in activity through emergent offices in Portugal, Sweden and Spain. A focus on specialty commercial and TMT business is beginning to augment renewals of the traditional household accounts.
- Net premiums written increased by 20.5% from £51.6 million to £62.2 million.
- Investment income has reduced to £2.5 million (2006: £3.9 million) due a change in the Group investments attributed to the European division.
- The Irish surety business continued its excellent performance in the year.
- Profit before tax increased to £4.6 million (2006: £0.7 million) following moderate net losses but including an exchange gain.
- Europe's net claims ratio of 45.2% represents a 5% improvement on the prior year despite moderate net losses early in the year from Windstorm Kyrill (estimated at approx. £1.5 million) together with a number of medium sized losses during the first half, particularly in the Netherlands and Germany.
- The expense ratio decreased to 51.0% (2006: 56.4%).
- The combined ratio improved to 96.2% (2006: 106.6%), primarily driven by favourable loss ratios in France and the Netherlands as well as in the new areas of European development.

Hiscox International performance

International comprises the results of Hiscox Insurance Company (Guernsey) Limited, Hiscox Insurance Company (Bermuda) Limited, Hiscox Inc. and Hiscox Insurance Company Inc.

- Bermuda gross premiums written increased by 45.5% to £220.2 million from £151.3 million. Bermuda grew gross premiums written so as to benefit from the strong underwriting rates on external catastrophe exposed business. Bermuda gross premiums written growth of approximately 60% was achieved despite the adverse foreign exchange effects of the weaker US Dollar. The US division has grown its gross premiums written by approximately 130% on the prior year. Underlying organic growth of approximately 90% (in translated Pound Sterling terms) has been augmented with approximately £2.9 million of new premiums contributed by the acquired Hiscox Insurance Company Inc. business.
- Net premiums written increased by 34.8% to £185.2 million, driven by growth in gross premiums written.
- Investment income increased to £23.9 million (2006: £16.4 million). The Bermuda investment income surpassed the 2006 level as continued strong cash generation led a rise in the average level of assets under management and US interest rates remained high.
- Profit before tax increased to £69.1 million (2006: £51.9 million) with strong profits from Hiscox Bermuda and Guernsey due to a favourable claims and rating environment.
- The claims ratio was 40.1% (2006: 17.5%) following a benign hurricane season.
- The expense ratio improved to 35.3% (2006: 45.2%). A number of one-off set-up costs were incurred in the prior year.
- The combined ratio increased to 75.4% from 62.7%.

Hiscox Corporate Centre performance

Corporate Centre comprises the investment return and administration costs associated with the Company and other Group management activities. These non-underwriting entities capture the majority of the Group's funding costs.

- Underlying investment income decreased to £10.8 million (2006: £36.7 million), mainly due to a one-off derivative gain of £27 million in 2006.
- Finance costs decreased to £8.1 million (2006: £9.1 million) due a 9% average weakening in the US dollar exchange rate in 2007 plus \$26 million higher borrowings for the first seven months of 2006. The change in average interest rates during the year was mildly negative.
- Loss before tax was £9.3 million (2006 profit: £25.4 million).

Group investment performance

The investment return benefited from the increase in funds under management together with higher interest rates, though the rates in Europe remained relatively low.

Bond portfolios in all currencies had short durations to protect the underlying assets against the changing interest rates in the US and UK.

The Group's equity weighting was increased to 10% in the early part of the year, with a defensive and more globally diversified portfolio which included some absolute return funds. The equity weighting was reduced to 8% in the last quarter of 2007.

Group investment performance

		31 December 2007			31 December 2006		
		Asset allocation %	Return %	Return £000	Asset allocation %	Return %	Return £000
Bonds	£	10.1	5.5		17.7	4.0	
	US\$	50.6	5.8		31.7	4.4	
	Other	9.7	3.7		10.5	2.2	
Bonds total		70.4	5.5	70,688	59.9	4.0	42,095
Equities		7.8	4.1	6,959	8.1	10.6	13,517
Deposits and cash equivalents		21.8	5.4	23,140	32.0	4.6	22,904
Total return			5.4	100,787		4.6	78,516
Group invested assets				£2,050.6m			£1,743.1m

The Group's cash flows originate from multiple sources. Core cash inflows include insurance premium remittances, which are typically received from policyholders in advance of providing risk coverage, losses recovered from reinsurance partners and net investment returns. After allowing for the payment of acquisition costs and other short-term expense requirements, surplus cash balances arising are invested in an optimal mix of assets, concentrated mainly on high quality debt and fixed income securities of short duration.

In general, the investment portfolio produces relatively steady cash returns during periods of interest rate stability. Where interest rates are lower for sustained periods, investment income typically reduces, as the proceeds from higher-yielding securities are reinvested in securities offering coupon payments at lower prevailing market rates. However, it is still possible to realise a partial cash flow benefit in a low interest rate environment, since the underlying market value of the investments tends to increase, leading to higher realised cash gains from their eventual sale.

Other cash inflows result from the sale and redemption of investments, investment management fees and underwriting agency commissions.

Aside from investing activities and the payment of acquisition and operating costs, the Group's principal cash requirements are primarily for the settlement of insurance claims, to pay for reinsurance cover, to settle fiscal tax liabilities, to service and reduce borrowings and to distribute dividends to shareholders.

The Group's cash flow is impacted to a large extent by the results of Syndicate 33. Until 2005, the Group had in general only received cash from the Syndicate following the closure of a year of account at the end of three years, except when Lloyd's allowed early profit distributions subject to solvency requirements. However, from 2006 onwards, syndicate cash distribution has been determined on a one-year accounting basis, although still subject to solvency requirements.

Cash flows for 2007

Cash flows from operating activities

A net cash outflow arose from operations during the year of £162.7 million (2006: inflow of £157.4 million) principally as a result of the Group making a net cash investment of £489.7 million (2006: £1.3 million disinvestment) into holdings of slightly longer dated financial assets that do not qualify for presentation as cash equivalents. The underlying positive cash conversion from operations of £327 million (2006: £156.1 million) was strong once again. The £170.9 million improvement on the prior year reflects the profitable growth in gross underwriting activity together with good collections of outstanding amounts from reinsurance partners. In addition, substantial payouts were made in the prior year in relation to large hurricane related catastrophe losses suffered in 2005.

Investment revenue receipts excluding derivative transactions increased by over 28% or almost £20 million on the prior year to £90.2 million, partially as a result of the larger portfolio generated from the growth in premiums collected and higher shareholder funds and also due to higher interest rates prevailing for much of the current year under review.

Interest payments of £8.2 million (2006: £9.4 million) were made during the year in respect of the Group's US\$182 million borrowings and assets held under finance leases. The reduction on the prior year is mainly attributable to the relative weakness in the US Dollar exchange rate during 2006 and \$26 million of principal repayments being made in July 2006.

Current tax payments increased to £42.8 million (2006: £36.4 million) mainly in anticipation of the higher attributable UK based profits falling due to be taxed and paid.

£327m
positive cash conversion
from operations

28%
increase in investment
revenue receipts

Cash flows from investing activities

2007 was a year of significant investment activities involving cash outflows. In July the Group announced the acquisition of the ALTOHA Inc. Group in the USA which involved a net outflow of cash of £11.1 million. The Group also experienced a net cash outflow of £0.9 million on the disposal of Hiscox Investment Management Limited in December.

Three new associate companies were purchased during the year which required net cash payments of £1.3 million.

Capital expenditure on fixed assets grew by £2.3 million to £7.8 million reflecting the start of a major IT transformation project in the Group.

£2.5 million cash was also spent acquiring intangible customer relationship assets during the year (2006: £0.3 million).

Cash flows from financing activities

The net cash outflow from financing activities rose by £8.6 million to £50 million, primarily due to an additional £13 million of dividends and £11.3 million in respect of shared buy-backs offset by £14 million of debt repayment in 2006.

£54.9 million (2006: £30.4 million) was returned to shareholders during 2007 comprising dividend payments of £43.6 million (2006: £30.4 million) and share repurchases of £11.3 million.

£5.2 million (2006: £3.2 million) cash was received in respect of share options exercised during the year.

£0.3 million (2006: £0.1 million) was paid in respect of finance lease obligations during the year. None of the Group's borrowings fell due for repayment during 2007 (2006: net payment of £14.2 million). It is management's intention that net debt will be reduced by approximately £50 million during 2008 excluding letters of credit. Investment income generated on the proceeds of borrowings largely offsets the interest obligations. However, such interest income is reported separately with operating activities in the cash flow statement.

Relationship between cash flow statement and income statement

The Group's premium income can only be earned as the risk coverage period to which it relates elapses. Consequently whilst the cash flow statement reports on actual funds received in the year from premiums written, the income statement is influenced by the exclusion of newer premium inflows relating to future risk coverage periods. Likewise much of the cash outflows made during 2007 relate to claim liabilities recognised in prior income statements.

Liquidity of debt and fixed income securities

The availability of funds at short notice is a prerequisite for any insurance business with short tail exposure to catastrophic events. The Group retains a deliberate level of debt and fixed income securities in instruments with imminent maturity dates which can be liquidated rapidly for cash as required.

Notwithstanding the contractual maturity profile of these securities, the Group is able to realise cash from its investment portfolios in a reasonable manner as and when required.

£489.7m
net cash investment
into financial assets

£54.9m
cash returned
to shareholders

Risk management framework

The risk management framework extends to all aspects of risk including insurance risk, market risk, credit risk, operational risk, liquidity, social, environmental and ethical risk.

The core business of Hiscox is dealing with risk. The understanding of risk is intrinsic to every level of decision-making in the Group.

The risks associated with the core business represent some of the greater exposures, however the Group is exposed to a number of other risks and has developed systems and procedures to identify and manage them.

Risk appetite is set by the main Board and cascaded down into the Group's operations through management and specialist committees. These latter committees have terms of reference that assign specific areas of focus, and oversee activities such as underwriting, loss modelling, reinsurance purchase and security, broker credit risk, investments, claims reserving and business continuity.

Senior management responsibilities are clearly identified together with their reporting lines and the execution of delegated responsibility is closely monitored by reporting to the Board and its committees. This monitoring, supported by financial and non-financial management information, covers performance against agreed targets and objectives, as well as the risks to achieving these objectives and the effectiveness of the measures in place to manage these risks.

In parallel with these direct risk management processes, there is a dedicated risk management function which, in conjunction with Internal Audit, monitors and reviews the effectiveness of risk management throughout the organisation and reports to the Board. These functions are organised centrally to assist in the integration of best practice throughout the Group. Risk management tools allow individual Group businesses to assess their own risks locally whilst feeding into weighted global reports at Group level.

Major risks

The major risks that the Group faces are presented below. A number of these factors are common to all insurance businesses, while others are relevant to Hiscox specifically. For a discussion of the major risks and uncertainties impacting the Group's financial statements, see note 3 to the financial statements.

Catastrophe and systemic insurance losses

Like other insurers, the Group's earnings can be affected by unpredictable events and circumstances. These may include, but are not limited to, conditions such as natural and other catastrophes, legal developments, social change and the emergence of latent risks. Such events could create significant levels of losses if the Group's underwriting models, aggregation tools and policy wordings do not prevent unplanned concentrations of risk, both in geographical regions and types of policy.

The failure to manage concentrations of exposure is therefore the single greatest risk to Hiscox.

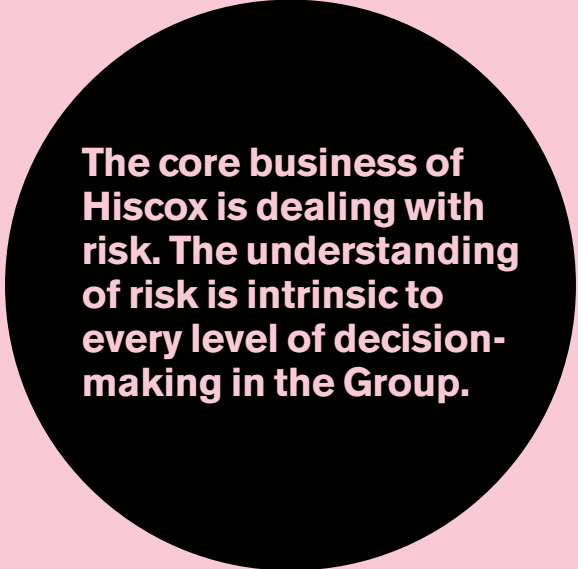
The Group continues to underwrite significant risks in geographical regions that are prone to natural peril. This business remains a compelling proposition for the Group, since it is capable of returning impressive margins over the medium- to long-term as the occurrence of catastrophes averages out.

By its nature, this business requires that underwriting staff exercise the greatest possible levels of foresight. The Group has developed robust risk management and mitigation techniques in preparation for the challenges that these risks present. These techniques are designed to shield the core capital base of the Group against unexpected, repeat clusters of all but the most destructive of events.

The portfolio of risks is actively managed to maintain a balanced and diversified book. This is supported by the use of exposure aggregation and scenario modelling tools and by the purchase of a reinsurance programme designed to cap losses from concentrations of risks. Policy wordings are reviewed regularly in the light of legal developments to ensure that the Group's exposure is restricted, where possible, to those risks identified at the time of policy issuance.

The modelling and monitoring tools are used both in the underwriting process and by independent risk specialists. They are used to design the insurance and reinsurance programmes and control the business underwritten to ensure that the risk profiles of contracts match the exposures for which the programmes were devised.

Aggregation and modelling resources are shared across the Group. Management at Hiscox insurance subsidiaries worldwide are therefore



The core business of Hiscox is dealing with risk. The understanding of risk is intrinsic to every level of decision-making in the Group.

able to adopt the Group's existing methodologies and models, albeit tailored to the intricacies of that particular market. Hiscox also runs realistic disaster scenario projections for each Group entity and for the Group as a whole. The Group's maximum net retentions based on the estimated losses from these scenarios are outlined in note 3.1 to the financial statements.

The Group's performance relative to the unprecedented impact of catastrophes on the industry in recent years highlights the ability of its models to suggest precise and logical reinsurance placements. It also shows the distinctive benefits that Hiscox derives from its diversification in coverage and geography. By writing a well-diversified book with a large focus on uncorrelated retail business, Hiscox is able to offset losses on its more volatile accounts.

Competition and the insurance cycle


Hiscox is continuing to grow its regional presence in the UK, Europe and USA. In all of these markets around the world, Hiscox competes against major international groups with very similar offerings. At times, a minority of these groups may choose to underwrite for cash flow or market share purposes and at prices that sometimes fall short of the suggested break-even technical price.

The Group is firm in its resolve to reject business that is unlikely to generate underwriting profits. Accepting insurance risk below the technical price is detrimental to the industry's prospects, since it drives the prevailing rates in the market lower to the point where business failures occur, insurers' capital is destroyed, customers receive sub-optimal service and the industry suffers from negative

publicity. As capacity levels in the market fall, prices inevitably rise until the point where the cycle of irrational pricing may begin again.

In common with all insurers, the Group is exposed to this price volatility. Prolonged periods of low premium rating levels or high levels of competition in the insurance markets are likely to have a negative impact on the Group's financial performance. Pricing levels are monitored on a continuous basis with monthly reports showing both current levels and trends over the past 12 months throughout a wide range of products.

To counter this, Hiscox alters its appetite for the lines of business and the layers it writes within them in response to market conditions and the risk appetite of the Group. The Group's cycle management strategy and related modelling and monitoring are essential to ensure that it controls any accumulating adverse effects of changes.



Hiscox is continuing to grow its regional presence in the UK, Europe and USA.

As the Group frequently acts as the lead insurer in the complex co-insurance programmes required to cover significant high value assets, it has some ability to set market rates rather than follow them.

Mutualisation is a related risk arising from the phenomenon of pricing cycles in the industry. The Group is required to contribute towards obligations of other insurers who fail. Syndicate 33 contributes to the New Central Fund operated by the Council of Lloyd's, and in the UK certain Hiscox entities contribute to the Financial Services Compensation Scheme (FSCS). Should the level of failures escalate, the Group could be subject to additional or special levies by Lloyd's and/or the FSCS.

The Group participates in many industry bodies, associations and task-force initiatives in order to monitor developments and influence their strategic direction. In particular, the involvement of the Group's executives in the reshaping of the Lloyd's market underscores that commitment.

Binding authorities and other outsourcing

Hiscox writes a considerable amount of premium income through agents to whom binding authority is given to accept risks on behalf of Hiscox Group insurance vehicles. Binder management exists as a separate discipline outside of the underwriting process at Hiscox. All delegations are strictly controlled through tight underwriting guidelines and limits and extensive vetting, monitoring, and auditing of the agencies. However, as there is no absolute guarantee that an agent will comply with the terms of its authority, Hiscox could be exposed to unanticipated losses.

Other business areas where the Group is to some extent reliant on the timely and effective supply of services from third parties include back office policy processing, data entry and cash collection. Although the Group manages these relationships to ensure continuity and quality of service, events could occur beyond its control that could affect these third parties and in turn impact on the Group's performance.

The Group selects its agents and business partners carefully. Significant areas of outsourcing undergo a rigorous tendering process, where numerous attributes other than just price competitiveness are given due consideration. All third parties operate within the terms of formal service level agreements, with repercussions for underperformance.

Credit risk with reinsurance counterparties

The Group purchases reinsurance protection to contain its exposure to single claims and the aggregation of claims from catastrophic events.

The Group places reinsurance with companies that it believes are strong financially and operationally. The limits on reinsurance counterparty risk are recommended by the Reinsurance Security Committee, which meets regularly under the chairmanship of the Group Finance Director. Evaluation criteria include financial strength, trading record, payment history, outlook and organisational structures. Information is drawn from the following sources: public information produced by the company; the Group's experience with the reinsurer and knowledge of their behaviour in the marketplace; analysis from a reinsurance consultant; rating agency commentary and gradings.

Sidecars have continued to be popular vehicles for acquiring additional capacity. These are reinsurance companies which participate in the business of another insurer, but which are separately capitalised or offer security or both. These companies may offer very high levels of reinsurance but are often vehicles of only a limited and very short-term duration and their attractiveness is highly dependent upon the amount and quality of collateralisation offered. Some reinsurance transactions have been entered into with these vehicles but each has been individually approved. There remains a risk that in the event of this shorter-term capacity being withdrawn following large losses it may be more difficult to replace in the conventional market. During the year the Group was the sole client of Panther Re, a Bermudian reinsurer that takes a 40% share of certain property catastrophe reinsurance lines written by Syndicate 33. This arrangement was not renewed for 2008 and was in part replaced by the new Cougar Syndicate.

The Group's experience of bad debt losses arising from its reinsurance arrangements has been minimal.

Claims volatility

The Group establishes provisions for unpaid claims, defence costs and related expenses to cover its ultimate liability in respect of both reported claims and incurred but not reported (IBNR) claims. These provisions take into account both the Group's and the industry's experience of similar business, historical trends in reserving patterns, loss payments and pending levels of unpaid claims and awards.

Reserve estimates are subject to regular reviews. Adjustments are made to take into account management's latest view of the probable ultimate liability, based on claims and other developments and new data. Yet there can be no absolute guarantee that the ultimate losses will not differ materially from the provisions the Group has established. It is particularly difficult to estimate IBNR claims and those arising from large catastrophes. Note 24 to the financial statements provides information on the Group's estimation of ultimate claim costs over recent years. Additional information is provided in note 3 to the financial statements.

Business continuity

It is critical for Hiscox that the key resources required to support insurance underwriting and other essential business activities continue to be available. The Group has taken significant steps to mitigate the impact of business interruptions that may result from a variety of events, including the loss of key individuals and facilities such as premises, computer networks and communications. The Group's business could be affected adversely if staff were to be prevented from using its major premises for any reason. The Group's staff are widely distributed with offices around the UK, Europe, USA, Bermuda and Guernsey. This geographical dispersion reduces the Group's exposure to natural, operational and terrorist events that could prevent access to its premises.

The business also relies on IT and telecommunications systems. Whilst the Group considers its systems to be resilient, their failure or impairment, or the inability to transfer data onto any new systems introduced, could cause a loss of business and/or damage to the reputation of the Hiscox Group, as well as remedial costs.

The most difficult continuity risk for Hiscox to manage is the loss of key staff. The recruitment and retention of high quality people is of fundamental importance to Hiscox and the Group takes the risk of losing such assets very seriously. To maintain the loyalty of staff, the Group provides competitive remuneration packages and benefits as well as extensive training and support and a unique culture that embraces the individual and their aspirations. More information about Hiscox's investment in its people can be found on pages 30 to 33.

In the event that key staff do leave, the Group's contingency plans ensure continuity of service both internally and to policyholders. These include cross-training and rotation of duties to ensure that staff can perform multiple roles. Most staff work in teams rather than in isolation, which lessens the impact of normal staff turnover on the business.

Hiscox has a formal disaster recovery plan that addresses its premises and technology related risks. Robust contingency strategies are in place for both workspace recovery and back-up of data centres and communications. In the event of an outage, these procedures will enable the Group to move operations to alternative facilities within very short periods of time. The alternative facilities are supplied by separate localised utility grids and telecommunications carriers. The disaster recovery plan is tested regularly and the Group also performs disaster simulations.

Currency fluctuations

The US Dollar is the Group's largest underwriting currency. A significant proportion of the Group's US Dollar insurance liabilities are supported by investments held in the same currency. However, as a significant proportion of the Group's operational cost base is located in the UK and Europe, movements in foreign exchange rates may have a material adverse effect on its financial performance and position.

Further details of the Group's investment profile and its management of currency risks are provided in notes 3, 18 and 20 to the financial statements.

Investment returns


The Group's entities hold significant portfolios of investments to support their obligations, including their insurance liabilities, and their profits depend in part upon the returns that these achieve. Changes in interest rates, equity returns and other economic variables can therefore affect the Group's financial performance substantially. A fall in the capital value of their investments could result in a reduction in the level of business that each entity is able to underwrite. In addition, a major insurance loss or unexpected sequence of attritional losses could result in a sustained cash outflow that might require the early realisation of investments on unfavourable terms.

The Group's investment strategy seeks to minimise the concentration of investment risk in any one particular sector.

Regulation

The Group's entities are incorporated and transact business in a variety of countries and states, all of which require strong levels of accountability to the local regulatory authorities.

The various Hiscox businesses operating in the UK are subject to high levels of regulation from the FSA and the Council of Lloyd's. The numerous regulatory bodies that oversee the Group's international operations include the Guernsey Financial Services Commission, the Bermuda Monetary Authority and individual state insurance departments in the USA. These bodies all have significant powers of intervention including the ultimate sanction of removing the authorisation to carry on insurance business.



Robust contingency strategies are in place for both workspace recovery and back up of data centres and communications.

Regulatory action could affect the Group's results and position in numerous ways. For example, it could be required to allocate inefficient levels of capital around the Group in order to overcome minimum regulatory hurdles, or bear the costs of implementing new compliance or sophisticated computer modelling systems.

Continual changes in, or inappropriate levels of, regulation in the Group's markets could also result in their becoming uncompetitive or unattractive to customers, which might lead them to place their insurance business in alternative markets in which the Group has no presence.

Hiscox devotes considerable resources throughout the Group to meet its regulatory obligations. The senior management of each Hiscox business maintains constructive, productive and valuable relationships with all of the regulatory bodies in their respective territories. Furthermore, the Group debates all current regulatory issues and encourages the development of new initiatives in areas such as risk management and reporting that will help safeguard the future of the industry.

Rating agencies

The ability of the Group's insurance operations to write certain classes of business, including reinsurance, may be affected by a change in the financial strength or credit rating issued by an accredited rating agency such as A.M. Best, Moody's or Standard & Poor's.

Syndicate 33 has its own rating and also benefits from the Lloyd's global rating. The Lloyd's rating could be affected by matters outside of the Group's influence or control. Hiscox Insurance Company Limited, Hiscox Insurance Company (Guernsey) Limited and Hiscox Insurance Company (Bermuda) Limited have their own ratings from accredited agencies.

A downgrading of any of the rated entities could have a material adverse impact. The Group might cease to meet the security criteria of brokers, resulting in a loss of new business, policy cancellations and non-renewals. The Group's borrowing facilities might also be subject to review.

The Group maintains an excellent relationship with the agencies that rate its entities.



The Group's investment strategy seeks to minimise the concentration of investment risk in any one particular sector.

Group senior management holds several meetings with representatives from the agencies each year and gives due consideration to the likelihood of rating consequences before executing any significant strategic action.

Fundamental to corporate and social responsibility is honest and fair dealing in all activities of the Company. Hiscox has always been extremely conscious of its reputation. Management has always believed that a reputation for integrity and decent behaviour in all dealings, be they within the Group or with those from outside who come in contact with the Group, will be good for morale and for the results of the business.

Robert Hiscox

Hiscox's commitment to responsible business practices is reflected:

In the marketplace

Dealing with customers

Hiscox UK is dedicated to advising customers on risk management to prevent burglary and fire in the home and other distressing losses. Should a loss occur, the Hiscox UK philosophy is that insurance is a promise to pay, and the claims service aims to support customers and make them whole as soon as possible. For more information about Claims at Hiscox see pages 22 to 25.

Dealing with business partners

Insurance brokers are an important Hiscox stakeholder, and Hiscox endeavours to have good relationships with them to create a competitive advantage in the marketplace. Clear communication is key to good relations and a quarterly Hiscox broker magazine keeps brokers informed of developments at Hiscox and in the insurance industry.

Dealing with investors

In keeping with its policy of open and transparent communication, Hiscox reports both its half and full year results to its investors via a series of presentations as well as ensuring all relevant Group financial information is available from its website. In addition, senior management and key performers meet investors and analysts to explain and take questions on the Group financial performance and business strategy.

In the workplace

Hiscox wants to employ the best people and provide them with the means and the motivation to excel. This is achieved with fair rewards and by providing staff with an environment in which they can enjoy their work and reach their full potential. Hiscox recognises how important it is for employees to maintain a healthy work/life balance and gives staff the option of flexible and home working wherever possible.

Equal opportunities

Hiscox is committed to providing equal opportunities to all employees and potential employees in all aspects of employment regardless of disability, sex, race, religion, sexual inclination or background.

Rewards and benefits

Hiscox encourages employees to identify with the success of the Group through performance-related pay and bonus schemes, savings-related share option schemes and executive share option schemes. Competitive benefits packages contain health, fitness, flexible working and career break opportunities. Salary packages are benchmarked by Watson Wyatt against the financial services industry as a whole and against the Lloyd's market specifically, where applicable.

Training and development

Hiscox is committed to training and developing its employees to help them maximise their potential. Each permanent member of staff is provided with a tailored personal development programme. Training and development needs are reviewed twice a year, along with performance, against clearly set objectives.

Communication and participation

Employees are kept informed of business developments through formal briefings, team meetings, intranet bulletins, video conferences and informal routes. Management takes these opportunities to listen to staff and involve them in taking the business forward. A monthly staff e-zine provides updates on issues and social events.

Culture

The Hiscox culture is underpinned by a set of core values that determine the standard of behaviour expected of employees. These core values – challenge convention, integrity, respect, courage, quality and excellence in execution – guide everything that Hiscox does in its business. By conducting its business with these core values in mind, the Group recognises that it is more likely to achieve business success and create value for its shareholders. Hiscox strives for the highest standards of corporate governance while being in essence a non-bureaucratic organisation. An effective and firm system of internal controls ensures that risks are managed within acceptable limits, but not at the expense of innovation or speed of response. The Group believes that it has got this balance right and that it is one of its greatest strengths. The Group's policies ensure that it continues to follow a best practice approach to managing its people and remains a fair and professional employer. In the unlikely event of an employee having a material concern relating to the operations of the business, a whistleblowing policy explains to staff how they can confidentially raise their misgivings.

Hiscox also subscribes to Public Concern at Work, which provides free legal advice to any employee with a concern about possible danger or malpractice in the workplace.

In the community

In total, Hiscox donated £616,572 to charities in 2007. As the Group expands throughout the world, it aims to recruit local staff wherever possible to help develop a rapport with the local community and make a direct contribution to the local economy.

The Group has maintained its involvement in its local communities with the strong support of its employees. In Bermuda, Hiscox supports the Bermuda Sunshine League which is a transitional living facility for children removed from unstable living environments and gives employees the opportunity to contribute their time and effort to children who require adult role models and a semblance of stability. Hiscox is a member of the Lloyd's Community programme, which supports local initiatives concerning education, training, enterprise and regeneration. In London for example, the Reading Partners scheme has continued, through which staff assist pupils at the Elizabeth Selby Infants School in Tower Hamlets. Employees also mentor students at Morpeth School in Tower Hamlets.

Supporting the arts

The Group continues to support the Bermuda Masterworks Foundation, which aims to repatriate artworks by Bermudian artists or featuring Bermuda landscapes/seascapes. Hiscox Art Projects, a contemporary exhibition space situated in the London office with free entry to the public, continues to provide artists with an opportunity to exhibit their talents.

The Hiscox Foundation

The Hiscox Foundation, a charity funded by an annual donation from Hiscox, has been set up to give donations to deserving causes. It gives priority to any charity in which a member of staff is involved with the aim of encouraging and developing such activity.

Hiscox staff also continued their six year long support of the Richard House Hospice, raising over £30,000 through various initiatives during 2007. One such initiative was the Ardèche challenge, where 24 people took part in a canoe race through the Ardèche Gorge

in South Eastern France raising over £12,000 for the charity. Money was also raised through book sales and a Christmas raffle.

In the environment

The way customers conduct their business is of paramount importance to the Group. Hiscox's approach to underwriting their risks will take into account customers' attitudes to all aspects of their business, including care of the environment.

As part of its approach, Hiscox has joined Climatewise, an insurance industry initiative which aims to reduce the economy's and society's long-term risk from climate change. Hiscox is developing a strategy to support the principles of Climatewise and is encouraged by the actions taken by Lloyd's to assist the market to meet the majority of the principles.

The Group's direct environmental impact is mainly from the energy it uses and the emissions and waste it generates from its premises. In accordance with the Group's Environmental Policy, consumables are recycled and reused wherever possible. The Group is taking steps to reduce the amount of raw materials used in business processes and by staff, particularly through the extensive use of computerisation and communications technology. During 2007, Hiscox upgraded its IT data centre and reduced the number of servers required by the Group. Programmes for recycling batteries, mobile phones, lamps and CDs continued during the year.

A Hiscox representative attends meetings organised by the City of London Corporation to keep abreast of environmental best practice and exchange ideas with other like-minded companies.

Executive Directors



Robert Ralph Scrymgeour Hiscox
Chairman
(Aged 65)

Robert Hiscox joined Hiscox in 1965 and has been Chairman of the main holding company of Hiscox since its incorporation in 1973. He was Deputy Chairman of Lloyd's between 1993 and 1995. He is a Non Executive Director of Grainger Trust plc.



Bronislaw Edmund Masojada
Chief Executive
(Aged 46)

Bronek Masojada joined Hiscox in 1993. From 1989 to 1993 he was employed by McKinsey and Co. Bronek served as a Deputy Chairman of Lloyd's from 2001 to 2007 and as Chairman of the Lloyd's Underwriting Agents Association from 1998 to 2001. He was a Non Executive Director of Ins-sure Holdings Limited from 2002 to 2006 and is a past president of The Insurance Institute of London. He is Chairman of the Lloyd's Tercentenary Foundation, a charity which supports research in areas of interest to the insurance industry.



Stuart John Bridges
Group Finance Director
(Aged 47)

Stuart Bridges joined Hiscox in 1999. He is a chartered accountant and has held posts in various financial service companies in the UK and US, including Henderson Global Investors. He was a member of the Financial Reporting Council's review group on The Turnbull Guidance on Internal Control.



Robert Simon Childs
Chief Underwriting Officer
Chief Executive Officer of Hiscox Bermuda and
Chairman of Hiscox USA
(Aged 56)

Robert Childs joined Hiscox in 1986, served as the Active Underwriter of the Hiscox Lloyd's Syndicate 33 between 1993 and 2005, and is the Group's Chief Underwriting Officer. Robert was Chairman of the Lloyd's Market Association from January 2003 to May 2005.

Independent
Non Executive
Directors



Carol Franklin Engler
Non Executive Director
(Aged 56) △○□

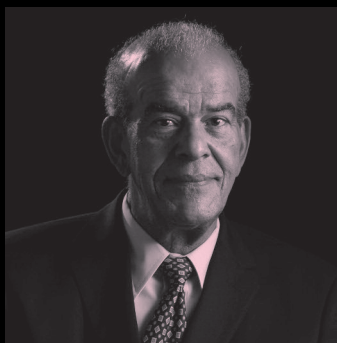
Carol Franklin Engler joined Hiscox in 1999. She is the Ombudsman for the Swiss telecommunication industry and the Executive Chairman of Forests for Friends Ltd and The Tree Partner Company in Switzerland. Carol was the Chief Executive Officer of the World Wide Fund for Nature in Switzerland from 1999 to 2002. From 1979 to 1999 she was employed by Swiss Re in a variety of roles including Head of the Aviation Department and Head of Human Resources.

**Independent
Non Executive
Directors**
continued



Daniel Maurice Healy
Non Executive Director and
Chairman of the Audit Committee
(Aged 65) ▲○□

Daniel Healy joined Hiscox in 2006. He was appointed Executive Vice President and Chief Financial Officer of North Fork Bancorporation in 1992 and a member of its Board of Directors in 2000. He was a partner with KPMG LLP before joining North Fork. He was the Managing Partner of the San José, California and Long Island, New York offices and held other positions in that firm during his tenure. He holds Board positions with KBW, Inc. and Harlem RBI, a not for profit organisation. He is also a senior adviser to Permira Advisers LLC an international private equity firm.



Dr James Austin Charles King
Non Executive Director and
Chairman of the Conflict Committee
(Aged 69) ▲●□

Dr James King joined Hiscox in 2006. He chairs Keytech Limited, The Bermuda Telephone Company Ltd, the Argus Group of Companies, Grotto Bay Properties Ltd and the Establishment Investment Trust, a UK listed company. He was chairman of the Bank of N.T. Butterfield & Son Limited until 19 April 2007. He is a Trustee of the Bermuda Institute of Ocean Sciences and a Director of Castle Harbour Limited. Dr King is a fellow of the Royal College of Surgeons, Canada and the American College of Surgeons.



Sir Mervyn Pedelty
Senior Independent Director and
Chairman of the Remuneration and Nomination Committee
(Aged 59) ○■

Sir Mervyn Pedelty joined Hiscox in 2005. He was previously the Chief Executive and an Executive Director of The Co-operative Bank plc (from 1997 until his retirement in 2004) and also of Co-operative Financial Services Limited and the Co-operative Insurance Society Limited (from 2002 to 2004). He was a Director of the Association of British Insurers (from 2002 to 2004) and is a former Council Member of the British Bankers' Association. Sir Mervyn is a Chartered Accountant and a Chartered Banker. His other current appointments include: independent Director of Friends Provident plc, Chairman of the FTSE4 Good Policy Committee, a Director of Performances Birmingham Limited and a Senior Adviser to Permira Advisers LLP.



Andrea Sarah Rosen
Non Executive Director
(Aged 53) ▲○□

Andrea Rosen joined Hiscox in 2006. She was appointed as a Director of Alberta Investment Management Corporation in October 2007 and is a Director of Emera Inc. She was previously Vice Chair of TD Financial Group and President of the TD Canada Trust from 2002 to 2005. Prior to this she held various positions within the TD Financial Group from 1994 to 2002, including Executive Vice President of TD Commercial Banking and Vice Chair of TD Securities. She was Vice President of Varsity Corporation from 1991 to 1994 and held various positions with Wood Gundy Inc. from 1981 to 1990.



Dirk Arie Stuurop
Non Executive Director
(Aged 59) ▲○□

Dirk Stuurop joined Hiscox in 2006. He is managing partner of Lighthouse Holdings LLC. In 2004 he was appointed Vice Chairman of the Board of RAM Holdings Limited, a Bermudian domiciled financial guaranty reinsurance operation. From 1999 to 2006, Dirk was President of Stuurop & Company, a privately owned firm providing strategic advice to executive managements and boards of directors. In 1999 he retired as Chairman of Global Financial Institutions at Merrill Lynch where he worked from 1982. He served as Chairman of Worldinsure Ltd, from 2000 to 2002 and as Senior Executive Director to Banc of America Securities in 2003.

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Robin Mehta

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▲
Member of the Audit
Committee
○
Member of the Conflict
Committee
□
Member of the
Remuneration and
Nomination Committee

Chairman of Committee
is highlighted in solid

Overview and basis of reporting

Hiscox Ltd ('the Company') is a Bermudian domiciled holding company for the Group. The Company is listed on the London Stock Exchange's main market for listed securities. The corporate governance framework for companies registered in Bermuda is established by the Company's constitution together with Companies Act legislation.

During 2007, and up to the date of this report and accounts, the Group has complied with the provisions of the Combined Code in all material respects.

The Board of Directors

The Board comprises four Executive Directors and six independent Non Executive Directors, including a Senior Independent Director. Biographical details for each member of the Board are provided on pages 50 to 51.

The roles and activities of the Chairman and Chief Executive are distinct and separate. The Chairman is responsible for running an effective Board and overall strategy, and the Chief Executive has responsibility for running the Group's business.

In accordance with the Company's Bye-Laws all Directors are required to submit themselves for re-election at least every three years.

All Directors are entitled to seek independent professional advice at the Company's expense. A copy of the advice is provided to the Company Secretary who will circulate it to all Directors. No such advice was sought during the year.

The Board meets at least four times a year and operates within established Terms of Reference. It is supplied with appropriate and timely information to enable it to review business strategy, trading performance, business risks and opportunities. The Board of Hiscox Ltd met five times during the year.

The Board considers all the Non Executive Directors to be independent within the meaning of the Combined Code as there are no relationships or circumstances which would interfere with the exercise of their independent judgement.

The Board's Terms of Reference include a Schedule of Matters Reserved for Board Decision, a copy of which can be found on the Group's website: www.hiscox.com.

The Board retains ultimate authority for high level strategic and management decisions including: setting Group strategy, approving significant mergers or acquisitions, approving the financial statements, declaration of the interim dividend and recommendation of the final dividend, approving Group business plans and budgets, approving major new areas of business, approving capital raising, approving any bonus or rights issues of share capital, setting Group investment guidelines, approving the Directors' remuneration, approving significant expenditure or projects, and approving the issue of share options. The Board has, however, authorised the boards of the trading entities and business divisions to manage their respective operational affairs, to the extent that Company Board level approval is not required.

The Board's committees

The Board has appointed and authorised a number of committees to manage aspects of the Group's affairs. Each committee operates within established written terms of reference and each committee Chairman reports directly to the Board.

The Group Executive Committee

The Group Executive Committee, comprised of the Executive Directors, meets monthly to raise and discuss topics such as Group strategy (subject always to Board approval), approval of senior appointments and remuneration (other than Board appointments), management of the Group's trading performance, mergers and acquisitions (which are not significant to the Group), significant issues raised by the London and International executive committees and approval of exceptional spend within the limits established by the Board. The London Executive Committee considers day-to-day issues arising from the Group's UK and mainland Europe businesses. The International Executive Committee considers issues arising from the Group's Bermuda, Guernsey and US businesses.

The Audit Committee

The Audit Committee of Hiscox Ltd comprises Daniel Healy as Chairman of the Committee together with Carol Franklin Engler, Dirk Stuurop, Andrea Rosen and Dr James King.

The Audit Committee meets at least four times a year to assist the Board on matters of financial reporting, risk management and internal control. The Audit Committee monitors the scope, results and cost effectiveness of the internal and external audit functions, the independence and objectivity of the external auditors, and the nature and extent of non-audit work undertaken by the external auditors together with the level of related fees. The internal and external auditors have unrestricted access to the Audit Committee. All non-audit work undertaken by the Group's external auditors with fees greater than £50,000 must be pre-approved by the Audit Committee. KPMG has confirmed to the Audit Committee that in its opinion it remains independent. The Committee is satisfied that this is the case.

The Remuneration and Nomination Committee

The Remuneration and Nomination Committee is chaired by Sir Mervyn Pedelty and comprises Carol Franklin Engler, Dirk Stuurop, Daniel Healy, Andrea Rosen and Dr James King. It meets a minimum of two times a year to deal with appointments to the Board and to recommend a framework of executive remuneration. The Directors' remuneration report is presented on pages 54 to 59.

The Conflicts Committee

The Group has a Conflicts Committee which is comprised of independent Non Executive Directors from within the Group, and chaired by Dr James King. It meets as and when required. Conflicts of interest may arise from time to time because Syndicate 33 and Cougar Syndicate are managed by a Hiscox-owned Lloyd's Managing Agency. 27.4% of the Names on Syndicate 33 are third parties with 72.6% of Syndicate 33 owned by a Hiscox Group company. 100% of Cougar Syndicate is owned by third parties. The Conflicts Committee serves to protect the interests of the third party Syndicate Names. Should such a potential conflict of interest arise, there is a formal procedure to refer the matter to this Committee.

Risk Committees

There are a number of committees within the Group which have been established to oversee key risk areas, including committees covering reinsurance credit risk, liquidity risk, broker credit risk, business continuity risk and investment risk. These committees are comprised of Directors within the Group companies and relevant senior employees.

Performance evaluation

During the year, the Chairman led a review of the performance of the Board as a whole. The Non Executive Directors met with the Chairman to discuss a wide range of issues, including the performance of the Executive Directors of the Board and senior management. In addition the Non Executives met without the Chairman and the Executive Directors during the year. The performance of the Executive Directors and the Chairman was discussed. No major issues regarding the performance of the Board were raised in these discussions.

The Chief Executive held one-to-one meetings with each of the Executive Directors to discuss their performance over the year and to set targets for the year ahead.

Shareholder communications

The Executive Directors communicate and meet directly with shareholders and analysts throughout each year, and do not limit this to the period following the release of financial results or other significant announcements.

All Directors endeavour to attend the Annual General Meeting.

The Company commissions independent research on feedback from shareholders and analysts on a regular basis following the Company's results announcements. This research together with the analysts' research notes are copied to the Non Executive Directors in full. The Chairman attends a number of meetings with shareholders as well as speaking at the analysts' presentations. In addition, any specific items covered in letters received from major shareholders are reported to the Board. Major shareholders are invited to request meetings with the Senior Independent Director and/or the other Non Executive Directors, and they have been given the contact details of the Senior Independent Director.

An alert service is available on www.hiscox.com to notify any stakeholder of new stock exchange announcements.

Accountability and internal control

The Directors are responsible for maintaining a sound system of internal control to safeguard the investment made by shareholders and the Company's assets, and for reviewing its effectiveness.

The risk management systems are set out in detail in the Risk management report on pages 44 to 47.

The Board has reviewed the effectiveness of internal controls during 2007, including financial, operational and compliance controls. The Board confirms there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Company, which has been in place throughout the year and up to the date of approval of the Annual Report and Accounts and accords with the guidance in the document 'Internal Control: Guidance for Directors on the Combined Code'. The head of each business area is responsible for implementing the risk management programme in their area of operations. The Risk team collates risk management information and the Head of Risk works with the risk committees to monitor significant risks and movements, and review the relevant internal controls.

The Group also has an Internal Audit function which has direct access to the Audit Committee and reports to each meeting.

The Board acknowledges that it is neither possible, nor desirable, to eliminate risk completely. The system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss. The constant aim is to be fully aware of the risks to which the business is exposed and to manage these risks to acceptable levels.

Meetings and attendance table

Director	Ltd Board	Audit Committee	Remuneration and Nomination Committee
	Attended	Attended	Attended
RRS Hiscox	5/5	n/a	n/a
BE Masojada	5/5	n/a	n/a
SJ Bridges	5/5	n/a	n/a
RS Childs	5/5	n/a	n/a
C Franklin Engler	4/5	3/4	1/2
DM Healy	5/5	4/4	2/2
Dr J King	5/5	4/4	2/2
Sir Mervyn Pedelty	4/5	n/a	2/2
AS Rosen	5/5	4/4	2/2
DA Stuurop	4/5	3/4	2/2

Directors' remuneration report

This report sets out the remuneration policy for the Group's senior executives. This policy is consistent with the overall reward approach across the Group. The sections of this report entitled 'Remuneration of Executive Directors', 'Annual cash incentives', 'Share incentive schemes' and 'Pensions' have been audited by KPMG. The remainder of the report is unaudited.

Remuneration and Nomination Committee

The Remuneration and Nomination Committee meets at least twice a year. Details of the members can be found on pages 50 to 51.

The Remuneration and Nomination Committee makes recommendations to the Board on the overall framework and cost of remuneration for Hiscox and determines the specific remuneration packages for the Executive Directors.

None of the Committee has any personal financial interest (other than as shareholders) or conflicts of interest arising from cross-directorships or day-to-day involvement in running the business. No Director plays any part in any discussion about his or her own remuneration.

Advice on specific topics is provided by Towers Perrin Remuneration Consultants.

Remuneration policy

The remuneration philosophy within Hiscox is to provide rewards which attract and retain quality staff and encourage and reward superior performance.

The Remuneration and Nomination Committee believes that pay should be competitive but that superior reward should be driven by superior business results.

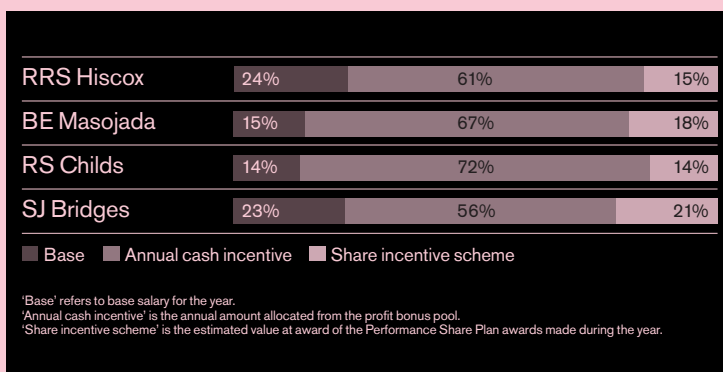
Remuneration of Executive Directors

The remuneration received by each person who served as an Executive Director during the year is set out in the table below.

Remuneration elements

There are four main elements of the remuneration packages in Hiscox: base salary and benefits, annual cash incentives (bonuses), share incentives and pensions.

The proportions of salary, cash incentives and share incentive schemes in the overall reward for Executive Directors are detailed below:



Base salary and benefits

Base salaries within the Group are reviewed annually. The Remuneration and Nomination Committee considers the overall budget and approach for the review, taking into account economic and operational conditions. Individual salaries are then reviewed using the Watson Wyatt Financial Services Salary Survey as a benchmark. Individual skills, experience and performance are also taken into account when setting salaries.

When approving Executive Director's pay increases the Remuneration and Nomination Committee takes into account rates of inflation, Watson Wyatt data, other publicly available reports and comparable companies' pay structures as appropriate.

Watson Wyatt is an independent remuneration consultant who provides ad hoc information to the Remuneration and Nomination Committee and does not provide any other services to the Company.

Annual cash incentives (bonuses)

Hiscox's remuneration policy is underpinned by the belief that a significant portion of total remuneration should be attained through incentive awards, therefore linking rewards directly with performance. The expectation is that successful performance should enable individuals to achieve upper quartile total remuneration. The table on page 55 shows the payment of annual cash incentives to Executive Directors over the past ten years and illustrates the alignment between business performance and reward.

Incentives are awarded by setting an overall bonus pool and then allocating individual awards from that pool based on personal performance ratings. Two bonus pools are operated: the Personal Performance Bonus (PPB) and the Profit Related Bonus (PRB). The PPB is only available to junior and mid-level staff and is based on individual performance. It is designed to ensure that staff in these roles continue to be motivated to perform and the benefit is up to 10% of relevant salaries.

Remuneration of Executive Directors

	2007 Basic salary £000	2007 Benefits £000	2007 Bonus £000	2007 Total £000	2006 Basic salary £000	2006 Benefits £000	2006 Bonus £000	2006 Total £000
RRS Hiscox	297	2	750	1,049	268	17	600	885
BE Masojada	405	2	1,750	2,157	326	15	800	1,141
RS Childs	336	90	1,750	2,176	308	13	1,200	1,521
SJ Bridges	307	2	750	1,059	268	14	600	882

As from 1 January 2007, certain benefits were rolled into basic salary.

All employees, including Executive Directors, are eligible for the Profit Related Bonus. The PRB scheme is triggered when the business profits of the Group, based on the year's pre-tax operating result, exceed a Return on Equity (ROE) linked to the longer term rate of return ('Hurdle Rate'). The minimum Hurdle Rate has previously been set at a 10% pre-tax return on allocated equity with the bonus pool comprising 15% of profits in excess of that. Bonus pools are then calculated for each major business division based on the performance of that division against the Hurdle Rate of return for the division's allocated equity.

Once the overall bonus pool has been established, individual bonuses, including those for Executive Directors, are calculated based on the results of each business area and individual performance. The Remuneration and Nomination Committee determines the bonuses to be paid to the Executive Directors based on the performance of the Group and an assessment of individual performance. In this way, the bonus scheme aligns the interests of Executive Directors and employees with shareholders.

The payment of larger bonuses is deferred over a three-year period as follows.

Bonus of £50,000/\$100,000/ €75,000 and below	Entire bonus taken in cash in year one
Bonus above £50,000/\$100,000/ €75,000 and below £100,000/ \$200,000/€150,000	£50,000/\$100,000/€75,000 taken in cash in year one Remainder of bonus split 50% in year two, 50% in year three
Bonus above £100,000/\$200,000/ €150,000	50% of bonus taken in year one 25% taken in year two 25% taken in year three

Share ownership is encouraged amongst senior personnel by allowing the deferred element of the annual bonus to be used, without deferral, for:

- _____ payment of the exercise price on the exercise of share options;
- _____ payment of tax on the exercise of share options;
- _____ purchase of shares; and
- _____ payment of debt due on share purchases.

to further align employee interests with those of the shareholder.

The following share incentive schemes are operated by Hiscox: the Hiscox Approved Share Option Scheme, the Hiscox Unapproved Share Option Scheme (the 'Share Option Schemes'), the Performance Share Plan and a Save as You Earn (SAYE) scheme. Options and awards that were granted under the share incentive schemes established by Hiscox plc were rolled over into Hiscox Ltd shares at the time of the re-domicile. Hiscox Ltd has established share incentive schemes which are substantially the same as those previously operated by Hiscox plc and since the re-domicile all options and awards have been granted under the Hiscox Ltd schemes.

Performance conditions

In order to ensure that these schemes are aligned with shareholders' interests, the Remuneration and Nomination Committee regularly reviews the terms and conditions of the grants, including the performance measure.

The Remuneration and Nomination Committee believes that using ROE as the long-term performance condition better aligns the interests of employees with shareholders because:

- _____ ROE captures the efficiency with which the Company is using shareholder funds to generate earnings, whereas EPS growth gives no indication of the level of return on the investment required to generate those additional earnings;
- _____ the Company operates in a highly cyclical business where earnings can fluctuate considerably, which can have a distorting effect on EPS growth. Where EPS is used as a performance condition this can introduce an element of luck as to when in the cycle share grants are made which can operate to the disadvantage of both employees and shareholders. The Remuneration and Nomination Committee believes that an average ROE performance requirement over the three-year period smoothes out the cyclical fluctuations in earnings and ensures that over any given period shareholders will receive a minimum return on equity before awards granted to employees will vest.

For the Special Awards (see below) and subsequent performance share awards ROE has been calculated as profit after tax and goodwill amortisation divided by shareholders' funds at the beginning of each year. The ROE for the option award granted in 2005 has been calculated as profit before tax and goodwill amortisation divided by shareholders' funds at the beginning of each year. The ROE will be calculated for each of the three financial years constituting the performance period and then averaged.

The performance conditions for each scheme are described below.

Share Option Schemes

Awards are made to Executive Directors, senior managers and other staff at the discretion of the Remuneration and Nomination Committee. No grants were made during 2007, or up until the date of this report and accounts.

The exercise of options granted since 22 June 2004 are subject to the following performance conditions:

- _____ an option will vest as to 100% of their shares if the Group's pre-tax ROE average is 10% over the three-year performance period (the 'maximum target');
- _____ an option will not vest at all unless the Group's pre-tax ROE average over the period equals or exceeds 8%, at which point the options will vest as to 40% of the shares (the 'minimum target');
- _____ an option will vest on a straight line basis if the Group's pre-tax ROE average is between the minimum target and the maximum target.

Executive Directors' cash incentives and ROE

	Pre-tax return on equity %	Average bonus as a percentage of salary %
1998	16	73
1999	0	0
2000	3	0
2001	(24)	0
2002	13	90
2003	30	202
2004	28	173
2005	19	54
2006	35	274
2007	36	372

Share incentive schemes

The Remuneration and Nomination Committee believes strongly in the value of employee participation in long-term share schemes in order

Performance Share Plan

Restricted share awards are made to Executive Directors, senior managers and all other staff under the Performance Share Plan at the discretion of the Remuneration and Nomination Committee. Awards under this plan were made in 2007 and the Remuneration and Nomination Committee has also agreed to make awards under this plan in 2008. Awards under this plan are subject to the same testing conditions that were applied to the special awards granted in 2006 (described below).

In 2005, following the Rights Issue, we received shareholder approval to grant special awards to individuals within the Company of over up to five million shares, of which a maximum of 20% were available for Executive Directors ('Special Award'). These awards vest after three years subject to the following performance conditions: 25% of the award vests if the Company achieves an average ROE of 10% post-tax over the three years and 100% vests if the average return exceeds 17.5% post-tax. Vesting will occur on a straight-line basis between these points.

Awards were granted of over 2,771,500 shares on 26 March 2007 and 52,000 shares on 2 October 2007 which were subject to the same testing performance conditions as the Special Awards, and it is also the current intention that future awards will be subject to those conditions.

The Remuneration and Nomination Committee has agreed the following changes to the Performance Share Plan:

- Dividends (or amounts equal to dividends) on shares granted under the Performance Share Plan (including in respect of the 2006 and 2007 grants) will roll up in the form of shares between the grant and vesting.
- At the end of the performance period the employee would have options over the proportion of the share grant which vests by reference to the satisfaction of the applicable performance target as well as over the number of shares representing the 'rolled up' dividends on those shares.
- After vesting but before exercise, the employee would then receive 'shadow dividends' (i.e. amounts equal to dividends paid) on the total number of shares remaining under option up to a maximum of 200,000 shares per employee. These amounts would be paid in cash, twice yearly, at the same time as dividends are paid to shareholders, until the option is exercised (which could be for up to a further seven years, when the option expires).

Above 200,000 shares under option, the dividends would be re-invested into shares within an employee benefit trust. Executive Directors, however, would have the entire dividend re-invested in shares within the trust.

The Remuneration and Nomination Committee believes that this change better aligns senior management with shareholders by focusing employees on ROE and dividends and therefore Total Shareholder Return. It also encourages employees to retain the shares which is consistent with our wish to create high levels of employee shareholding.

Details of this change will be included in the Notice of the Annual General Meeting.

Save as You Earn

The sharesave scheme and international sharesave scheme are offered to all employees and currently have a 53% participation.

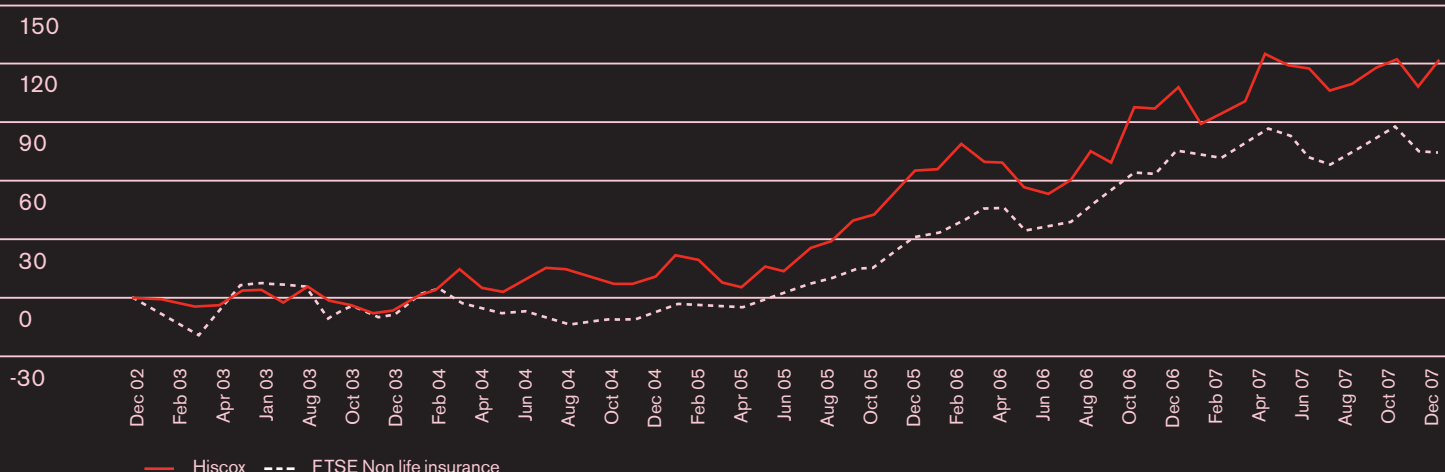
The table at the end of the Remuneration report details Directors' interests in the long-term incentive plans.

Pensions

The final salary pension scheme (the Scheme) was closed for future accrual on 31 December 2006. All active members, including SJ Bridges and BE Masojada, transferred to the Group Personal Pension arrangement (the GPP), a defined contribution arrangement on 1 January 2007. As compensation for the closure of the Scheme, Transitional Allowances were made. The amount was fixed in April 2007, payable over three years and could be taken as cash or paid into the GPP. In 2007 the payment made to BE Masojada was £33,600 and to SJ Bridges was £39,800. RRS Hiscox, a pensioner member, retired on 3 January 2003 and RS Childs who left the Scheme on 31 December 2005, is an existing deferred member.

The pension entitlement from the Scheme is shown opposite. This is the benefit that would be paid annually on retirement, based on service to date of deferment and then increased to 31 December 2007. The increase in the accrued pension for the year excludes any increase for inflation. However, figures for RRS Hiscox are based on his actual pension in payment. The transfer values have been calculated on the basis of actuarial advice in accordance with version 9 Actuarial Guidance Note GN 11: Retirement Benefit Schemes – Transfer Values.

Total shareholder return (%)



Executive Directors' service contracts

Directors' service contracts are on a rolling basis and the unexpired term shown in the following table is therefore the same as the notice period. The Remuneration and Nomination Committee believes that these notice periods provide an appropriate balance and provide sufficient protection to the Company, having regard to prevailing market conditions and current practice amongst public companies. None of the contracts include any provision for compensation payments on early termination.

Service contract table

Director	Effective date of Hiscox Ltd contract	Unexpired term and notice period
RRS Hiscox	12 Dec 2006	12 months
BE Masojada	12 Dec 2006	6 months
RS Childs	12 Dec 2006	6 months
SJ Bridges	12 Dec 2006	6 months
C Franklin Engler	11 Oct 2006	3 months
D Healy	11 Oct 2006	3 months
Dr J King	11 Oct 2006	3 months
Sir Mervyn Pedelty	11 Oct 2006	3 months
A Rosen	11 Oct 2006	3 months
D Stuurop	11 Oct 2006	3 months

External Non Executive Directorships

No external appointment may be accepted by an Executive Director where such appointment may give rise to a conflict of interest. The consent of the Chairman is required in any event. During the year RRS Hiscox was a Non Executive Director of Grainger Trust plc and was paid £35,000 for his services and AGICM Ltd for which he received no fees. BE Masojada was Deputy Chairman of Lloyd's until 31 January 2007 and the fees were remitted to the Group for his service. Neither SJ Bridges nor RS Childs held Non Executive Director positions during the year.

Remuneration of Non Executive Directors

Non Executive Directors receive an annual fee in respect of their Board appointments together with additional compensation for their further duties in relation to Board committees. All amounts are denominated in US Dollars. The structure of the fees paid are detailed below:

The fees in relation to Hiscox Ltd for the year were:

	Hiscox Ltd Board \$000	Committees \$000	Total 2007 \$000	Total 2006 \$000
C Franklin Engler	75	25	100	6
D Healy	75	35	110	24
Dr J King	75	30	105	23
Sir Mervyn Pedelty	75	50*	125	10
A Rosen	75	25	100	22
D Stuurop	75	25	100	22

The Pound Sterling equivalent of the total was £321,000 (2006: £55,000).

*Sir Mervyn Pedelty receives £10,000 for serving on a UK subsidiary board.

The comparative amounts for the prior year reflect the fees paid in relation for the period from appointment to 31 December 2006. The fees are reviewed annually but not necessarily increased. Fees are set at a level to attract individuals with a broad range of relevant skills and experience. The Non Executive Directors receive no other benefits.

Pensions

	Increase in accrued pension during the year £000	Total accrued annual pension at 31 Dec 07 £000	Transfer value of increase in accrued pension £000	Transfer value of accrued pension at 1 Jan 07 £000	Transfer value of accrued pension at 31 Dec 07 £000	Increase/(decrease) in transfer value of accrued benefit during the year £000
RRS Hiscox	9	195	43	4,213	4,301	88
BE Masojada	2	36	4	479	533	54
RS Childs	9	209	30	3,867	4,258	391
SJ Bridges	1	28	2	337	378	41

This table relates to the closed final salary pension scheme.

Share options

The conditions of exercise of the Approved and Unapproved share options are described on pages 55 and 56.

	Number of options at 1 January 2007	Number of options granted	Number of options lapsed	Number of options exercised	Number of options at 31 December 2007	Exercise price £	Market price at date of exercise £	Date from which exercisable	Expiry date
RRS Hiscox	90,237	—	—	—	90,237	1.574	—	20 Oct 01	19 Oct 08
	56,396	—	—	—	56,396	1.020	—	15 Jun 03	14 Jun 10
	56,398	—	—	—	56,398	1.755	—	03 May 04	02 May 11
	51,526	—	—	—	51,526	1.465	—	02 Apr 06	01 Apr 13
	51,526	—	—	—	51,526	1.514	—	13 Jul 07	12 Jul 14
	51,526	—	—	—	51,526	1.499	—	06 Apr 08	05 Apr 15
	357,609	—	—	—	357,609				
BE Masojada	90,237	—	—	—	90,237	1.574	—	20 Oct 01	19 Oct 08
	112,797	—	—	—	112,797	1.281	—	13 Oct 02	12 Oct 09
	169,195	—	—	—	169,195	1.020	—	15 Jun 03	14 Jun 10
	78,958	—	—	—	78,958	1.755	—	03 May 04	02 May 11
	140,997	—	—	—	140,997	0.806	—	27 Sep 04	26 Sep 11
	206,104	—	—	—	206,104	1.252	—	19 Nov 05	18 Nov 12
	206,104	—	—	—	206,104	1.465	—	02 Apr 06	01 Apr 13
	206,104	—	—	—	206,104	1.514	—	13 Jul 07	12 Jul 14
	206,104	—	—	—	206,104	1.499	—	06 Apr 08	05 Apr 15
1,416,600	—	—	—	1,416,600					
RS Childs	90,238	—	—	—	90,238	1.574	—	20 Oct 01	19 Oct 08
	112,797	—	—	—	112,797	1.281	—	13 Oct 02	12 Oct 09
	169,197	—	—	(169,197)	—	1.020	3.01	15 Jun 03	14 Jun 10
	78,958	—	—	—	78,958	1.755	—	03 May 04	02 May 11
	140,997	—	—	(140,997)	—	0.806	3.01	27 Sep 04	26 Sep 11
	206,104	—	—	—	206,104	1.252	—	19 Nov 05	18 Nov 12
	206,104	—	—	—	206,104	1.465	—	02 Apr 06	01 Apr 13
	206,103	—	—	—	206,103	1.514	—	13 Jul 07	12 Jul 14
	206,104	—	—	—	206,104	1.499	—	06 Apr 08	05 Apr 15
1,416,602	—	—	(310,194)	1,106,408					
SJ Bridges	84,597	—	—	(22,559)	62,038	1.281	3.01	13 Oct 02	12 Oct 09
	112,797	—	—	(1,073)	111,724	1.020	3.01	15 Jun 03	14 Jun 10
	56,398	—	—	—	56,398	1.755	—	03 May 04	02 May 11
	140,997	—	—	(100,000)	40,997	0.806	3.01	27 Sep 04	26 Sep 11
	180,341	—	—	—	180,341	1.252	—	19 Nov 05	18 Nov 12
	154,578	—	—	—	154,578	1.465	—	02 Apr 06	01 Apr 13
	154,578	—	—	—	154,578	1.514	—	13 Jul 07	12 Jul 14
	154,578	—	—	—	154,578	1.499	—	06 Apr 08	05 Apr 15
1,038,864	—	—	(123,632)	915,232					
Other employees	127,452	—	—	(127,452)	—	1.702	2.60-3.01	17 Dec 00	16 Dec 07
	317,948	—	—	(72,057)	245,891	1.574	2.61-3.01	20 Oct 01	19 Oct 08
	348,523	—	—	(178,208)	170,315	1.281	2.64-3.01	13 Oct 02	12 Oct 09
	728,240	—	—	(274,521)	453,719	1.020	2.60-3.01	15 Jun 03	14 Jun 10
	118,436	—	—	(118,436)	—	1.001	2.64-3.01	09 Nov 03	08 Nov 10
	95,039	—	—	—	95,039	1.685	—	14 Feb 04	13 Feb 11
	491,768	—	—	(140,990)	350,778	1.755	2.62-3.01	03 May 04	02 May 11
	947,487	—	—	(320,190)	627,297	0.806	2.60-2.97	27 Sep 04	26 Sep 11
	1,455,371	—	—	(448,272)	1,007,099	1.252	2.62-2.97	19 Nov 05	18 Nov 12
	1,714,800	—	—	(662,102)	1,052,698	1.465	2.62-2.91	02 Apr 06	01 Apr 13
	2,308,336	—	—	(530,708)	1,777,628	1.514	2.62-3.01	13 Jul 07	12 Jul 14
	2,457,753	—	(103,052)	(121,083)	2,233,618	1.499	2.67-3.01	06 Apr 08	05 Apr 15
11,111,153	—	(103,052)	(2,994,019)	8,014,082					
Total	15,340,828	—	(103,052)	(3,427,845)	11,809,931				

Share options

The interests of the Directors and employees under the UK and International Sharesave Schemes of the Group are set out below:

	Number of options at 1 January 2007	Number of options granted	Number of options lapsed	Number of options exercised	Number of options at 31 December 2007	Exercise price £	Market price at date of exercise £	Date from which exercisable	Expiry date
UK Sharesave Scheme									
RRS Hiscox	5,932	–	–	–	5,932	1,576	–	01 Dec 08	31 May 09
BE Masojada	7,168	–	–	(7,168)	–	1,322	2.61	01 Dec 07	31 May 08
	–	4,343	–	–	4,343	2,210	–	01 Dec 10	31 May 11
RS Childs	7,544	–	–	(7,544)	–	1,223	2.80	01 Dec 06	31 May 07
SJ Bridges	–	4,256	–	–	4,256	2,220	–	01 May 10	31 Oct 10
Other employees	84,328	–	–	(84,328)	–	1,223	2.64-2.83	01 Dec 06	31 May 07
	525,550	–	(7,510)	(470,450)	47,590	1,322	2.63-2.91	01 Dec 07	31 May 08
	317,903	–	(40,931)	(9,837)	267,135	1,576	2.67-2.89	01 Dec 08	31 May 09
	–	436,125	(49,455)	(1,530)	385,140	2,220	2.61-2.74	01 May 10	31 Oct 10
	–	410,609	(7,088)	–	403,521	2,210	–	01 Dec 10	31 May 11
	948,425	855,333	(104,984)	(580,857)	1,117,917				
International Sharesave Scheme									
RS Childs	–	4,147	–	–	4,147	2,220	–	01 May 10	31 Oct 10
Other employees	8,136	–	–	(8,136)	–	1,223	2.99	01 Dec 06	31 May 07
	24,021	–	(3,709)	(5,729)	14,583	1,322	2.64	01 Dec 07	31 May 08
	37,868	–	(3,243)	–	34,625	1,576	–	01 Dec 08	31 May 09
	–	179,720	(3,451)	–	176,269	2,220	–	01 May 10	31 Oct 10
	–	7,363	–	–	7,363	2,220	–	01 Jul 10	31 Dec 10
	–	63,965	–	–	63,965	2,210	–	01 Dec 10	31 May 11
	70,025	255,195	(10,403)	(13,865)	300,952				

The aggregate gain made by the Directors on exercise of the above options (based on market price at date of exercise less the exercise price) was £929,045 (2006: £25,568). The market price of Hiscox Ltd shares at 31 December 2007 was 286.5p (2006: 280.25p). The highest and lowest prices of Hiscox shares during 2007 were 304.5p and 246.75p (2006: 280.25p and 193.75p).

Performance share plan

	Number of options at 1 January 2007	Number of awards granted	Number of awards lapsed	Number of awards exercised	Number of awards at 31 December 2007	Market price at date of exercise £	Date from which released
RRS Hiscox	100,000	–	–	–	100,000	–	12 Jan 09
	–	80,000	–	–	80,000	–	26 Mar 10
BE Masojada	260,000	–	–	–	260,000	–	12 Jan 09
	–	200,000	–	–	200,000	–	26 Mar 10
RS Childs	250,000	–	–	–	250,000	–	12 Jan 09
	–	150,000	–	–	150,000	–	26 Mar 10
SJ Bridges	215,000	–	–	–	215,000	–	12 Jan 09
	–	120,000	–	–	120,000	–	26 Mar 10
Other employees	3,383	–	–	(3,383)	–	2.58	01 Apr 05
	3,337,500	–	(197,500)	–	3,140,000	–	12 Jan 09
	25,000	–	–	–	25,000	–	13 Mar 09
	190,000	–	(20,000)	–	170,000	–	05 Oct 09
	–	2,221,500	(95,000)	–	2,126,500	–	26 Mar 10
	–	52,000	–	–	52,000	–	02 Oct 10
Total	4,380,883	2,823,500	(312,500)	(3,383)	6,888,500		

By order of the Board

Andrea Rosen

Acting Chairman of the Remuneration and Nomination Committee

Wessex House, 45 Reid Street, Hamilton HM 12, Bermuda

3 March 2008

The Directors have pleasure in submitting their Annual Report and financial statements for the year ended 31 December 2007.

Principal activity and business review

The Company is a holding company for subsidiaries involved in the business of insurance in Bermuda, the US, the UK and Europe.

An analysis of the development and performance of the business can be found within the Chief Executive's report on pages 8 to 15. A description of the major risks can be found in the Risk management section on pages 44 to 47.

Financial results

The Group achieved a pre-tax profit for the year of £237.2 million (2006: £201.1 million). Detailed results for the year are shown in the consolidated income statement on page 62, and also within the Group financial performance section on pages 39 to 41.

Going concern

After making enquiries, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the accounts.

Directors' responsibility

The Board is responsible for ensuring the maintenance of proper accounting records which disclose with reasonable accuracy the financial position of the company. It is required to ensure that the financial statements present a fair view for each financial period.

Dividends

An interim dividend of 4p (net) per share (2006: 3p (net)) was paid on 1 October 2007 by Hiscox Ltd in respect of the year ended 31 December 2007.

The Directors recommend the payment of a final dividend of 8p (net) per share (2006: 7p (net)). If approved this will be paid on 17 June 2008 to shareholders on the register at the close of business on 16 May 2008, provided that such dividend will not be paid to those shareholders who, prior to 16 May 2008, have made an election to participate in the Company's Dividend Access Plan if Hiscox plc subsequently declares a dividend for the purposes of such Dividend Access Plan prior to the payment date of such dividend.

If Hiscox Ltd has declared a dividend, those shareholders who have elected to participate in the Dividend Access Plan will receive payment of that dividend on 17 June 2008.

Directors' interests

Executive Directors

RRS Hiscox
BE Masojada
RS Childs
SJ Bridges

Non Executive Directors

C Franklin Engler
D Healy
Dr J King
Sir Mervyn Pedelty
A Rosen
D Stuurop

	31 December 2007 5p Ordinary Shares number of shares beneficial	31 December 2007 5p Ordinary Shares number of shares non-beneficial	31 December 2006 5p Ordinary Shares number of shares beneficial	31 December 2006 5p Ordinary Shares number of shares non-beneficial
RRS Hiscox	9,398,065	560,237	9,395,065	570,237
BE Masojada	2,710,070	–	2,702,902	–
RS Childs	1,703,805	–	1,386,067	–
SJ Bridges	592,053	–	468,421	–
C Franklin Engler	23,288	–	23,288	–
D Healy	55,000	–	50,000	–
Dr J King	–	–	–	–
Sir Mervyn Pedelty	18,000	–	–	–
A Rosen	–	–	–	–
D Stuurop	50,000	–	–	–

Share capital

Details of the structure of the Company's share capital and changes in the share capital during the year are disclosed in note 22 to the consolidated financial statements.

Directors

The names and details of the individuals who served as Directors of the Company during the year are set out on pages 50 to 51.

Robert Hiscox, Dr James King and Andrea Rosen retire by rotation in accordance with the Bye-Laws of the Company and they have each submitted themselves for re-election at the second Annual General Meeting of the Company.

A copy of the Company's Bye-Laws is available for inspection at the Company's registered office.

Political and charitable contributions

The Group made no political contributions during the year (2006: £nil).

Charitable donations totalled £616,572 (2006: £567,000) of which £550,000 (2006: £500,000) was donated to the Hiscox Foundation, a UK registered charity. The policy of the Hiscox Foundation is to assist and improve education, the arts and independent living for disabled and disadvantaged members of society. Further information concerning the Group's charitable activities is contained in the report on Corporate responsibility on pages 48 to 49.

Major interests in shares

The Company has been notified of the following shareholdings of 5% or more in the ordinary shares of the Company as at 3 March 2008:

	Number of shares	% of total
Invesco Limited	59,434,439	15.1
Jupiter Asset Management	25,210,566	6.4

Annual General Meeting

The notice of Annual General Meeting, to be held at the Elbow Beach Hotel, 60 South Shore Road, Paget PG04, Bermuda on 4 June 2008 at 10am (2pm BST), is contained in a separate circular to shareholders enclosed with this report.

By order of the Board

Robin Mehta
Secretary

Wessex House, 45 Reid Street, Hamilton HM 12, Bermuda
3 March 2008

Report of the independent registered public accounting firm to the Board of Directors and the shareholders of Hiscox Ltd

We have audited the accompanying consolidated financial statements of Hiscox Ltd ('the Company') on pages 62 to 105 which comprise the consolidated balance sheet as at 31 December 2007, and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

In addition to our audit of the consolidated financial statements, the Directors have engaged us to audit the information in the Directors' remuneration report that is described as having been audited, which the Directors have decided to prepare as if the Company were required to comply with the requirements of Schedule 7A to the UK Companies Act 1985.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and, under the terms of our engagement letter, to audit the part of the Directors' remuneration report that is described as having been audited.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements and the part of the Directors' remuneration report to be audited are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements and the part of the Directors' remuneration report to be audited. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements and the part of the Directors' remuneration report to be audited, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements and the part of the Directors' remuneration report to be audited in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements and the part of the Directors' remuneration report to be audited.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

In addition to our audit of the consolidated financial statements, the Directors have engaged us to review their Corporate Governance Statement as if the Company were required to comply with the Listing Rules of the Financial Services Authority in relation to those matters. We review whether the Corporate Governance Statement reflects the Company's compliance with the nine provisions of the 2006 Combined Code specified for our review by those rules, and we report if it does not. We are not required by the terms of our engagement to consider whether the Board's statements on internal control cover all risks and controls, or to form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We also read the other information contained in the Report and Accounts and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Opinion

In our opinion:

- the consolidated financial statements give a true and fair view of the consolidated financial position of the Company as at 31 December 2007, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards; and
- the part of the Directors' remuneration report which we were engaged to audit has been properly prepared in accordance with Schedule 7A to the UK Companies Act 1985, as if those requirements were to apply to the Company.

KPMG

Hamilton
Bermuda
3 March 2008

Consolidated income statement
For the year ended 31 December 2007

	Note	2007 £000	2006 £000
Income			
Gross premiums written	4	1,198,949	1,126,164
Outward reinsurance premiums		(224,039)	(150,767)
Net premiums written	4	974,910	975,397
<hr/>			
Gross premiums earned		1,179,444	1,033,585
Premiums ceded to reinsurers		(214,254)	(144,757)
Net premiums earned	4	965,190	888,828
Investment result	6	99,677	105,550
Other revenues	9	19,044	15,692
Revenue		1,083,911	1,010,070
Expenses			
Claims and claim adjustment expenses, net of reinsurance	24.2	(423,365)	(382,341)
Expenses for the acquisition of insurance contracts	8	(264,570)	(235,797)
Administration expenses		(76,813)	(76,533)
Other expenses	9	(73,868)	(104,943)
Total expenses		(838,616)	(799,614)
Results of operating activities		245,295	210,456
Finance costs	11	(8,177)	(9,404)
Share of profit of associates after tax	16	81	10
Profit before tax		237,199	201,062
Tax expense	26	(45,951)	(37,216)
Profit for the year (all attributable to equity shareholders of the Company)		191,248	163,846
<hr/>			
Earnings per share on profit attributable to equity shareholders of the Company			
Basic	29	48.4p	41.7p
Diluted	29	46.8p	40.5p

The notes on pages 66 to 105 are an integral part of these consolidated financial statements.

Consolidated balance sheet
At 31 December 2007

	Note	2007 £000	2006 £000
Assets			
Intangible assets	14	40,452	33,212
Property, plant and equipment	15	19,378	13,821
Investments in associates	16	1,502	28
Deferred acquisition costs	8	123,081	117,115
Financial assets carried at fair value	18	1,747,827	1,241,910
Loans and receivables including insurance receivables	19	385,222	446,272
Reinsurance assets	17, 24	280,088	302,772
Cash and cash equivalents	21	302,742	502,871
Total assets		2,900,292	2,658,001
Equity and liabilities			
Shareholders' equity			
Share capital	22	19,898	19,694
Share premium	22	4,955	—
Contributed surplus	22	398,834	442,425
Other reserves	23	(43,265)	(40,396)
Retained earnings	23	443,882	260,362
Total equity (all attributable to equity shareholders of the Company)		824,304	682,085
Employee retirement benefit obligations			
Deferred tax	28	—	3,801
Insurance liabilities	27	9,751	8,467
Financial liabilities carried at fair value	24	1,713,887	1,594,101
Current tax	18	91,764	93,929
Trade and other payables	25	24,711	20,793
		235,875	254,825
Total liabilities		2,075,988	1,975,916
Total equity and liabilities		2,900,292	2,658,001

The notes on pages 66 to 105 are an integral part of these consolidated financial statements.

The consolidated Group financial statements were approved by the Board of Directors on 3 March 2008 and signed on its behalf by:

RRS Hiscox
Chairman

SJ Bridges
Group Finance Director

Consolidated statement of changes in equity

	Note	Share capital £000	Share premium £000	Contributed surplus £000	Merger reserve £000	Currency translation reserve £000	Capital redemption reserve £000	Retained earnings £000	Total £000
Balance at 1 January 2006		19,570	401,365	–	4,723	822	33,244	118,289	578,013
Currency translation differences	13	–	–	–	–	(41,218)	–	–	(41,218)
Net expense recognised directly in equity		–	–	–	–	(41,218)	–	–	(41,218)
Profit for the year		–	–	–	–	–	–	163,846	163,846
Total recognised income/(expense) for year		–	–	–	–	(41,218)	–	163,846	122,628
Employee share options:									
Equity settled share based payments		–	–	–	–	–	–	5,238	5,238
Deferred tax release on share based payments		–	–	–	–	–	–	3,367	3,367
Proceeds from shares issued	22	124	2,829	264	–	–	–	–	3,217
Transfer on reverse acquisition	22	–	(404,194)	442,161	(4,723)	–	(33,244)	–	–
Change in own shares held in treasury		–	–	–	–	–	–	50	50
Dividends to external shareholders	30	–	–	–	–	–	–	(30,428)	(30,428)
Balance at 31 December 2006		19,694	–	442,425	–	(40,396)	–	260,362	682,085
Currency translation differences	13	–	–	–	–	(4,269)	–	–	(4,269)
Net investment hedge		–	–	–	–	1,400	–	–	1,400
Net expense recognised directly in equity		–	–	–	–	(2,869)	–	–	(2,869)
Profit for the year		–	–	–	–	–	–	191,248	191,248
Total recognised income/(expense) for year		–	–	–	–	(2,869)	–	191,248	188,379
Employee share options:									
Equity settled share based payments		–	–	–	–	–	–	5,689	5,689
Deferred tax transfer on share based payments		–	–	–	–	–	–	(2,074)	(2,074)
Proceeds from shares issued	22	204	4,955	–	–	–	–	–	5,159
Change in own shares held in treasury		–	–	–	–	–	–	(11,343)	(11,343)
Dividends to external shareholders	30	–	–	(43,591)	–	–	–	–	(43,591)
Balance at 31 December 2007		19,898	4,955	398,834	–	(43,265)	–	443,882	824,304

The notes on pages 66 to 105 are an integral part of these consolidated financial statements.

Consolidated cash flow statement
For the year ended 31 December 2007

	Note	2007 £000	2006 £000
Profit before tax		237,199	201,062
Adjustments for:			
Interest and equity dividend income		(90,205)	(70,243)
Interest expense		8,177	9,404
Net (gains)/losses on financial investments derivatives and borrowings		687	(9,422)
Non-cash movement in retirement benefit obligation		(3,801)	(12,876)
Depreciation	15	4,917	3,898
Charges in respect of share based payments	10	5,689	5,238
Other non-cash movements		(641)	1,551
Changes in operational assets and liabilities:			
Insurance and reinsurance contracts		133,951	45,426
Financial assets		(489,745)	1,311
Other assets and liabilities		31,112	(17,953)
Cash flows from operations		(162,660)	157,396
Interest received		85,435	68,644
Equity dividends received		4,770	1,599
Interest paid		(8,243)	(9,416)
Current tax paid		(42,823)	(36,363)
Net cash flows from operating activities		(123,521)	181,860
Cash outflow from the acquisition of subsidiary	31	(11,133)	–
Cash outflow from the sale of subsidiary	32	(936)	–
Cash outflow from acquisition of associates	16	(1,273)	–
Cash flows from the purchase of property, plant and equipment		(7,789)	(5,452)
Cash flows from the purchase of intangible assets	14	(2,500)	(300)
Net cash flows from investing activities		(23,631)	(5,752)
Proceeds from the issue of ordinary shares	22	5,159	3,217
Cash flows from the purchase of own shares including those arising on share buy-back programme	22	(11,343)	50
Dividends paid to Company's shareholders	30	(43,591)	(30,428)
Repayments of borrowings and financial liabilities		(272)	(14,334)
Net cash flows from financing activities		(50,047)	(41,495)
Net (decrease)/increase in cash and cash equivalents		(197,199)	134,613
Cash and cash equivalents at 1 January		502,871	413,759
Net increase in cash and cash equivalents		(197,199)	134,613
Effect of exchange rate fluctuations on cash and cash equivalents		(2,930)	(45,501)
Cash and cash equivalents at 31 December	21	302,742	502,871

The purchase, maturity and disposal of financial assets is part of the Group's insurance activities and is therefore classified as an operating cash flow. The purchase, maturity and disposal of derivative contracts is also classified as an operating cash flow.

Included within cash and cash equivalents held by the Group are balances totalling £53,336,000 (2006: £41,304,000) not available for immediate use by the Group outside of the Lloyd's Syndicate within which they are held.

The notes on pages 66 to 105 are an integral part of these consolidated financial statements.

1 General information

The Hiscox Group, which is headquartered in Hamilton, Bermuda, comprises Hiscox Ltd (the parent Company, referred to herein as the 'Company') and its subsidiaries (collectively, the 'Hiscox Group' or the 'Group'). For the period under review the Group provided insurance, reinsurance and investment management services to its clients worldwide. It has operations in Bermuda, the UK, Europe, and USA and employs over 800 people.

The Company is registered and domiciled in Bermuda and on 12 December 2006 its ordinary shares were listed on the London Stock Exchange. As such it is required to prepare financial information in accordance with the Bermuda Companies Act 1981, which permits the Group to prepare financial statements which comprise the consolidated income statement, the consolidated balance sheet, the consolidated statement of changes in equity, the consolidated cash flow statement and the related notes 1 to 36 in accordance with International Financial Reporting Standards ('IFRS'). Accordingly, the financial information has been prepared in accordance with Bermuda Law.

The consolidated financial statements for the year ended 31 December 2007 include all of the Group's subsidiary companies and the Group's interest in associates. All amounts relate to continuing operations.

The financial statements were approved for issue by the Board of Directors on 3 March 2008.

2 Significant accounting policies

The principal accounting policies applied in the preparation of these consolidated Group financial statements are set out below. The most critical individual components of these financial statements that involve the high degree of judgement or significant assumptions and estimations are identified at note 2.23.

2.1 Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards and in accordance with the provisions of the Bermuda Companies Act 1981.

Since 2002, the standards adopted by the International Accounting Standards Board (IASB) have been referred to as IFRS. The standards from prior years continue to bear the title 'International Accounting Standards' (IAS). Insofar as a particular standard is not explicitly referred to, the two terms are used in these financial statements synonymously. Compliance with IFRS includes the adoption of interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC).

In March 2004, the IASB issued IFRS 4 Insurance Contracts which specifies the financial reporting for insurance contracts by an insurer. The standard is only the first phase in the IASB's insurance contract project and as such is only a stepping stone to phase II, introducing limited improvements to accounting for insurance contracts. Accordingly, to the extent that IFRS 4 does not specify the recognition or measurement of insurance contracts, transactions reported in these consolidated financial statements have been prepared in accordance with another comprehensive body of accounting principles for insurance contracts, namely accounting principles generally accepted in the UK.

2.2 Basis of preparation

The financial statements are presented in Pounds Sterling and are rounded to the nearest thousand unless otherwise stated. They are compiled on a going concern basis and prepared on the historical cost basis except that pension scheme plan assets included in the measurement of the employee retirement benefit obligation, and

financial instruments including derivative instruments and financial liabilities at fair value through profit or loss, are measured at fair value. Employee retirement benefit obligations are determined using actuarial analysis. The balance sheet of the Group is presented in order of increasing liquidity.

The accounting policies have been applied consistently by all Group entities, to all periods presented, solely for the purpose of producing the consolidated Group financial statements.

The comparative amounts reported herein for the year ended 31 December 2006 have been extracted from the previously published report for that period, but have been adjusted for reclassification of certain minor overseas agency underwriting expenses and commissions from 'other expenses' and 'other revenues' to 'expenses for the acquisition of insurance contracts', and for the Group's revised presentation of segment information (note 4). The effect of the reclassification of the aforementioned expenses and commissions is to increase the previously reported 'expenses for the acquisition of insurance contracts' for the year ended 31 December 2006 by £9,948,000. Simultaneous identical reductions have been made in total to 'other expenses' and 'other revenues'. These presentational adjustments have no impact on the Group's previously reported result from operating activities, profit before tax or shareholders' equity. The Directors believe that the amended classification of these expenses and commissions provides a more appropriate presentation of their operating nature.

The Group elected to apply the transitional arrangements contained in IFRS 4 that permitted the disclosure of only five years of data in claims development tables, in the year ended 31 December 2005 which was the year of adoption. The number of years of data presented was increased from six in the prior year, to seven in the current financial year, and will be increased in each succeeding additional year up to a maximum of ten years if material outstanding claims exist for such periods.

As detailed in note 3 the Group adopted IFRS 7 Financial Instruments: Disclosures, and a corresponding amendment to IAS 1 Presentation of Financial Statements – Capital Disclosures on 1 January 2007. The adoption of IFRS 7 and the amendments to IAS 1 impacted the type and amount of disclosures made in these financial statements, but had no impact on the reported profits or financial position of the Group. In accordance with the transitional requirements of the standards, the Group has provided full comparative information.

The consolidated financial statements also reflect the early adoption of IFRS 8 Operating Segments from that date. IFRS 8 is a disclosure standard concerning the designation and presentation of operating segment information and therefore has no impact on the reported primary financial statements or financial position of the Group. Four IFRIC interpretations became effective for financial reporting purposes during the year under review, however their adoption has not resulted in any changes to the Group's stated accounting policies.

The Directors have considered recently published IFRS, new interpretations and amendments to existing standards that are mandatory to the Group's accounting periods commencing on or after 1 January 2008 and which have not been subject to early adoption. With the exception of recent revisions to IFRS 3 Business Combinations, which generally require transaction costs on business combinations to be accounted for separately as period costs by way of an immediate charge to the income statement rather than being capitalised as part of the overall cost of combination for goodwill purposes, the Directors' current assessment is that the adoption of these changes will necessitate minor presentational changes only.

2.3 Change of holding company in prior year

On 12 December 2006 Hiscox Ltd replaced Hiscox plc as the Group's holding company by way of a share for share exchange.

2 Significant accounting policies continued

2.3 Change of holding company in prior year continued

Hiscox Ltd was incorporated under the laws of Bermuda on 6 September 2006. Details of the share for share exchange transaction and its effects are disclosed in note 22.

For the period from incorporation to 12 December 2006, Hiscox Ltd was a shell company with no material revenues or assets and did not constitute a 'business' as defined by IFRS 3 Business Combinations. Consequently, due to the relative values of both Companies, the shareholders of Hiscox plc immediately before the share exchange acquired, in effect, 100% of the enlarged share capital of Hiscox Ltd on completion of the transaction.

In order to appropriately reflect the substance of the transaction outlined above, the new holding Company was accounted for using the reverse acquisition principles outlined in IFRS 3. Consequently, Hiscox plc was deemed to be the acquirer for accounting purposes and the legal parent Company, Hiscox Ltd, was treated as a subsidiary whose identifiable assets and liabilities are incorporated into the Group at fair value.

The Group's consolidated financial statements are issued in the name of the legal parent Company, Hiscox Ltd. However, as a consequence of applying reverse acquisition accounting, the results for the year ended 31 December 2006 represented a continuation of the consolidated activities of Hiscox plc for the year ended 31 December 2006 plus those of Hiscox Ltd from 12 December 2006. In accordance with Bermuda law the Group's previously reported share premium, merger reserve and capital redemption reserve were presented as contributed surplus at 31 December 2006. Contributed surplus is a distributable reserve.

2.4 Basis of consolidation

(a) Subsidiaries

Subsidiaries are those entities controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Generally this occurs when the Group obtains a shareholding of more than half of the voting rights of an entity. In assessing control, potential voting rights that are currently exercisable or convertible are taken into account. The consolidated financial statements include the assets, liabilities and results of the Group up to 31 December each year. The financial statements of subsidiaries are included in the consolidated financial statements only from the date that control commences until the date that control ceases.

Hiscox Dedicated Corporate Member Limited underwrites as a corporate member of Lloyd's on the main syndicate managed by Hiscox Syndicates Limited (the 'main managed syndicate'). In view of the several but not joint liability of underwriting members at Lloyd's for the transactions of syndicates in which they participate, the Group's attributable share of the transactions, assets and liabilities of this main Syndicate has been included in the financial statements.

The Group uses the purchase method of accounting to account for the acquisition of subsidiaries. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

(b) Associates

Associates are those entities in which the Group has significant influence but not control over the financial and operating policies. Significant influence is generally identified with a shareholding of between 20% and 50% of an entity's voting rights. The consolidated financial statements include the Group's share of the total recognised gains and losses of associates on an equity accounted basis from the date that significant influence commences until the date that significant influence ceases. The Group's share of its associates' post-acquisition profits or losses after tax is recognised in the income statement each period, and its share of the movement in the associates' net assets is reflected in the investments' carrying values in the balance sheet. When the Group's share of losses equals or exceeds the carrying amount of the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred obligations in respect of the associate.

(c) Transactions eliminated on consolidation

Intragroup balances, transactions and any unrealised gains arising from intragroup transactions are eliminated in preparing the consolidated financial statements. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Unrealised gains arising from transactions with associates are eliminated to the extent of the Group's interest in the entity. Unrealised gains arising from transactions in associates are eliminated against the investment in the associate. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

2.5 Foreign currency translation

(a) Functional and presentational currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). The functional currency of all individual entities in the Group is deemed to be Sterling with the exception of the entities operating in France, Germany, the Netherlands and Belgium whose functional currency is Euros, those entities operating from the USA and Bermuda whose functional currency is US Dollars, and Hiscox Insurance Company (Guernsey) Limited whose functional currency is also US Dollars.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the retranslation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying net investment hedges. Non-monetary items carried at historical cost are translated in the balance sheet at the exchange rate prevailing on the original transaction date. Non-monetary items measured at fair value are translated using the exchange rate ruling when the fair value was determined.

(c) Group companies

The results and financial position of all the Group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- (i) assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet
- (ii) income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the date of the transactions)

2 Significant accounting policies continued

2.5 Foreign currency translation continued

(c) Group companies continued

(iii) all resulting exchange differences are recognised as a separate component of equity.

When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as the foreign entity's assets and liabilities and are translated at the closing rate.

2.6 Property, plant and equipment

Property, plant and equipment are stated at historical cost less depreciation and any impairment loss. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance items are charged to the income statement during the financial period in which they are incurred.

Land and artwork assets are not depreciated as they are deemed to have indefinite useful economic lives. The cost of leasehold improvements is amortised over the unexpired term of the underlying lease or the estimated useful life of the asset, whichever is shorter.

Depreciation on other assets is calculated using the straight-line method to allocate their cost or revalued amounts, less their residual values, over their estimated useful lives. The rates applied are as follows:

Buildings	50 years
Vehicles	3 years
Leasehold improvements including fixtures and fittings	10–15 years
Furniture, fittings and equipment	3–15 years

The assets' residual values and useful lives are reviewed at each balance sheet date and adjusted if appropriate.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

2.7 Intangible assets

(a) Goodwill

Goodwill represents amounts arising on acquisition of subsidiaries and associates. In respect of acquisitions that have occurred since 1 January 2004, goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary or associate at the acquisition date.

In respect of acquisitions prior to this date, goodwill is included on the basis of its deemed cost, which represents the amount recorded under previous GAAP.

Goodwill on acquisition of subsidiaries is included in intangible assets. Goodwill on acquisition of associates is included in investments in associates. Goodwill is not amortised but is tested annually for impairment and carried at cost less accumulated impairment losses. The impairment review process examines whether or not the carrying value of the goodwill attributable to individual cash generating units exceeds its implied value. Any excess of goodwill over the recoverable amount arising from the review process indicates impairment.

Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

(b) Syndicate capacity

The cost of purchasing the Group's participation in the Lloyd's insurance syndicates is not amortised but is tested annually for impairment and is carried at cost less accumulated impairment losses. Having considered the future prospects of the London insurance market, the Board believe that the Group's ownership of syndicate capacity will provide economic benefits over an indefinite number of future periods.

(c) State authorisation licences

State authorisation licences acquired in business combinations are recognised initially at their fair value. The asset is not amortised, as the Board considers that economic benefits will accrue to the Group over an indefinite number of future periods, but is tested annually for impairment, and any accumulated impairment losses recognised are deducted from the historical cost amount to produce the net balance sheet carrying amount.

(d) Rights to customer contractual relationships

Costs directly attributable to securing the intangible rights to customer contract relationships are recognised as an intangible asset where they can be identified separately and measured reliably and it is probable that they will be recovered by directly related future profits. These costs are amortised on a straight-line basis over the useful economic life which is deemed to be 20 years and are carried at cost less accumulated amortisation and impairment losses.

(e) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring into use the specific software. These costs are amortised over the expected useful life of the software of between three and five years on a straight-line basis.

Internally developed computer software is only capitalised where the cost can be measured reliably, the Group intends to and has adequate resources to complete development and where the computer software will yield future economic benefits in excess of the costs incurred.

2.8 Financial assets including loans and receivables

The Group has classified financial assets as a) financial assets designated at fair value through profit or loss, and b) loans and receivables. Management determines the classification of its financial investments at initial recognition. The decision by the Group to designate all financial investments, comprising debt and fixed income securities, equities and shares in unit trusts and deposits with credit institutions, at fair value through profit or loss reflects the fact that the investment portfolios are managed, and their performance evaluated, on a fair value basis. Regular way purchases and sales of investments are accounted for at the date of trade.

Financial assets are initially recognised at fair value. Subsequent to initial recognition financial assets are measured as described below.

Financial assets are de-recognised when the right to receive cash flows from them expires or where they have been transferred and the Group has also transferred substantially all risks and rewards of ownership.

Fair value for securities quoted in active markets is the bid price exclusive of transaction costs. For the minority of instruments where no active market exists, fair value is determined by referring to recent transactions and other valuation factors including the discounted value of expected future cash flows. Fair value changes are recognised immediately within the investment result line in the income statement.

2 Significant accounting policies continued

2.8 Financial investments including loans and receivables continued

(a) Financial assets at fair value through profit or loss

A financial asset is classified into this category at inception if it is managed and evaluated on a fair value basis in accordance with documented strategy, if acquired principally for the purpose of selling in the short-term, or if it forms part of a portfolio of financial assets in which there is evidence of short-term profit taking.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market. Receivables arising from insurance contracts are included in this category and are reviewed for impairment as part of the impairment review of loans and receivables. Loans and receivables are carried at amortised cost less any provision for impairment in value.

2.9 Cash and cash equivalents

The Group has classified cash deposits and short-term highly liquid investments as cash and cash equivalents. These assets are readily convertible into known amounts of cash and are subject to inconsequential changes in value. Cash equivalents are financial investments with less than three months to maturity at the date of acquisition.

2.10 Impairment of assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually or whenever there is an indication of impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

Non-financial assets

Objective factors that are considered when determining whether a non-financial asset (such as goodwill, an intangible asset or item of property, plant and equipment) or group of non-financial assets may be impaired include, but are not limited to, the following:

- adverse economic, regulatory or environmental conditions that may restrict future cash flows and asset usage and/or recoverability;
- the likelihood of accelerated obsolescence arising from the development of new technologies and products; and
- the disintegration of the active market(s) to which the asset is related.

Financial assets

Objective factors that are considered when determining whether a financial asset or group of financial assets may be impaired include, but are not limited to, the following:

- negative rating agency announcements in respect of investment issuers, reinsurers and debtors;
- significant reported financial difficulties of investment issuers, reinsurers and debtors;
- actual breaches of credit terms such as persistent late payments or actual default;
- the disintegration of the active market(s) in which a particular asset is traded or deployed; and
- adverse economic or regulatory conditions that may restrict future cash flows and asset recoverability.

Impairment loss

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units).

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior periods. A reversal of an impairment loss is recognised as income immediately. Impairment losses recognised in respect of goodwill are not subsequently reversed.

2.11 Derivative financial instruments

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently valued at their fair value at each balance sheet date. Fair values are obtained from quoted market values and, if these are not available, valuation techniques including option pricing models as appropriate. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged. For derivatives not formally designated as a hedging instrument, fair value changes are recognised immediately in the income statement.

Changes in the value of derivative and other financial instruments formally designated as hedges of net investments in foreign operations are recognised in the currency translation reserve to the extent they are effective; gains or losses relating to the ineffective portion of the hedging instruments are recognised immediately in the consolidated income statement.

The Group had no derivative instruments designated for hedge accounting during the current and prior financial year (see note 2.18).

2.12 Own shares

Where any Group company purchases the parent Company's equity share capital (own shares), the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted from equity attributable to the Company's equity shareholders. Where such shares are subsequently sold, reissued or otherwise disposed of, any consideration received is included in equity attributable to the Company's equity shareholders, net of any directly attributable incremental transaction costs and the related tax effects.

2.13 Revenue

Revenue comprises insurance premiums earned on the rendering of insurance protection, net of reinsurance, together with profit commission, investment returns, agency fees and other income inclusive of foreign exchange gains on instruments not formally designated for hedge accounting treatment. The Group's share of the results of associates is reported separately. The accounting policies for insurance premiums are outlined below. Profit commission, investment income and other sources of income are recognised on an accruals basis net of any discounts and amounts such as sales based taxes collected on behalf of third parties.

2.14 Insurance contracts

(a) Classification

The Group issues short-term casualty and property insurance contracts that transfer significant insurance risk. Such contracts may also transfer a limited level of financial risk.

(b) Recognition and measurement

Gross premiums written comprise premiums on business incepting in the financial year together with adjustments to estimates of premiums written in prior accounting periods. Estimates are included for pipeline premiums and an allowance is also made for cancellations. Premiums are stated before the deduction of brokerage and commission but net of taxes and duties levied. Premiums are recognised as revenue (earned premiums) proportionally over the period of coverage. The portion of premium received on in-force contracts that relates to unexpired risks at the balance sheet date is reported as the unearned premium liability.

2 Significant accounting policies continued

2.14 Insurance contracts continued

(b) Recognition and measurement continued

Claims and associated expenses are charged to profit or loss as incurred based on the estimated liability for compensation owed to contract holders or third parties damaged by the contract holders. They include direct and indirect claims settlement costs and arise from events that have occurred up to the balance sheet date even if they have not yet been reported to the Group. The Group does not discount its liabilities for unpaid claims. Liabilities for unpaid claims are estimated using the input of assessments for individual cases reported to the Group and statistical analysis for the claims incurred but not reported, and an estimate of the expected ultimate cost of more complex claims that may be affected by external factors e.g. court decisions.

(c) Deferred acquisition costs ('DAC')

Commissions and other direct and indirect costs that vary with and are related to securing new contracts and renewing existing contracts are capitalised as deferred acquisition costs. All other costs are recognised as expenses when incurred. DAC are amortised over the terms of the policies as premium is earned.

(d) Liability adequacy test

At each balance sheet date, liability adequacy tests are performed by each segment of the Group to ensure the adequacy of the contract liabilities net of related DAC. In performing these tests, current best estimates of future contractual cash flows and claims handling and administration expenses, as well as investment income from assets backing such liabilities, are used. Any deficiency is immediately charged to profit or loss initially by writing-off DAC and by subsequently establishing a provision for losses arising from liability adequacy tests ('the unexpired risk provision').

Any DAC written-off as a result of this test cannot subsequently be reinstated.

(e) Outwards reinsurance contracts held

Contracts entered into by the Group, with reinsurers, under which the Group is compensated for losses on one or more insurance or reinsurance contracts and that meet the classification requirements for insurance contracts, are classified as insurance contracts held. Contracts that do not meet these classification requirements are classified as financial assets.

The benefits to which the Group is entitled under outwards reinsurance contracts are recognised as reinsurance assets. These assets consist of short-term balances due from reinsurers (classified within loans and receivables) as well as longer-term receivables (classified as reinsurance assets) that are dependent on the expected claims and benefits arising under the related reinsured insurance contracts. Reinsurance liabilities primarily comprise premiums payable for 'outwards' reinsurance contracts. These amounts are recognised in profit or loss proportionally over the period of the contract. Receivables and payables are recognised when due.

The Group assesses its reinsurance assets on a regular basis and if there is objective evidence, after initial recognition, of an impairment in value, the Group reduces the carrying amount of the reinsurance asset to its recoverable amount and recognises the impairment loss in the income statement.

(f) Receivables and payables related to insurance contracts

Receivables and payables are recognised when due. These include amounts due to and from agents, brokers and insurance contract holders.

If there is objective evidence that the insurance receivable is impaired, the Group reduces the carrying amount of the insurance receivable

accordingly and recognises the impairment loss in profit or loss.

(g) Salvage and subrogation reimbursements

Some insurance contracts permit the Group to sell property acquired in settling a claim (i.e. salvage). The Group may also have the right to pursue third parties for payment of some or all costs (i.e. subrogation). Estimates of salvage recoveries are included as an allowance in the measurement of the insurance liability for claims and salvage property is recognised in other assets when the liability is settled. The allowance is the amount that can reasonably be recovered from the disposal of the property.

Subrogation reimbursements are also considered as an allowance in the measurement of the insurance liability for claims and are recognised in other assets when the liability is settled. The allowance is the assessment of the amount that can be recovered from the action against the liable third party.

2.15 Deferred tax

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, if the deferred income tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss, it is not recognised. Deferred tax is determined using tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets are recognised to the extent that it is probable that the future taxable profit will be available against which the temporary differences can be utilised. Deferred tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the Group controls the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

2.16 Employee benefits

(a) Pension obligations

The Group operated a defined contribution arrangement for all active employees during the year under review. The defined benefit scheme closed to future accrual with effect from 31 December 2006 and active members were offered membership of the defined contribution arrangement from 1 January 2007.

A defined contribution arrangement is one under which the Group pays fixed contributions into a separate entity and has no further obligation beyond the agreed contribution rate. A defined benefit scheme is a pension scheme that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation. For the defined contribution arrangement, the Group pays contributions to a privately administered pension insurance plan on a contractual basis. The contributions are recognised as an employee benefit expense when they are due.

The liability recognised in the balance sheet in respect of the defined benefit pension scheme is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets, together with adjustments for unrecognised actuarial gains or losses and past service costs. Scheme assets exclude any insurance contracts issued by the Group. On curtailment, all unrecognised actuarial gains or losses are recognised in the income statement where relevant.

Adjustments either from or to other parties participating in the Lloyd's Syndicate regarding the defined benefit scheme are recognised as a

2 Significant accounting policies continued

2.16 Employee benefits continued

(a) Pension obligations continued

component of the income statement charge or credit and within receivables on the balance sheet in accordance with the policies outlined at 2.8 (b) above.

(b) Other long-term employee benefits

The Group provides sabbatical leave to employees on completion of a minimum service period of ten years. The present value of the expected costs of these benefits is accrued over the period of employment. In determining this liability, consideration is given to future increases in salary levels, experience with employee departures and periods of service.

(c) Share based compensation

The Group operates a number of equity settled share based employee compensation plans. These include both the approved and unapproved share option schemes, and the Group's performance share plans, outlined in the Directors' remuneration report together with the Group's save as you earn ('SAYE') schemes.

The fair value of the employee services received, measured at grant date, in exchange for the grant of the awards is recognised as an expense with the corresponding credit being recorded in retained earnings within equity. The total amount to be expensed over the vesting period is determined by reference to the fair value of the awards granted, excluding the impact of any non-market vesting conditions (e.g. profitability or net asset growth targets). Non-market vesting conditions are included in assumptions about the number of awards that are expected to become exercisable. At each balance sheet date, the Group revises its estimates of the number of awards that are expected to vest. It recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment to equity, over the remaining vesting period.

When the terms and conditions of an equity settled share based employee compensation plan are modified, and the expense to be recognised increases as a result of the modification, then the increase is recognised evenly over the remaining vesting period. When a modification reduces the expense to be recognised, there is no adjustment recognised and the pre-modification expense continues to be applied.

The proceeds received net of any directly attributable transaction costs are credited to share capital and share premium when the options are exercised.

In accordance with the transitional arrangements of IFRS 2 only share based awards granted or modified after 7 November 2002, but not yet vested at the date of adoption of IFRS are included in the calculations.

(d) Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits when it is demonstrably committed to either: terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal; or providing termination benefits as a result of an offer made to encourage voluntary redundancy.

(e) Profit sharing and bonus plans

The Group recognises a liability and an expense for bonuses and profit sharing, based on a formula that takes into consideration the profit attributable to the Company's shareholders after certain adjustments. The Group recognises a provision where a contractual obligation to employees exists or where there is a past practice that has created a constructive obligation.

(f) Accumulating compensation benefits

The Group recognises a liability and an expense for accumulating compensation benefits (e.g. holiday entitlement), based on the additional amount that the Group expects to pay as a result of the unused entitlement accumulated at the balance sheet date.

2.17 Borrowings

Borrowings are financial liabilities and are designated on inception as being held at fair value through profit or loss if they are managed and evaluated on a fair value basis in accordance with a documented strategy or if they eliminate or significantly reduce a measurement or recognition inconsistency. Borrowings are initially measured at fair value with all incremental transaction costs immediately expensed. Borrowings are then consequently measured at fair value at each balance sheet date thereafter, using observable market interest rate data for similar instruments, with all changes in value from one accounting period to the next reflected in the income statement unless they form part of a designated hedge accounting relationship in which case certain changes in value are recognised directly in equity, (see notes 2.18 and 18).

2.18 Net investment hedge accounting

In order to qualify for hedge accounting, the Group is required to document in advance the relationship between the item being hedged and the hedging instrument. The Group is also required to document and demonstrate an assessment of the relationship between the hedged item and the hedging instrument, which shows that the hedge will be highly effective on an ongoing basis. This effectiveness testing is re-performed at each period end to ensure that the hedge remains highly effective.

The Group hedges elements of its net investment in certain foreign entities through foreign currency borrowings that qualify for hedge accounting; accordingly gains or losses on retranslation are recognised in equity to the extent that the hedge relationship is effective. Accumulated gains or losses are recycled to the income statement only when the foreign operation is disposed of. The ineffective portion of any hedge is recognised immediately in the income statement.

2.19 Finance costs

Finance costs consist of interest charges accruing on the Group's borrowings and bank overdrafts together with commission fees charged in respect of letters of credit. Arrangement fees in respect of financing arrangements are charged over the life of the related facilities.

2.20 Provisions

The Group is subject to various insurance related assessments and guarantee fund levies. Provisions are recognised where there is a present obligation (legal or constructive) as a result of a past event that can be measured reliably and it is probable that an outflow of economic benefits will be required to settle that obligation.

2.21 Leases

(a) Hiscox as lessee

Leases in which significantly all of the risks and rewards of ownership are transferred to the Group are classified as finance leases. At the commencement of the lease term, finance leases are recognised as assets and liabilities at the lower of the fair value of the asset and the present value of the minimum lease payments. The minimum lease payments are apportioned between finance charges and repayments of the outstanding liability, finance charges being charged to each period of the lease term so as to produce a constant rate of interest on the outstanding balance of the liability.

All other leases are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor)

2 Significant accounting policies continued

2.21 Leases continued

(a) Hiscox as lessee continued

are charged to the income statement on a straight-line basis over the period of the lease.

(b) Hiscox as lessor

Rental income from operating leases is recognised on a straight-line basis over the term of the relevant contractual agreement.

2.22 Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved.

2.23 Use of critical estimates and assumptions

The Directors consider the accounting policies for determining insurance liabilities, amounts denominated in foreign currencies, the valuation of investments, the valuation of retirement benefit scheme obligations and the determination of current and deferred tax assets and liabilities as being most critical to an understanding of the Group's result and position.

The inherent uncertainty of insurance risk requires the Group to make estimates and assumptions that affect the reported amounts of insurance and reinsurance assets and liabilities at the balance sheet date. This is the most significant area of potential uncertainty in the Group's financial statements.

There are several sources of uncertainty that need to be considered in the estimation of the insurance liabilities that the Group will ultimately pay for valid claims. These include but are not restricted to: inflation; changes in legislation; changes in the Group's claims handling procedures; and discordant judicial opinions which extend the Group's coverage of risk beyond that envisaged at the time of original policy issuance. The Group seeks to gather corroborative evidence from all relevant sources before making judgements as to the eventual outcome of claims, particularly those under litigation, which have occurred and been notified to the Group but remain unsettled at the balance sheet date.

Estimates are continually evaluated based on entity specific historical experience and contemporaneous developments observed in the wider industry, and are also updated for expectations of prospective future developments. Although the possibility exists for material changes in insurance liabilities estimates to have a critical impact on the Group's reported performance and financial position, it is anticipated that the scale and diversity of the Group's portfolio of insurance business considerably lessens the likelihood of this occurring. Note 24 to consolidated financial statements provides a greater analysis of the main methods used by the Group when formulating estimates of the insurance claims liabilities at each balance sheet date.

With regard to employee retirement benefit scheme obligations, the assets, liabilities and changes disclosed in these consolidated financial statements are sensitive to assumptions regarding mortality, inflation, investment returns and interest rates on corporate bonds, the latter of which has been subject to specific recent volatility.

Legislation concerning the determination of taxation assets and liabilities is complex and continually evolving. In preparing the Group's financial statements, the Directors estimate taxation assets and liabilities after taking appropriate professional advice. The determination and finalisation of agreed taxation assets and liabilities may not occur until several years after the balance sheet date and consequently the final amounts payable or receivable may differ from those presently recorded in these financial statements.

2.24 Reporting of additional performance measures

The Directors consider that the claims ratio, expense ratio and combined ratio measures reported in respect of operating segments and the Group overall at note 4 provide useful information regarding the underlying performance of the Group's businesses. These measures are widely recognised by the insurance industry and are consistent with internal performance measures reviewed by senior management including the chief operating decision maker. However, these three measures are not defined within the IFRS framework and body of standards and interpretations and therefore may not be directly comparable with similarly titled additional performance measures reported by other companies.

3 Management of risk

Overview of risk

The Group enters into contracts that directly accept and transfer insurance risk, which in turn necessarily creates exposure to financial and other classes of risk. Consequently, Hiscox is fundamentally concerned with the identification and management of all significant risks.

The Group's overall appetite for accepting and managing varying classes of risk is defined by the Group's Board. The Board has developed a governance framework and set Group-wide risk management policies and procedures which cover specific areas such as risk identification, risk management and mitigation, and risk reporting. The objective of these policies and procedures is to protect the Group's shareholders, policyholders and other stakeholders from negative events that could hinder the Group's delivery of its contractual obligations and its achievement of sustainable profitable economic and social performance.

The Board exercises oversight over the development and operational implementation of its risk management policies and procedures, and ongoing compliance therewith, partially through its own enquiries but primarily through a dedicated internal audit function, which has operational independence, clear terms of reference influenced by the Board's Non Executive Directors and a clear upwards reporting structure back into the Board.

The main sources of risk relevant to the Group's operations and its financial statements fall into two broad categories: insurance risk and financial risk. Note 3.1 details the Group's approach to managing insurance risk specifically whilst note 3.2 onwards outlines the Group's sensitivity to financial risk generally. Additional information is also provided in the Corporate governance and Risk management sections of this Report and Accounts.

3.1 Insurance risk

Insurance risk is transferred to the Group by contract holders through the underwriting process. The Group's exposure to insurance risk arises from the possibility that an insured event occurs, and a claim is subsequently submitted by the insured for payment. Management of insurance risk on a day-to-day basis is the responsibility of the Chief Underwriting Officer, who receives assistance from the management information and risk modelling departments.

The Board sets the Group's underwriting strategy for accepting and managing insurance risk prospectively, seeking to exploit identified opportunities and taking cognisance of other relevant anticipated market conditions. Specific underwriting objectives such as aggregation limits, reinsurance protection thresholds, geographical disaster event risk exposures and line of business diversification parameters are prepared and reviewed by the Chief Underwriting Officer in order to translate the Board's summarised underwriting strategy into specific measurable actions and targets. These actions and targets are reviewed and approved by the Board in advance of each underwriting year. The Board continually reviews its underwriting strategy throughout each underwriting year in light of the evolving

3 Management of risk continued

3.1 Insurance risk continued

market pricing and loss conditions and as opportunities present themselves.

The Board requires all underwriters to operate within an overall Group appetite for individual events. This defines the maximum exposure that the Group is prepared to retain on its own account for any one potential catastrophe event or disaster. The Group's underwriting risk appetite seeks to ensure that it should not lose more than one years profit plus 15% of core capital as a result of a 1 in 250 bad year.

Realistic disaster scenarios are extreme, hypothetical events selected by Lloyd's to represent major events occurring in areas with large insured values. They also reflect the areas that represent significant exposures for Hiscox. The Group compiles estimates of losses arising from realistic disaster events using statistical models alongside input from its underwriters. The selection of realistic disaster scenario events is adjusted each year and they are not therefore necessarily directly comparable from one year to the next. The events are extreme and as yet untested, and as such these estimates may prove inadequate as a result of incorrect assumptions, model deficiencies, or losses from unmodelled risks. This means that should a realistical disaster actually eventuate, the Group's final ultimate losses could materially differ from the current estimates presented below. Estimates of the Group's maximum loss exposure to a selection of realistic disaster scenarios are shown in the first table below. The Group's estimated concentration of insurance risk, determined in relation to the broad categories of insurance liabilities reserved on the balance sheet, is summarised in the tables on page 74.

The Group's underwriters and management consider insurance risk at an individual contract level, and also from a portfolio perspective where the risks assumed in similar classes of policies are aggregated and the exposure evaluated in light of historical portfolio experience and prospective factors. To assist with the process of pricing and managing insurance risk the Group routinely performs a wide range of activities including the following:

- regularly updating the Group's risk models;
- documenting, monitoring and reporting on the Group's strategy to manage risk;
- developing systems that facilitate the identification of emerging issues promptly;

- utilising sophisticated computer modelling tools to simulate catastrophes and measure the resultant potential losses before and after reinsurance;
- monitoring legal developments and amending the wording of policies when necessary;
- regularly aggregating risk exposures across individual underwriting portfolios and known accumulations of risk;
- examining the aggregated exposures in advance of underwriting further large risks; and
- developing processes that continually factor market intelligence into the pricing process.

The delegation of underwriting authority to specific individuals, both internally and externally, is subject to regular review. All underwriting staff and binding agencies are set strict parameters in relation to the levels and types of business they can underwrite, based on individual levels of experience and competence. These parameters cover areas such as the maximum sums insured per insurance contract, maximum gross written premiums and maximum aggregated exposures per geographical zone and risk class. Monthly meetings are held between the Chief Underwriting Officer and a specialist central analysis and review team in order to monitor claim development patterns and discuss individual underwriting issues as they arise. The Chief Underwriting Officer also holds weekly video conference meetings with this team to discuss interim underwriting matters.

The Group's insurance contracts include provisions to contain losses such as the ability to impose deductibles and demand reinstatement premiums in certain cases. In addition, in order to manage the Group's exposure to repeated catastrophic events, relevant policies frequently contain payment limits to cap the maximum amount payable from these insured events over the contract period.

One tool for managing insurance risk is reinsurance. Reinsurance protection such as excess of loss cover is purchased at an entity level and is also considered at an overall Group level to mitigate the effect of catastrophes and unexpected concentrations of risk. However, the scope and type of reinsurance protection purchased may change depending on the competitiveness of cover available in the market.

Estimated sensitivity to realistic disaster scenarios at 1 January 2008

	Gross loss £m	Net loss £m	Gross loss as a % of GWP	Net loss as a % of NWP	Net loss as a % of insurance industry loss	Industry loss size £ billion	Return period* years
Japan Earthquake	164	109	14	11	0.4	25	100
Gulf of Mexico Windstorm	484	187	40	19	0.3	65	115
Florida Windstorm	333	92	28	9	0.2	58	105
European Windstorm	250	104	21	11	0.7	15	60
San Francisco Earthquake	336	93	28	10	0.5	20	120

Estimated sensitivity to realistic disaster scenarios at 1 January 2007

	Gross loss £m	Net loss £m	Gross loss as a % of GWP	Net loss as a % of NWP	Net loss as a % of insurance industry loss	Industry loss size £ billion	Return period* years
Japan Earthquake	151	101	13	10	0.2	42	190
Gulf of Mexico Windstorm	376	139	33	14	0.2	64	100
Florida Windstorm	321	88	29	9	0.2	58	90
European Windstorm	341	147	30	15	0.9	17	80
San Francisco Earthquake	269	78	24	8	0.4	20	120

*A return period relates to the annual probability of a loss from an individual event for a particular peril exceeding a given amount. For example if industry underwriting models suggests that there is a 1% chance per year of a Japanese earthquake generating an insured loss to the industry exceeding £25 billion, then the return period for a £25 billion Japanese earthquake would commonly be described as 100 years. Similarly a 250 year return period suggests a level of insured loss to the industry with a 0.4% probability of exceedance.

3 Management of risk continued

3.1 Insurance risk continued

Estimated concentration of gross and net insurance liabilities on balance sheet by territory coverage of premium written

		Types of insurance risk in Group							
		Reinsurance inwards £000	Property – Marine and major assets £000	Property – Other assets £000	Casualty – Professional indemnity £000	Casualty – Other risks £000	Other* £000	Total £000	
31 December 2007	UK and Ireland	Gross	47,633	7,200	122,967	263,869	1,332	28,446	471,447
		Net	40,498	6,841	101,690	199,573	1,235	17,307	367,144
Europe	Gross	43,751	22,367	47,799	66,758	11,662	15,340	207,677	
	Net	41,167	16,918	41,764	53,523	9,022	10,194	172,588	
United States	Gross	111,008	26,390	92,012	131,466	18,083	13,095	392,054	
	Net	87,937	15,270	90,686	129,457	16,495	10,406	350,251	
Other territories	Gross	34,163	96,391	53,664	75,478	58,735	37,827	356,258	
	Net	31,292	74,946	52,564	61,171	43,920	49,650	313,543	
Multiple territory coverage	Gross	103,081	81,095	18,364	1,808	48,576	33,527	286,451	
	Net	88,419	61,345	18,165	1,101	32,842	28,401	230,273	
Total	Gross	339,636	233,443	334,806	539,379	138,388	128,235	1,713,887	
	Net	289,313	175,320	304,869	444,825	103,514	115,958	1,433,799	

		Types of insurance risk in Group							
		Reinsurance inwards £000	Property – Marine and major assets £000	Property – Other assets £000	Casualty – Professional indemnity £000	Casualty – Other risks £000	Other* £000	Total £000	
31 December 2006	UK and Ireland	Gross	74,176	5,889	87,420	237,914	9,722	44,525	459,646
		Net	49,679	5,226	80,863	188,166	9,431	22,091	355,456
Europe	Gross	32,039	17,757	45,372	40,539	1,975	6,451	144,133	
	Net	26,751	15,250	37,801	32,995	1,583	5,257	119,637	
United States	Gross	67,037	69,949	113,768	188,770	27,734	17,652	484,910	
	Net	58,556	59,135	98,274	152,688	20,756	13,269	402,678	
Other territories	Gross	17,147	58,868	45,701	13,558	42,543	43,482	221,299	
	Net	14,990	50,949	39,698	10,475	30,151	41,718	187,981	
Multiple territory coverage	Gross	74,750	112,707	17,027	125	43,105	36,399	284,113	
	Net	64,024	85,621	14,709	100	33,548	27,575	225,577	
Total	Gross	265,149	265,170	309,288	480,906	125,079	148,509	1,594,101	
	Net	214,000	216,181	271,345	384,424	95,469	109,910	1,291,329	

*Includes a diverse mix of certain specialty lines such as kidnap and ransom, terrorism, bloodstock and other risks which contain a mix of property and casualty exposures.

Frequency and severity of claims

The specific insurance risks accepted by the Group fall broadly into four main categories: reinsurance inwards, marine and major property risks, other property risks and casualty insurance risks. These specific categories are defined for risk review purposes only and are not exclusively aligned to any specific reportable segment in the Group's operational structure or the primary internal reports reviewed by the chief operating decision maker. A discussion of the frequency and severity of claims for each of those categories is given below. The Group has no significant exposure to asbestos risks or life insurance business.

Reinsurance inwards

The Group's reinsurance inwards acceptances are primarily focused on large commercial property, homeowner and marine exposures held by other insurance companies predominantly in North America and other developed economies. This business is characterised more by large claims arising from individual events or catastrophes than the high frequency, low severity attritional losses associated with certain other business written by the Group. Multiple insured losses can periodically arise out of a single natural or man-made occurrence.

The main circumstances that result in claims against the reinsurance inwards book are conventional catastrophes, such as earthquakes or storms, and other events including fires and explosions. The occurrence and impact of these events is very difficult to model over the short-term which complicates attempts to anticipate loss

frequencies on an annual basis. In those years where there is a low incidence of severe catastrophes, loss frequencies on the reinsurance inwards book can be relatively low.

A significant proportion of the reinsurance inwards business provides cover on an excess of loss basis for individual events. The Group agrees to reimburse the cedant once their losses exceed a minimum level. Consequently the frequency and severity of reinsurance inwards' claims is related not only to the number of significant insured events that occur but also to their individual magnitude. If numerous catastrophes occurred in any one year but the cedant's individual loss on each was below the minimum stated, then the Group would have no liability under such contracts.

Maximum gross line sizes and aggregate exposures are set for each type of programme.

Property risks – Marine and major assets

The Group directly underwrites a diverse range of property risks. The risk profile of the property covered under marine and major asset policies is different to that typically contained in the other classes of property (such as private households and contents insurance) covered by the Group.

Typical property covered by marine and other major property contracts include fixed and moveable assets such as ships and other vessels, cargo in transit, energy platforms and installations, pipelines, other

3 Management of risk continued

3.1 Insurance risk continued

Property risks – Marine and major assets continued

subsea assets, satellites, commercial buildings and industrial plants and machinery. These assets are typically exposed to a blend of catastrophic and other large loss events, and attritional claims arising from conventional hazards such as collision, flooding, fire and theft. Climatic changes may give rise to more frequent and severe extreme weather events (for example earthquakes, windstorms and river flooding etc.) and it may be expected that their frequency will increase over time.

For this reason the Group accepts major property insurance risks for periods of mainly one year so that each contract can be re-priced on renewal to reflect the continually evolving risk profile. The most significant risks covered for periods exceeding one year are certain specialist lines such as marine and offshore construction projects which can typically have building and assembling periods of between three and four years. These form a small proportion of the Group's overall portfolio.

Marine and major property contracts are normally underwritten by reference to the commercial replacement value of the property covered. The cost of repairing or rebuilding assets, of replacement or indemnity for contents and time taken to restart or resume operations to original levels for business interruption losses are the key factors that influence the level of claims under these policies.

Other property risks

The Group provides home and contents insurance, together with cover for art work, antiques, classic cars, jewellery, collectables and other assets held by affluent individuals.

Events which can generate claims on these contracts include burglary, acts of vandalism, fires, flooding and storm damage. Losses can be predicted with a greater degree of certainty as there is a rich history of actual loss experience data and the locations of the assets covered, and the individual levels of security taken by owners, are relatively static from one year to the next. The losses associated with these contracts tend to be of a higher frequency and lower severity than the marine and other major property assets covered above.

The Group's home and contents insurance contracts are exposed to weather and climatic risks such as floods and windstorms and their consequences. As outlined earlier the frequency and severity of these losses do not lend themselves to accurate prediction over the short-term. Contract periods are therefore not normally more than one year at a time to enable risks to be regularly re-priced.

Contracts are underwritten by reference to the commercial replacement value of the properties and contents insured, and claims payment limits are always included to cap the amount payable on occurrence of the insured event.

Casualty insurance risks

The casualty underwriting strategy attempts to ensure that the underwritten risks are well diversified in terms of type and amount of potential hazard, industry and geography. However, the Group's exposure is more focused towards marine and professional and technological liability risks rather than human bodily injury risks, which are only accepted under limited circumstances. Claims typically arise from incidents such as errors and omissions attributed to the insured, professional negligence and specific losses suffered as a result of electronic or technological failure of software products and websites. The provision of insurance to cover allegations made against individuals acting in the course of fiduciary or managerial responsibilities, including directors' and officers' insurance, is one example of a casualty insurance risk. However the Group's specific exposure to this specific risk category is relatively limited. The Group's casualty insurance contracts mainly experience low severity attritional losses.

The Group's pricing strategy for casualty insurance policies is typically based upon historical claim frequencies and average claim severities, adjusted for inflation and extrapolated forwards to incorporate projected changes in claims patterns. In determining the price of each policy an allowance is also made for acquisition and administration expenses, reinsurance costs, investment returns and the Group's cost of capital.

Sources of uncertainty in the estimation of future claim payments

The Group's procedures for estimating the outstanding costs of settling insured losses at the balance sheet date, including those not yet notified by, or apparent to, the insured, are detailed in note 24.

The majority of the Group's insurance risks are short tail and, based on past history, significant claims are normally notified and settled within 12 to 24 months of the insured event occurring. Those claims taking the longest time to develop and settle typically relate to casualty risks where legal complexities occasionally develop regarding the insured's alleged omissions or negligence.

The majority of the Group's casualty exposures are written on a claims made basis. However the final quantum of these claims may not be established for a number of years after the event. Consequently a significant proportion of the casualty insurance amounts reserved on the balance sheet may not be expected to settle within 24 months of the balance sheet date.

Certain marine and property insurance contracts such as those relating to subsea and other energy assets, and the related business interruption risks, can also take longer than normal to settle. This is because of the length of time required for detailed subsea surveys to be carried out and damage assessments agreed together with difficulties in predicting when the assets can be brought back into full production.

3.2 Financial risk Overview

The Group is exposed to financial risk through its ownership of financial assets including loans and receivables, financial liabilities and reinsurance assets. These items collectively represent a significant element of the Group's net shareholder funds.

The key financial risk for the Group is that the proceeds from its financial assets are not sufficient to fund the obligations arising from its insurance contracts and financial liabilities. The most important entity and economic variables that could result in such an outcome relate to risk factors such as equity price risk, interest rate risk, credit risk, liquidity risk and currency risk. The Group's policies and procedures for managing exposure to these specific categories of risk are detailed below.

(a) Equity price risk

The Group is exposed to equity price risk through its holdings of equity and unit trust investments. However this is limited to a small and controlled proportion of the overall investment portfolio and the equity and unit trust holdings involved are well diversified over a number of companies and industries. The fair value amounts held at the balance sheet date may be analysed as follows:

	2007 % weighting	2006 % weighting
Nature of equity and unit trust holdings		
Directly held equity securities	3	1
Units held in funds – traditional long only	77	92
Units held in funds – long and short and special strategies	20	7
Geographic focus		
Specific UK mandates	40	59
Global mandates	60	41

3 Management of risk continued

3.2 Financial risk continued

(a) Equity price risk continued

The allocation of equity risk is not heavily confined to any one market index so as to reduce the Group's exposure to individual sensitivities. A 10% downward correction in equity prices at 31 December 2007 would have been expected to reduce Group equity and profit after tax for the year by approximately £11.6 million (2006: £9.9 million). A 10% upward movement is estimated to have an equal but opposite effect.

Reliability of fair values

The Group has elected to carry all financial investments at fair value through income as they are managed and evaluated on a fair value basis in accordance with a documented strategy. With the exception of unquoted equity investments, all of the financial investments held by the Group trade in public markets and the Group therefore determines fair value by reference to published price quotations in the most active financial markets in which the assets trade. The Group determines the fair value of financial assets primarily with reference to their closing bid market prices at the balance sheet date. The ability to obtain quoted bid market prices may be reduced in periods of diminished liquidity, such as those prevailing for certain categories of asset-backed and mortgage-backed fixed income instruments affected by the continued market dislocation that commenced during the second half of 2007. In such instances fair values may be determined using other observable market inputs such as prices provided by market makers such as dealers and brokers, and prices achieved in the most recent regular transaction of identical or closely related instruments occurring before the balance sheet date but updated for relevant perceived changes in market conditions.

At 31 December 2007, the Group holds asset-backed and mortgage-backed fixed income instruments in its investment portfolio but has minimal direct exposure to sub-prime asset classes. All such instruments with sub-prime exposure held by the Group were independently rated AAA by at least one of the major rating agencies at 31 December 2007. Together with the Group's investment managers, management continues to monitor the potential for any adverse development associated with this investment exposure through the analysis of relevant factors such as credit ratings, collateral, subordination levels and default rates in relation to the securities held.

Valuation of these securities will continue to be impacted by external market factors including default rates, rating agency actions, and liquidity. The Company will make adjustments to the investment portfolio as appropriate as part of its overall portfolio strategy, but its ability to mitigate its risk by selling or hedging its exposures may be limited by the market environment. The Company's future results may be impacted, both positively and negatively, by the valuation adjustments applied to these securities, however management does not feel that this will have a material impact on the Group's results, cash flows or reported financial position. The Group currently expects all such instruments to mature as expected on their pre-determined contractual terms.

The fair value of unquoted equity investments is determined by reference to recent observable market transactions and other valuation factors including the discounted value of expected future cash flows. The carrying value of unquoted equity investments included in the Group's balance sheet at 31 December 2007 was £4,151,000 (2006: £976,000), representing less than 1% of the total financial assets carried at fair value.

(b) Interest rate risk

Fixed income investments represent a significant proportion of the Group's assets and the Board continually monitors investment strategy to minimise the risk of a fall in the portfolio's market value which could affect the amount of business that the Group is able to underwrite or its ability to settle claims as they fall due. The fair value of the Group's

investment portfolio of debt and fixed income securities is inversely correlated to movements in market interest rates. If market interest rates fall, the fair value of the Group's debt and fixed income investments would tend to rise and vice versa.

Debt and fixed income assets are predominantly invested in high quality corporate, government and asset backed bonds. The investments typically have relatively short durations and terms to maturity. The portfolio is managed to minimise the impact of interest rate risk on anticipated Group cash flows.

The fair value of debt and fixed income assets in the Group's balance sheet at 31 December 2007 was £1,445million (2006: £1,044 million). These may be analysed as follows:

	31 December 2007 % weighting	31 December 2006 % weighting
Nature of debt and fixed income holdings		
Government issued bonds and instruments	35	45
Asset backed securities (all AAA rated)	16	18
Mortgage backed instruments – Agency (all AAA rated)	7	3
Mortgage backed instruments – Non-agency (all AAA rated)	13	14
Corporate bonds	27	18
Lloyd's and money market deposits	2	2

One method of assessing interest rate sensitivity is through the examination of duration-convexity factors in the underlying portfolio. Using a duration-convexity based sensitivity analysis, if market interest rates had risen by 100 basis points at the balance sheet date, the fair value might have been expected to decrease by £22 million (2006: decrease of £13 million).

Insurance contract liabilities are not directly sensitive to the level of market interest rates, as they are undiscounted and contractually non-interest-bearing. The Group's debt and fixed income assets are further detailed at note 18.

The Group's major borrowing facility at 31 December 2007 totalled £91,764,000 (2006: £92,852,000). The Group agreed an interest rate margin at the commencement of the borrowing term in November 2005 and the applicable base interest rate element is reset to applicable LIBOR market rates at periodic intervals dependent on the Group's perception of interest rate outlook. The overall interest charge associated with these borrowings is currently fixed at 6.12% until 30 June 2008. The Group has no other significant borrowings or other assets or liabilities carrying interest rate risk, other than the facilities and Letters of Credit outlined in note 33.

(c) Credit risk

The Group has exposure to credit risk, which is the risk that a counterparty will suffer a deterioration in perceived financial strength or be unable to pay amounts in full when due.

Key areas of exposure to credit risk include:

- reinsurers' share of insurance liabilities;
- amounts due from reinsurers in respect of claims already paid;
- amounts due from insurance contract holders; and
- counterparty risk with respect to cash and cash equivalents, and investments including deposits and derivative transactions.

The Group's maximum exposure to credit risk is represented by the carrying values of monetary assets and reinsurance assets included in the consolidated balance sheet. The Group does not use credit derivatives or other products to mitigate maximum credit risk exposures. The Group structures the levels of credit risk accepted by placing limits

3 Management of risk continued

3.2 Financial risk continued

(c) Credit risk continued

on their exposure to a single counterparty, or groups of counterparties, and having regard to geographical locations. Such risks are subject to an annual or more frequent review. There is no significant concentration of credit risk with respect to loans and receivables, as the Group has a large number of internationally dispersed debtors with unrelated operations.

Reinsurance is used to contain insurance risk. This does not, however, discharge the Group's liability as primary insurer. If a reinsurer fails to pay a claim for any reason, the Group remains liable for the payment to the policyholder. The creditworthiness of reinsurers is therefore continually reviewed throughout the year.

The Group Reinsurance Security Committee assesses the creditworthiness of all reinsurers by reviewing credit grades provided by rating agencies and other publicly available financial information detailing their financial strength and performance. The financial analysis of reinsurers produces an assessment categorised by Standard & Poor's (S&P) rating (or equivalent when not available from S&P).

The Committee considers the reputation of its reinsurance partners and

also receives details of recent payment history and the status of any ongoing negotiations between Group companies and these third parties. This information is used to update the reinsurance purchasing strategy.

Individual operating units maintain records of the payment history for significant brokers and contract holders with whom they conduct regular business. The exposure to individual counterparties is also managed by other mechanisms, such as the right of offset where counterparties are both debtors and creditors of the Group. Management information reported to the Group's Board includes details of provisions for impairment on loans and receivables and subsequent write-off. Exposures to individual intermediaries and groups of intermediaries are collected within the ongoing monitoring of the controls associated with regulatory solvency.

The Group also mitigates credit counterparty risk by concentrating debt and fixed income investments in high quality instruments, including a particular emphasis on government gilts issued mainly by European Union and North American countries.

An analysis of the Group's major exposures to counterparty credit risk excluding loans and receivables, based on Standard & Poor's or equivalent rating, is presented below:

	Note	AAA £000	AA £000	A £000	Other/ not rated £000	Total £000
As at 31 December 2007						
Debt and fixed income securities	18	1,116,903	106,754	158,157	62,718	1,444,532
Reinsurance assets	17	15,309	134,475	120,536	9,768	280,088
Cash and cash equivalents	21	97,816	173,755	31,166	5	302,742
Deposits with credit institutions	18	35,911	501	107,462	-	143,874
Derivative financial assets/(liabilities)	18, 20	-	-	-	-	-
Total		1,265,939	415,485	417,321	72,491	2,171,236
Amounts attributable to largest single counterparty		252,875	96,909	17,984	4,996	

The largest counterparty exposure within AAA rating is with the US Treasury. A significant proportion of 'other/not rated' reinsurance assets at 31 December 2007 are supported by letter of credit guarantees issued by financial institutions with Standard & Poor's or equivalent credit or financial strength ratings of A or better.

	Note	AAA £000	AA £000	A £000	Other/ not rated £000	Total £000
As at 31 December 2006						
Debt and fixed income securities	18	742,964	72,210	140,634	87,861	1,043,669
Reinsurance assets	17	20,892	130,155	121,261	30,464	302,772
Cash and cash equivalents	21	115,661	242,980	144,228	2	502,871
Deposits with credit institutions	18	-	-	54,715	-	54,715
Derivative financial assets/(liabilities)	18, 20	-	608	-	-	608
Total		879,517	445,953	460,838	118,327	1,904,635
Amounts attributable to largest single counterparty		215,745	46,600	23,649	17,209	

The largest counterparty exposure within the AAA rating is with the US Treasury. The largest counterparty exposure under other ratings is a reinsurance asset that is supported by Letter of Credit guarantees rated A or better.

At 31 December 2007 the Group held no material debt and fixed income assets that were past due or impaired beyond their reported fair values, either for the current period under review or on a cumulative basis (2006: £nil). For the current and prior periods under review, all of the Group's maturing financial instruments settled on their original contractual terms and payment dates, and the Group therefore experienced no losses of, or delays in recovering, principal amounts invested.

(d) Liquidity risk

The Group is exposed to daily calls on its available cash resources mainly from claims arising from insurance contracts. Liquidity risk is the risk that cash may not be available to pay obligations when due at a reasonable cost. The Board sets limits on the minimum level of cash and maturing funds available to meet such calls and on the minimum level of borrowing facilities that should be in place to cover at unexpected levels of claims and other cash demands.

A significant proportion of the Group's investments are in highly liquid assets which could be converted into cash in a prompt fashion and at minimal expense. The deposits with credit institutions largely comprise short dated certificates for which an active market exists and which the Group can easily access. The Group's exposure to equities is concentrated on shares and funds that are frequently traded on internationally recognised stock exchanges.

3 Management of risk continued

3.2 Financial risk continued

(d) Liquidity risk continued

The main focus of the investment portfolio is on high quality short duration debt and fixed income securities, and cash. There is no significant holdings of investments with specific repricing dates. Notwithstanding the regular interest receipts and also the Group's ability to liquidate these securities and its other financial instrument assets, for cash in a prompt and reasonable manner, the contractual maturity profile of the fair value of these securities at 31 December was as follows:

Fair values at balance sheet date analysed by contractual maturity

	Debt and fixed income securities £000	Cash and cash equivalents £000	Deposits with credit institutions £000	2007 Total £000	2006* Total £000
Less than one year	176,432	302,742	132,757	611,931	783,477
Between one and two years	374,869	–	11,117	385,986	257,883
Between two and five years	563,052	–	–	563,052	307,325
Over five years	282,110	–	–	282,110	192,890
Sub-total	1,396,463	302,742	143,874	1,843,079	1,541,575
Perpetual notes and other non-dated instruments	48,069	–	–	48,069	60,288
Total	1,444,532	302,742	143,874	1,891,148	1,601,863

*Included in amounts receivable in 'less than one year' are derivative balances at 31 December 2007 of £nil (2006: £608,000).

The Group's equities and shares in unit trusts and perpetual notes and other non-dated instruments have no contractual maturity terms but could also be orderly liquidated for cash in a prompt and reasonable timeframe within one year of the balance sheet date if so required.

Average contractual maturity analysed by denominational currency of investments

	2007 Years	2006 Years
Pound Sterling	4.69	3.56
US Dollar	9.42	7.76
Euro	4.11	3.99
Canadian Dollar	1.83	1.47

The following is an analysis by liability type of the estimated timing of net cash flows based on the net claims liabilities held. The Group does not discount claims liabilities. The estimated phasing of settlement is based on current estimates and historical trends and the actual timing of future settlement cash flows may differ materially from that disclosure below.

Liquidity requirements to settle estimated profile of net claim liabilities on balance sheet

	Within one year £000	Between one and two years £000	Between two and five years £000	Over five years £000	2007 Total £000
Reinsurance inwards	95,083	71,981	20,058	21,404	208,526
Property – marine and major assets	53,458	53,688	15,932	7,947	131,025
Property – other assets	108,740	50,832	16,618	6,369	182,559
Casualty – professional indemnity	104,889	121,326	87,778	34,188	348,181
Casualty – other risks	26,851	32,324	15,355	12,462	86,992
Other*	14,965	13,062	4,518	3,387	35,932
Total	403,986	343,213	160,259	85,757	993,215

Liquidity requirements to settle estimated profile of net claim liabilities on balance sheet

	Within one year £000	Between one and two years £000	Between two and five years £000	Over five years £000	2006 Total £000
Reinsurance inwards	57,103	52,221	21,183	23,864	154,371
Property – marine and major assets	51,151	56,694	17,690	8,519	134,054
Property – other assets	85,524	44,636	15,204	6,074	151,438
Casualty – professional indemnity	106,976	105,249	77,332	25,095	314,652
Casualty – other risks	28,405	27,570	11,482	10,360	77,817
Other*	12,000	11,420	4,163	3,341	30,924
Total	341,159	297,790	147,054	77,253	863,256

*Includes a diverse mix of certain specialty lines such as kidnap and ransom, terrorism, bloodstock and other risks which contain a mix of property and casualty exposures.

Details of the payment profile of other Group liabilities is given in notes 18 and 25.

(e) Currency risk

The Group operates internationally and its exposures to foreign exchange risk arise primarily with respect to the US Dollar and the Euro. The assets of the Group's Bermudian, US and European insurance businesses are generally invested in assets denominated in the same currencies as their insurance and investment liabilities.

The Group has financed a portion of its net investment in its Bermudian and Guernsey based operations, which have US Dollar functional currencies, using US Dollar denominated borrowings, to which net investment hedge accounting has applied for the vast majority of the year under review,

3 Management of risk continued

3.2 Financial risk continued

(e) Currency risk continued

(see note 18). The Group also entered into foreign currency derivative transactions during the current and prior years under review, details of which are given in note 20. All foreign currency derivative transactions are managed centrally by designated individuals, delegated thresholds are set and Board approval is required in advance of all significant individual and aggregated positions being taken. Included in the tables below are net non-monetary liabilities of £233 million (2006: £231 million) which are denominated in foreign currencies.

The profile of the Group's assets and liabilities, categorised by currency at their translated carrying amount is as follows:

At 31 December 2007	Sterling £000	US Dollar £000	Euro £000	Other £000	Total £000
Intangible assets	35,369	5,083	–	–	40,452
Property, plant and equipment	17,281	1,499	598	–	19,378
Investments in associates	986	–	516	–	1,502
Deferred acquisition costs	47,637	56,001	15,204	4,239	123,081
Financial assets carried at fair value	411,908	1,130,080	165,258	40,581	1,747,827
Loans and receivables including insurance receivables	158,151	168,889	48,280	9,902	385,222
Reinsurance assets	87,963	166,436	19,912	5,777	280,088
Cash and cash equivalents	116,780	130,634	44,606	10,722	302,742
Total assets	876,075	1,658,622	294,374	71,221	2,900,292
	Sterling £000	US Dollar £000	Euro £000	Other £000	Total £000
Employee retirement benefit obligations	–	–	–	–	–
Deferred tax	9,751	–	–	–	9,751
Insurance liabilities	491,339	1,015,832	167,302	39,414	1,713,887
Financial liabilities carried at fair value	–	91,764	–	–	91,764
Current tax	24,711	–	–	–	24,711
Trade and other payables	51,390	114,521	54,219	15,745	235,875
Total liabilities	577,191	1,222,117	221,521	55,159	2,075,988
	Sterling £000	US Dollar £000	Euro £000	Other £000	Total £000
At 31 December 2006					
Intangible assets	33,212	–	–	–	33,212
Property, plant and equipment	12,222	1,088	511	–	13,821
Investments in associates	28	–	–	–	28
Deferred acquisition costs	53,503	52,463	10,276	873	117,115
Financial assets carried at fair value	478,159	580,028	147,386	36,337	1,241,910
Loans and receivables including insurance receivables	152,076	242,823	41,588	9,785	446,272
Reinsurance assets	83,325	192,657	20,758	6,032	302,772
Cash and cash equivalents	69,219	392,644	33,273	7,735	502,871
Total assets	881,744	1,461,703	253,792	60,762	2,658,001
	Sterling £000	US Dollar £000	Euro £000	Other £000	Total £000
Employee retirement benefit obligations	3,801	–	–	–	3,801
Deferred tax	8,467	–	–	–	8,467
Insurance liabilities	441,619	984,763	132,912	34,807	1,594,101
Financial liabilities carried at fair value	297	93,555	77	–	93,929
Current tax	20,793	–	–	–	20,793
Trade and other payables	114,428	99,382	35,432	5,583	254,825
Total liabilities	589,405	1,177,700	168,421	40,390	1,975,916

Sensitivity analysis

A 10% strengthening or weakening of the following currencies against Pound Sterling at 31 December 2007 would be estimated to have (decreased)/increased equity and profit or loss before tax by the approximate amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2006.

	Effect on equity £m	Effect on profit before tax £m
31 December 2007		
US Dollar	51.3	32.2
Euro	6.9	9.9
31 December 2006		
US Dollar	40.6	15.5
Euro	7.3	10.4

3 Management of risk continued

3.2 Financial risk continued

(e) Currency risk continued

Sensitivity analysis continued

A 10% weakening of the Pound Sterling against the above currencies at 31 December would have been expected to result in equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

(f) Limitations of sensitivity analysis

The sensitivity information given in notes (a) to (e) above demonstrates the impact of a change in a major input assumption while other assumptions remain unchanged. In reality, there is normally significant levels of correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results.

The sensitivity analyses do not take into consideration that the Group's assets and liabilities are actively managed. Additionally, the financial position of the Group may vary at the time that any actual market movement occurs. For example, the Group's financial risk management strategy aims to manage the exposure to market fluctuations.

As investment markets move past various trigger levels, management actions could include selling investments, changing investment portfolio allocation and taking other protective action.

3.3 Capital risk management

The Group's primary objectives when managing its capital position are:

- to safeguard its ability to continue as a going concern, so that it can continue to provide long-term growth and progressive dividend returns for shareholders;
- to provide an adequate return to the Group's shareholders by pricing its insurance products and services commensurately with the level of risk;
- the attainment of an efficient cost of capital; and
- to comply with all regulatory requirements by a significant margin.

The Group sets the amount of capital required in its funding structure in proportion to risk. The Group then manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to obtain or maintain an optimal capital structure the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares, assume debt, or sell assets to reduce debt.

The Group's activities are funded by a mixture of capital sources including issued equity share capital, retained earnings, Letters of Credit, bank debt and other third party insurance capital.

The Board ensures that the use and allocation of capital are given a primary focus in all significant operational actions. With that in mind, the Group has developed and embedded sophisticated capital modelling tools within its business. These join together short-term and long-term business plans and link divisional aspirations with the Group's overall strategy. The models provide the basis of the allocation of capital to different businesses and business lines, as well as the regulatory and rating agency capital processes.

There were no changes in the Group's approach to capital risk management during the current or prior year under review.

Gearing

The Group currently utilises short-to medium-term gearing as an additional source of funds to maximise the opportunities from strong markets and to reduce the risk profile of the business when the rating

environment shows a weaker model for the more volatile business.

The Group's gearing is obtained from a number of sources, including:

- Letters of Credit – in November 2005, the Group secured a £137.5 million facility from a syndicate of banks at a margin of 1.1%;
- term and revolving loan facility – also in November 2005, the Group secured a \$225 million facility at 1.3% margin of which \$182 million remains available;
- external Names – 27.4% of Syndicate 33's capacity is capitalised by third parties paying a profit share of approximately 17.5%;
- sidecar – in December 2006, Syndicate 33 entered into a limited tenancy quota share reinsurance arrangement with Panther Re, whose sole activity was to participate in the 2007 year property catastrophe reinsurance business of its only client, Syndicate 33. Panther Re was capitalised at \$360 million and all risks underwritten were fully collateralised;
- Cougar Syndicate at Lloyd's – with a capacity of £34.6 million, this syndicate is wholly backed by external members and will take a pure 2008 year of account quota share of Syndicate 33's international property catastrophe reinsurance account;
- gearing quota shares – historically the Group has used reinsurance capital to fund its capital requirement for short-term expansions in the volume of business underwritten by the Syndicate; and
- qualifying quota shares – these are reinsurance arrangements that allow the Group to increase the amount of premium it writes in hard markets.

The funds raised through Letters of Credit and loan facilities have been applied to support both the 2008 year of account for Syndicate 33 and the capital requirements of Hiscox Insurance Company (Bermuda) Limited, formed in 2005.

Financial strength

Standard & Poor's and A.M. Best's ratings of the financial strength of the Group's UK insurance company subsidiary, Hiscox Insurance Company Limited, remained at A- (Excellent) during the year. Similarly Hiscox Insurance Company (Bermuda) Limited and Hiscox Insurance Company (Guernsey) Limited retained their A- (Excellent) ratings from A.M. Best. Syndicate 33 benefits from an A.M. Best rating of A (Excellent) and the Lloyd's ratings of A (Excellent) from A.M. Best and A+ (Strong) from Standard & Poor's.

Capital performance

The Group's main capital performance measure is the achieved Return on Equity (ROE). This marker best aligns the aspirations of employees and shareholders. As variable remuneration, the vesting of options and longer-term investment plans all relate directly to ROE, this concept is embedded in the workings and culture of the Group. The Group maintains its cost of capital levels and its debt to overall equity ratios in line with others in the non-life insurance industry.

Capital modelling and regulation

The capital requirements of an insurance group are determined by its exposure to risk and the solvency criteria established by management and statutory regulations.

In 2005, the Financial Services Authority (FSA) and Lloyd's introduced a new capital regime that enables insurance companies the chance to calculate their own capital requirements through Individual Capital Assessments (ICA). Hiscox Insurance Company Limited and Syndicate 33 maintain ICA models in accordance with this regime. The models are concentrated specifically on the particular product lines, market conditions and risk appetite of each entity. If the FSA considers an ICA to be inadequate, it can require the entity to maintain an increased

3 Management of risk continued

3.3 Capital risk management continued

Capital modelling and regulation continued

capital safeguard. The Directors are also required to certify that the Group has complied, in all material aspects, with the provisions of the Interim Prudential Sourcebook: Insurers (IPRU(INS)), the Integrated Prudential Sourcebook for Insurers (INSPRU) and General Prudential Sourcebook (GENPRU) when completing the ICA return.

The Group used its own integrated modelling expertise to produce the ICA calculations. The results mirrored those driving the existing internal capital setting process.

The assessed capital requirement for the business placed through Hiscox Insurance Company Limited is driven by the level of resources necessary to maintain an A-rating. The Group's internal work on the ICA of Hiscox Insurance Company for regulatory purposes has produced results that also support the level of capital required by the rating agencies.

For Syndicate 33, the ICA process produces a result that is uplifted by Lloyd's to identify the capital required to hold the A rating. The strong control and risk management environment, together with the sophistication of the modelling, have produced a capital ratio below that suggested under the previous risk-based capital regime.

Another key area of capital modelling for Hiscox is to identify which insurance vehicle produces the best return on capital employed for the Group, given certain restraints from licences, reinsurance and the regulatory environment. This modelling takes into account transactional costs and tax, in addition to the necessary capital ratios. It proves the capital efficiency of Lloyd's, despite a tax disadvantage against offshore entities, and the cost advantage of processing smaller premium business outside of Lloyd's.

In addition to the ICA modelling process, the EU Insurance Group's Directive of 1998, as amended by the Financial Group's Directive (FGD), compels insurance companies that are members of a group to consider the solvency margin of their ultimate parent company. This consideration must refer to the surplus assets of the ultimate parent's related insurers, reinsurers, intermediate holding companies and other regulated entities.

The FGD has been applied in the UK through INSPRU and GENPRU. In accordance with these provisions, the parent company's solvency margin consideration became a minimum capital requirement for the Group from 31 December 2006 onwards. The estimated regulatory capital position of the Group under FGD at 31 December 2007 was a surplus of £536 million (2006: surplus of £435 million), which is calculated as below. The final regulatory capital position will be submitted to the FSA before 30 April 2008 in accordance with the required regulatory timetable.

In the Group's other geographical territories, including the USA, its subsidiaries underwriting insurance business are required to operate within broadly similar risk-based externally imposed capital requirements when accepting business.

Estimated Group capital position

At 31 December	2007 £m	2006 £m
Group capital resources	738	617
Group capital resources requirement	(202)	(182)
Surplus	536	435

Group capital resources are less than the Group's total equity value primarily as a result of the inadmissibility of certain assets including intangible assets for regulatory purposes.

4 Operating segments

The Group adopted IFRS 8 Operating Segments with effect from 1 January 2007. The Group also made minor changes to the structure of its internal organisation during the year under review. As a consequence of both events, minor changes have occurred in the identification of the Group's reportable segments from the prior year. Previously IAS 14 Segment Reporting (the predecessor standard to IFRS 8) resulted in the Group identifying and reporting disaggregated primary statement information for two sets of reportable segments, whose designation was based on the dissimilarity of risks and rewards in the Group's operations and geographical location. Segment information is now required to be presented with singular reference to the basis of those regular internal reports about the separate components of the Group that inform the chief operating decision maker and which are used in the assessment of financial performance and allocation of resources.

Management have identified the Group's operating segments in line with its internal organisation, which recognises the differences in products and services, customer groupings and geographical areas in addition to the discrete major legal entities of the Group.

The Group's four operating segments arising on the adoption of IFRS 8 are therefore identified as follows:

————— **Global Markets** comprises the results of Syndicate 33, excluding Syndicate 33's fine art, UK regional events coverage, non-US household business and underwriting result of Hiscox Inc. It includes the results of the larger retail TMT business written by Hiscox Insurance Company Limited.

————— **UK and Europe** comprises the results of Hiscox Insurance Company Limited, the results of Syndicate 33's fine art, UK regional events coverage and non-US household business, together with the income and expenses arising from the Group's retail agency activities in the UK and in continental Europe. It excludes the results of the larger retail TMT business written by Hiscox Insurance Company Limited.

————— **International** comprises the results of Hiscox Insurance Company (Guernsey) Limited, Hiscox Inc., Hiscox Insurance Company (Bermuda) Limited and the ALTOHA sub-group.

————— **Corporate Centre** comprises the investment return, finance costs and administrative costs associated with Group management activities. Corporate Centre forms a reportable segment due to its investment activities which earn significant external revenues.

The four reportable segments identified above, and the under noted financial information related thereto, differ from the three primary business segments disclosed in the prior year, in three main ways:

————— The Group's central functions are now separately identified as the 'Corporate Centre' segment, with a greater proportion of central revenues and expenses now being allocated to individual operating segments where appropriate. Previously all central revenues and expenses were included with the Global Markets business within a single segment. This is a change arising from the adoption of IFRS 8.

————— The Group's specie business, all of which is written in Syndicate 33, is now presented within the Global Markets segment and not within the UK and Europe segment as previously reported. This is a change arising from minor amendments made to the Group's internal organisation during the year.

————— The Global Markets segment also now includes all of the Group's larger TMT risks. In prior years, those risks underwritten by Hiscox Insurance Company Limited were reported in the UK and Europe segment.

4 Operating segments continued

This is a change arising from minor amendments made to the Group's internal organisation during the year. Information regarding the Group's operating segments is presented below. The comparative amounts for the prior year have been restated to conform to the requirements of IFRS 8. The comparative amounts have also been restated to reflect the re-classification of certain agency commissions and expenses outlined at note 2.2 above. All amounts reported below represent transactions with external parties only, with all inter-segment amounts eliminated. Performance is measured based on each reportable segments profit before tax.

(a) Profit before tax by segment

	Year to 31 December 2007					Year to 31 December 2006				
	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000
Gross premiums written	676,464	302,273	220,212	-	1,198,949	709,080	265,778	151,306	-	1,126,164
Net premiums written	524,683	265,001	185,226	-	974,910	603,562	234,414	137,421	-	975,397
Net premiums earned	552,205	248,348	164,637	-	965,190	567,490	227,865	93,473	-	888,828
Investment result including interest revenues*	46,617	18,343	23,915	10,802	99,677	33,123	19,327	16,449	36,651	105,550
Other revenues	11,996	2,672	1,216	3,160	19,044	6,878	4,931	421	3,462	15,692
Revenue	610,818	269,363	189,768	13,962	1,083,911	607,491	252,123	110,343	40,113	1,010,070
Claims and claim adjustment expenses, net of reinsurance	(246,876)	(115,032)	(61,457)	-	(423,365)	(271,120)	(95,317)	(15,904)	-	(382,341)
Expenses for the acquisition of insurance contracts	(157,718)	(65,423)	(41,429)	-	(264,570)	(145,458)	(62,861)	(27,478)	-	(235,797)
Administration expenses	(27,822)	(37,399)	(11,592)	-	(76,813)	(37,001)	(31,360)	(8,172)	-	(76,533)
Other expenses	(22,830)	(29,692)	(6,104)	(15,242)	(73,868)	(62,933)	(29,473)	(6,878)	(5,659)	(104,943)
Total expenses	(455,246)	(247,546)	(120,582)	(15,242)	(838,616)	(516,512)	(219,011)	(58,432)	(5,659)	(799,614)
Results of operating activities	155,572	21,817	69,186	(1,280)	245,295	90,979	33,112	51,911	34,454	210,456
Finance costs including interest expense	-	-	(82)	(8,095)	(8,177)	(312)	-	(36)	(9,056)	(9,404)
Share of profit of associates after tax	-	-	-	81	81	-	-	-	10	10
Profit before tax	155,572	21,817	69,104	(9,294)	237,199	90,667	33,112	51,875	25,408	201,062

*Interest revenues total £85,435,000 (2006: £68,644,000).

The following charges are included within the consolidated income statement:

	Year to 31 December 2007					Year to 31 December 2006				
	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000
Depreciation	975	3,303	599	40	4,917	1,412	2,276	170	40	3,898
Amortisation of intangible assets	40	137	41	5	223	40	135	-	12	187

The Group's wholly owned subsidiary, Hiscox Syndicates Limited, oversees the operation of Syndicate 33 at Lloyd's. The Group's percentage participation in Syndicate 33 can fluctuate from year to year and consequently, presentation of the results at the 100% level removes any distortions arising therefrom.

100% ratio analysis	Year to 31 December 2007					Year to 31 December 2006				
	Global Markets	UK and Europe	International	Corporate Centre	Total	Global Markets	UK and Europe	International	Corporate Centre	Total
Claims ratio (%)	44.3	45.6	40.1	-	44.0	55.7	41.3	17.5	-	49.3
Expense ratio (%)	37.4	52.6	35.3	-	40.4	34.4	54.9	45.2	-	39.8
Combined ratio (%)	81.7	98.2	75.4	-	84.4	90.1	96.2	62.7	-	89.1

In calculating the claims and expense ratios the Group has applied an estimated allocation of the foreign exchange gains and losses to each category. The impact on profit before tax of a 1% change in each component of the segmental combined ratios is:

	Year to 31 December 2007					Year to 31 December 2006				
	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000
At 100% level (note 4b)										
1% change in claims or expense ratio			7,660	2,598	1,695	-	7,865	2,400	948	-
At Group level										
1% change in claims or expense ratio			5,522	2,483	1,646	-	5,675	2,279	935	-

4 Operating segments continued

(b) 100% operating result by segment

	Year to 31 December 2007					Year to 31 December 2006				
	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000
Gross premiums written	932,251	316,017	227,576	-	1,475,844	971,174	281,038	154,999	-	1,407,211
Net premiums written	722,209	276,967	191,219	-	1,190,395	827,424	247,891	141,114	-	1,216,429
Net premiums earned	765,959	259,841	169,465	-	1,195,265	786,471	240,039	94,794	-	1,121,304
Investment result	64,552	19,161	23,915	10,802	118,430	54,207	19,886	16,449	36,651	127,193
Other revenues	2,665	2,672	500	3,160	8,997	-	4,931	1,480	3,462	9,873
Claim and claim adjustment expenses, net of reinsurance	(345,318)	(118,418)	(67,938)	-	(531,674)	(377,006)	(99,047)	(16,597)	-	(492,650)
Expenses for the acquisition of insurance contracts	(222,965)	(69,428)	(42,375)	-	(334,768)	(204,579)	(67,259)	(27,763)	-	(299,601)
Administration expenses	(34,640)	(38,079)	(11,913)	-	(84,632)	(43,798)	(31,872)	(8,172)	-	(83,842)
Other expenses	(22,858)	(29,350)	(5,596)	(15,242)	(73,046)	(83,135)	(32,783)	(6,878)	(5,659)	(128,455)
Results of operating activities	207,395	26,399	66,058	(1,280)	298,572	132,160	33,895	53,313	34,454	253,822

Segment results at the 100% level presented above differ from those presented at the Group's share at note 4(a) solely as a result of the Group not owning 100% of the capacity of Syndicate 33 at Lloyd's.

(c) Segmental analysis of assets and liabilities

The segment assets and liabilities at 31 December and the capital expenditure for the year then ended are as follows:

	31 December 2007					Total £000
	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Intragroup items and eliminations £000	
Financial assets	954,701	271,572	385,091	137,965	-	1,749,329
Reinsurance assets	162,516	102,137	28,691	-	(13,256)	280,088
Intangible assets	25,275	2,985	7,543	4,649	-	40,452
Deferred acquisition costs	56,231	36,087	24,792	-	5,971	123,081
Other assets	456,515	248,366	222,796	658,318	(878,653)	707,342
Total assets	1,655,238	661,147	668,913	800,932	(885,938)	2,900,292
Insurance liabilities	1,081,287	407,332	229,481	-	(4,213)	1,713,887
Other liabilities	419,549	166,858	51,859	158,760	(434,926)	362,100
Total liabilities	1,500,836	574,190	281,340	158,760	(439,139)	2,075,987
Capital expenditure	9,409	190	3,375	167		13,141

	31 December 2006					Total £000
	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Intragroup items and eliminations £000	
Financial assets	746,900	328,871	16,848	149,319	-	1,241,938
Reinsurance assets	237,165	78,929	4,679	-	(18,001)	302,772
Intangible assets	25,315	3,120	-	4,777	-	33,212
Deferred acquisition costs	68,895	29,225	20,414	-	(1,419)	117,115
Other assets	497,321	152,693	380,751	504,007	(571,808)	962,964
Total assets	1,575,596	592,838	422,692	658,103	(591,228)	2,658,001
Insurance liabilities	1,167,765	354,720	89,617	-	(18,001)	1,594,101
Other liabilities	323,279	158,832	16,486	127,139	(243,921)	381,815
Total liabilities	1,491,044	513,552	106,103	127,139	(261,922)	1,975,916
Capital expenditure	4,330	230	1,159	231		5,950

Segment assets and liabilities primarily consist of operating assets and liabilities, which represent the majority of the balance sheet. Intragroup assets and liabilities that cross segments are presented under the separate category heading 'Intragroup items and eliminations'.

Capital expenditure comprises expenditure on intangible assets (note 14) other than goodwill, and additions to property, plant and equipment (note 15), but excluding assets acquired on business combinations.

(d) Geographical information

The Group's operational segments underwrite business from locations in the UK and Ireland, and also through its branch network in Guernsey, France, Germany, Belgium, the Netherlands, Spain, Portugal and Sweden. In addition, the Group commenced underwriting and agency operations in Bermuda and the USA in 2006.

4 Operating segments continued

(d) Geographical information continued

The following table provides an analysis of the Group's gross premium revenues earned by material geographical location of external parties:

Gross premium revenues earned from external parties	Year to 31 December 2007					Year to 31 December 2006				
	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000	Global Markets £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000
UK and Ireland	85,441	202,703	9,095	-	297,239	99,006	183,834	5,361	-	288,201
Europe	69,956	77,171	19,913	-	167,040	82,129	64,459	11,518	-	158,106
United States	310,892	2,006	101,485	-	414,383	347,000	3,774	48,565	-	399,339
Rest of World	234,808	3,924	62,050	-	300,782	137,369	4,703	45,867	-	187,939
	701,097	285,804	192,543	-	1,179,444	665,504	256,770	111,311	-	1,033,585

The Group's largest external policyholder contributed less than 2% of total gross Group premium revenues earned and the details thereof are not disclosed on the grounds of materiality.

The Group has not reported segmental details of non-current assets excluding financial instruments and including loans and receivables, rights and obligations under insurance and reinsurance contracts, investments in associates and subsidiaries on the grounds of the relevance of these items to the Group's operations and the usefulness of such information to users.

5 Net asset value per share

	2007		2006	
	Net asset value (total equity) £000	NAV per share pence	Net asset value (total equity) £000	NAV per share pence
Net asset value	824,304	209.5	682,085	173.2
Net tangible asset value	783,852	199.3	648,873	164.8

The net asset value per share is based on 393,386,041 shares (2006: 393,725,396), being the adjusted number of shares in issue at 31 December.

There is no impact on the comparative amount for the application of reverse acquisition accounting in the prior year (note 2.3).

6 Investment result

The total result for the Group before taxation comprises:

	2007 £000	2006 £000
Investment income including interest receivable	90,259	75,526
Net realised gains/(losses) on financial investments at fair value through profit or loss	10,105	(5,731)
Net fair value gains on financial investments at fair value through profit or loss	423	8,721
Return on financial investments and financial liabilities (note 7)	100,787	78,516
Fair value gains/(losses) on derivative instruments and borrowings	(1,110)	27,034
Total result	99,677	105,550

Investment expenses are presented within other expenses (note 9).

7 Analysis of return on investments

The return on investments for the year by currency was:

	2007 %	2006 %
Sterling	4.9	5.4
US Dollar	5.5	4.8
Other	3.6	2.2

The return on financial investments and financial liabilities by asset class for the year was:

	Global Markets		UK and Europe		International		Corporate Centre		2007 Total	
	£000	%	£000	%	£000	%	£000	%	£000	%
Debt and fixed income securities	43,802	5.2	9,599	5.6	11,553	6.1	5,734	6.1	70,688	5.5
Equities and shares in unit trusts	-	-	1,131	1.3	2,181	9.1	3,647	6.4	6,959	4.1
Deposits with credit institutions/cash and cash equivalents	2,815	4.9	7,613	5.5	10,181	5.2	2,531	6.5	23,140	5.4
	46,617	5.2	18,343	4.6	23,915	5.9	11,912	6.3	100,787	5.4

7 Analysis of return on investments continued

	Global Markets		UK and Europe		International		Corporate Centre		2006 Total	
	£000	%	£000	%	£000	%	£000	%	£000	%
Debt and fixed income securities	30,518	4.2	7,601	3.3	323	2.6	3,653	4.0	42,095	4.0
Equities and shares in unit trusts	194	9.9	6,994	9.9	1,014	17.6	5,315	10.4	13,517	10.6
Deposits with credit institutions/cash and cash equivalents	2,411	3.8	4,732	4.2	15,112	4.9	649	3.9	22,904	4.6
	33,123	4.2	19,327	4.6	16,449	5.1	9,617	5.8	78,516	4.6

8 Deferred acquisition costs

	2007			2006		
	Gross £000	Reinsurance £000	Net £000	Gross £000	Reinsurance £000	Net £000
Balance deferred at 1 January	117,115	(6,529)	110,586	106,747	(2,496)	104,251
Acquisition costs incurred in relation to insurance contracts written	284,071	(12,645)	271,426	253,271	(11,139)	242,132
Acquisition costs expensed to the income statement	(278,105)	13,535	(264,570)	(242,303)	7,106	(235,797)
Balance deferred at 31 December	123,081	(5,639)	117,442	117,115	(6,529)	110,586

The deferred amount of insurance contract acquisition costs attributable to reinsurers of £5,639,000 (2006: £6,529,000) is not eligible for offset against the gross balance sheet asset and is included separately within trade and other payables (note 25).

The amounts expected to be recovered before and after one year are estimated as follows:

	2007 £000	2006 £000
Within one year	117,442	110,586
After one year	–	–
	117,442	110,586

9 Other revenues and expenses

	Note	2007 £000	2006 £000
Agency related income		4,626	4,861
Profit commission		10,468	5,332
Other income		3,950	5,499
Other revenues		19,044	15,692
Managing agency expenses		28,870	17,258
Overseas underwriting agency expenses		23,811	22,033
Connect agency expenses		14,492	12,547
Net foreign exchange (gains)/losses	13	(8,401)	38,354
Investment expenses		1,250	1,306
Other Group expenses including depreciation and amortisation	14, 15	13,846	13,445
Other expenses		73,868	104,943

10 Employee benefit expense

The aggregate remuneration and associated costs were:

	Note	2007 £000	2006 £000
Wages and salaries, including holiday pay and sabbatical leave charges		68,135	58,568
Social security costs		8,909	7,512
Share based payments cost of options granted to Directors and employees	22	5,689	5,238
Pension costs – defined contribution		7,256	1,689
Pension costs – net expense/(credit) arising on defined benefit schemes	28	(3,801)	12,180
		86,188	85,187

The average monthly number of staff employed by the Group was 804 (2006: 637) comprising 301 underwriting and 503 administrative staff (2006: 270 and 367 respectively). Of the total remuneration shown above, an amount of £19,838,000 (2006: £20,780,000) was recharged to the syndicate managed by Hiscox Syndicates Limited.

11 Finance costs

	Note	2007 £000	2006 £000
Interest and expenses associated with bank borrowings carried at fair value	18	6,278	7,325
Interest and charges associated with Letters of Credit	33	1,845	2,038
Interest charges arising on finance leases		54	41
		8,177	9,404

12 Auditors' remuneration

Fees payable to the Group's main external auditor KPMG, its member firms and its associates (exclusive of VAT) include the following amounts recorded in the consolidated income statement:

Group	2007 £000	2006 £000
Fees payable to the Company's auditor for the audit of the Group's consolidated financial statements	201	110
Fees payable to the Company's auditor and its associates for other services:		
The audit of subsidiaries pursuant to legislation	345	321
Other services pursuant to legislation	50	30
All other services*	93	307
	689	768
Fees in respect of the defined benefit pension scheme:		
Audit	12	9
Total auditors' remuneration expense	701	777

*Other fees relate primarily to corporate advisory and financial reporting consulting services (2006: Group's Scheme of Arrangement and the listing of Hiscox Ltd on the London Stock Exchange). Non-audit services with fees greater than £50,000 must be pre-approved by the Audit Committee which is composed solely of independent Non Executive Directors.

The full audit fee payable for the Syndicate audit has been included above, although an element of this is borne by the third party participants in the Syndicate.

Fees payable to other external auditors in respect of the Company's subsidiaries in the United States pursuant to legislation during 2007 were £51,000 (2006: £nil).

13 Net foreign exchange gains/(losses)

The net foreign exchange gains/(losses) for the year include the following amounts:

	2007 £000	2006 £000
Exchange gains/(losses) recognised in the consolidated income statement	8,401	(38,354)
Exchange losses classified as a separate component of equity**	(2,869)	(41,218)

This excludes profits or losses on foreign exchange derivative contracts which are included within the investment result and are outlined in note 20.

Overall impact of foreign exchange related items

	Note	2007 £000	2006 £000
Consolidated income statement			
Derivative gains/(losses) on foreign exchange contracts included within investment return	6, 20	(1,110)	27,034
Unearned premiums and deferred acquisition costs adjustment		14,438	(25,511)
Foreign exchange gains on borrowings for economic hedging of Hiscox Insurance Company (Bermuda) Limited		-	14,121
Other foreign exchange losses		(6,037)	(26,964)
		8,401	(38,354)
Impact of foreign exchange related items on consolidated income statement		7,291	(11,320)

**Foreign exchange differences recognised directly in equity during 2007 include £1,400,000 of losses arising on the retranslation of a portion of the Group's net investment in its Bermudian and Guernsey subsidiaries, which are entirely offset by corresponding gains of the same amount on the retranslation of certain foreign currency borrowings designated for hedge accounting (2006: £nil recognised in equity on foreign currency borrowings). Further details are provided at note 18 to these financial statements.

14 Intangible assets

	Goodwill £000	Syndicate capacity £000	State authorisation licences £000	Other £000	Total £000
At 1 January 2006					
Cost	8,547	24,505	–	2,670	35,722
Accumulated amortisation and impairment	(2,442)	–	–	(181)	(2,623)
Net book amount	6,105	24,505	–	2,489	33,099
Year ended 31 December 2006					
Opening net book amount	6,105	24,505	–	2,489	33,099
Other additions	–	–	–	300	300
Amortisation and impairment charge	–	–	–	(187)	(187)
Closing net book amount	6,105	24,505	–	2,602	33,212
At 31 December 2006					
Cost	8,547	24,505	–	2,970	36,022
Accumulated amortisation and impairment	(2,442)	–	–	(368)	(2,810)
Net book amount	6,105	24,505	–	2,602	33,212
Year ended 31 December 2007					
Opening net book amount	6,105	24,505	–	2,602	33,212
Additions in year on business combinations	–	–	5,083	–	5,083
Other additions	–	–	–	2,500	2,500
Disposal on sale of subsidiary	(39)	–	–	(81)	(120)
Amortisation charges	–	–	–	(223)	(223)
Closing net book amount	6,066	24,505	5,083	4,798	40,452
At 31 December 2007					
Cost	8,496	24,505	5,083	5,361	43,445
Accumulated amortisation and impairment	(2,430)	–	–	(563)	(2,993)
Net book amount	6,066	24,505	5,083	4,798	40,452

The Group's intangible asset relating to syndicate capacity has been allocated, for impairment testing purposes, to one individual cash generating unit being the active Lloyd's corporate member entity. The Group has considered the recoverable amount from the active Lloyd's corporate member entity on a value in use basis. This calculation uses cash flow projections based on financial forecasts approved by management covering a five-year period. Cash flows beyond the five-year period are extrapolated based on an average level of return and annual growth estimated at 2% consistent with the industry long term average. A pre-tax discount factor of 7% has been applied to projected cash flows as part of the exercise. The results of this exercise indicate that the recoverable amount exceeds the intangible's carrying value. The Group's weighted average cost recognised on the balance sheet is approximately 10 Pence per Pound of syndicate capacity held, which is significantly below the average open market price of 26 Pence per Pound witnessed in the recent Lloyd's of London Syndicate 33 capacity auctions in Autumn 2007.

The Group has recognised intangible assets of £5,083,000 relating to insurance authorisation licences for 50 US states acquired in the business combination of ALTOHA Inc. (note 31). This intangible asset has been allocated for impairment testing purposes to one individual cash generating unit being the Group's North American underwriting businesses. The Group has considered the recoverable amount of this cash generating unit on a consistent basis to the active Lloyd's corporate member entity outlined above.

Other intangibles primarily relate to the costs of acquiring rights to customer contractual relationships, and at 31 December 2006 also included a limited level of capitalised software costs. The additions during 2006 primarily comprised the Group's acquisition of the customer relationships of Global Flying Insurance Services. The additions during 2007 primarily relate to the costs of acquiring rights to customer contractual relationships held previously by AON Limited.

The amortisation charge for the year includes £40,000 (2006: £40,000) relating to capitalised software costs. The net book value of capitalised software costs at 31 December 2007 was £nil (2006: £40,000). There are no charges for impairment during the current or prior financial year.

The Group had no internally generated intangible assets at 31 December 2007 (2006: £nil).

Goodwill is allocated to the Group's cash generating units ('CGUs') identified according to country of operation and business segment.

At 31 December 2007 and 2006 the Group's goodwill net book amount is all attributable to UK based operations.

15 Property, plant and equipment

	Land and buildings £000	Leasehold improvements £000	Vehicles £000	Furniture, fittings and equipment and art £000	Total £000
At 1 January 2006					
Cost	2,985	6	647	24,925	28,563
Accumulated depreciation	(80)	–	(171)	(16,184)	(16,435)
Net book amount	2,905	6	476	8,741	12,128
Year ended 31 December 2006					
Opening net book amount	2,905	6	476	8,741	12,128
Additions	–	508	169	4,973	5,650
Disposals	–	–	(55)	(4)	(59)
Depreciation charge	(40)	(78)	(125)	(3,655)	(3,898)
Closing net book amount	2,865	436	465	10,055	13,821
At 31 December 2006					
Cost	2,985	514	679	29,894	34,072
Accumulated depreciation	(120)	(78)	(214)	(19,839)	(20,251)
Net book amount	2,865	436	465	10,055	13,821
Year ended 31 December 2007					
Opening net book amount	2,865	436	465	10,055	13,821
Additions	–	262	260	10,119	10,641
Additions on business combinations	–	99	18	10	127
Disposals	–	–	(31)	(263)	(294)
Depreciation charge	(40)	(132)	(116)	(4,629)	(4,917)
Closing net book amount	2,825	665	596	15,292	19,378
At 31 December 2007					
Cost	2,985	1,044	896	34,978	39,903
Accumulated depreciation	(160)	(379)	(300)	(19,686)	(20,525)
Net book amount	2,825	665	596	15,292	19,378

The Group's land and buildings assets relate to freehold property in the United Kingdom. At 31 December 2006 part of the buildings were occupied by third parties under separate operating lease arrangements (note 34).

Assets with a net book value of £510,000 were held under finance leases (2006: £465,000). The total depreciation charge for the year in respect of assets held under finance leases was £106,000 (2006: £125,000).

At 31 December 2007 there were £2,336,000 of assets under construction, upon which no depreciation has yet been charged (2006: £nil).

16 Investments in associates

	2007 £000	2006 £000
Year ended 31 December		
At beginning of year	28	18
Additions during the year	1,393	–
Share of post-tax profit recognised for the period	81	10
At end of year	1,502	28

The Group's interests in its principal associates, all of which are unlisted, were as follows:

Name	% interest held at 31 December	Country of incorporation	Entity 100% pro-forma information for year ended 31 December 2007			
			Assets £000	Liabilities £000	Revenues £000	Profit £000
Blyth Valley Ltd	25.2	UK	192	83	784	40
Total at the end of 2006			192	83	784	40
Blyth Valley Ltd	25.2	UK	565	179	1,325	192
Plexstar Insurance Services Limited	49.0	UK	769	579	573	98
Barta & Partner GmbH	25.0	Austria	1,232	1,074	1,064	310
HIM Capital Holdings Ltd	40.0	UK	300	–	–	–
Total at the end of 2007			2,866	1,832	2,962	600

16 Investments in associates continued

The additions during the current year relate to equity investments made in Plexstar Insurance Services Limited, Barta & Partner GmbH and HIM Capital Holdings Ltd. Cash consideration of £1,273,000 was paid.

The equity interests held by the Group in respect of associates do not have quoted market prices and are not traded regularly in any active recognised market. The associates concerned have no material impact on the results or assets of the Group. No impairments were identified during the current or prior financial year under review.

17 Reinsurance assets

	Note	2007 £000	2006 £000
Reinsurers' share of insurance liabilities		283,414	306,550
Provision for non-recovery and impairment		(3,326)	(3,778)
Reinsurance assets	24	280,088	302,772

The amounts expected to be recovered before and after one year, based on historical experience, are estimated as follows:

Within one year	147,987	136,790
After one year	132,101	165,982
	280,088	302,772

Amounts due from reinsurers in respect of outstanding premiums and claims already paid by the Group are included in loans and receivables (note 19). The Group recognised a gain during the year of £452,000 (2006: £4,094,000) in respect of impaired balances.

18 Financial assets and liabilities carried at fair value

Financial assets and liabilities are measured at their bid price fair values and ask price fair values respectively, with all changes from one accounting period to the next being recorded through the income statement, except in the case of unlisted equity investments, and borrowing instruments that formed part of a designated hedge accounting relationship from 1 January 2007 as provided for by IAS 39.

	Note	2007 Cost £000	2007 Fair value £000	2006 Cost £000	2006 Fair value £000
Debt and fixed income securities		1,435,373	1,444,532	1,046,009	1,043,669
Equities and shares in unit trusts		135,427	159,421	117,457	141,841
Deposits with credit institutions		143,852	143,874	54,800	54,715
Total investments		1,714,652	1,747,827	1,218,266	1,240,225
Derivative instrument assets	20	-	-	-	1,685
Total financial investments at fair value through profit or loss		1,714,652	1,747,827	1,218,266	1,241,910
	Note	2007 Cost £000	2007 Fair value £000	2006 Cost £000	2006 Fair value £000
Borrowings from credit institutions (see below)		91,457	91,764	92,857	92,852
Derivative instrument liabilities	20	-	-	-	1,077
Total financial liabilities at fair value through profit or loss		91,457	91,764	92,857	93,929

An analysis of the credit risk and contractual maturity profiles of the Group's debt and fixed income securities is given in notes 3.2(c) and 3.2(d). The Group has no material exposure to financial assets not actively traded on recognised markets.

The Group's borrowings from credit institutions at 31 December 2006 and 2007 are denominated in US Dollars, half fall due for repayment in 2008 and half fall due for repayment in 2009. The movement in fair value of financial liabilities during 2007 includes no net principal repayments, £1,400,000 of foreign exchange gains recognised directly in equity (see note 13 and below) and £302,000 of fair value losses (2006: £14,212,000 of net principal repayments, £14,121,000 of foreign exchange gains and £5,000 of fair value gains). The amounts recognised as fair value gains and losses are attributable to changes in applicable benchmark interest rates.

The amount of financial liabilities payable on maturity is not materially different to the cost disclosed above.

Included in financial liabilities at 31 December 2007 are foreign currency borrowings from credit institutions totalling US\$182,000,000 (2006: US\$nil) that were designated as a hedging instrument in a net investment hedge relationship. The hedged item was the foreign currency spot retranslation risk associated with the first US\$182,000,000 of the Group's net investment in its Bermudian and Guernsey subsidiaries. The hedging relationship commenced on 3 January 2007 and was entirely effective throughout the entire period up until the balance sheet date. Investments at 31 December are denominated in the following currencies at their fair value:

18 Financial assets and liabilities carried at fair value continued

	2007 £000	2006 £000
Debt and fixed income securities		
Sterling	206,357	308,914
US Dollars	1,038,412	552,015
Euro and other currencies	199,763	182,740
	1,444,532	1,043,669
Equities and shares in unit trusts		
Sterling	102,196	114,530
US Dollars	51,148	26,328
Euro and other currencies	6,077	983
	159,421	141,841
Deposits with credit institutions		
Sterling	95,541	54,715
US Dollars	48,333	–
Euro and other currencies	–	–
	143,874	54,715
Total investments	1,747,827	1,240,225

The table below illustrates the movements in financial assets during the year:

	2007 £000	2006 £000
At 1 January	1,240,225	1,237,778
Net additions/(disposals) into investment portfolio	507,179	(6,274)
Net fair value gains	423	8,721
At 31 December	1,747,827	1,240,225

19 Loans and receivables including insurance receivables

	Note	2007 £000	2006 £000
Gross receivables arising from insurance and reinsurance contracts		329,156	356,354
Less provision for impairment		(1,392)	(875)
Net receivables arising from insurance and reinsurance contracts		327,764	355,479
Due from contract holders, brokers, agents and intermediaries		201,157	280,694
Due from reinsurance operations		126,607	74,785
		327,764	355,479
Prepayments and accrued income		9,562	6,746
Other loans and receivables:			
Net profit commission receivable		13,850	14,443
Accrued interest		9,003	6,065
Right to reimbursement of defined benefit obligation	28	–	1,163
Share of Syndicate's other debtors' balances		12,705	44,316
Other debtors including related party amounts		12,338	18,060
Total loans and receivables including insurance receivables		385,222	446,272

The amounts expected to be recovered before and after one year are estimated as follows:

Within one year	381,639	446,272
After one year	3,583	–
	385,222	446,272

There is no significant concentration of credit risk with respect to loans and receivables, as the Group has a large number of internationally dispersed debtors. The Group has recognised a loss of £517,000 (2006: gain of £143,000) for the impairment (and subsequent recovery) of receivables during the year ended 31 December 2007.

20 Derivative financial instruments

Derivative financial instruments are used on occasion to hedge certain economic relationships including the foreign exchange volatility arising from translating the net investments in, and results of, subsidiary companies with different functional currencies, and the foreign exchange impact of insurance business dominated in foreign currencies. During the current and prior financial year, the Group has not elected to denominate any derivative contracts as formal hedging instruments and, as a consequence, has not applied the hedge accounting provisions of IAS 39 in respect of these contracts.

At 31 December 2007 the Group had no derivative exposure on foreign exchange cylinder option contracts (2006: financial asset with net fair value of £1,685,000). The Group recognised gains totalling £317,000 in respect of these contracts in the current year (2006: gain of £6,577,000). No expenses or charges were incurred in the acquisition of the derivative contracts (2006: £nil).

The Group also entered into conventional foreign exchange forward and option contracts during the current and prior year primarily in order to manage the net investment in the Bermudian operation and currency exposures related to the proceeds raised from the Rights Issue. The contract outstanding at the prior balance sheet date required the Group to sell US \$293,000,000 at an agreed future rate to Pound Sterling at a fixed date within one year of the balance sheet date. At 31 December 2007, this contract had been closed out and a gain recognised of £732,000. Other contracts opened and closed during the current year resulted in a loss of £2,159,000 being recognised. The Group had no outstanding derivative exposures at 31 December 2007.

	2007			2006		
	Contract notional amounts \$000	Fair value of assets £000	Fair value of liabilities £000	Contract notional amounts \$000	Fair value of assets £000	Fair value of liabilities £000
Foreign exchange cylinder option contracts expiring:						
Within one year	-	-	-	50,000	1,700	15
Between one and five years	-	-	-	-	-	-
Total at 31 December	-	-	-	50,000	1,700	15
Foreign exchange forward contract expiring:						
Within one year	-	-	-	293,000	-	1,077
Total at 31 December	-	-	-	293,000	-	1,077

The Group had the right and intention to settle all contracts on a net basis at 31 December 2006. Consequently, only the net balance was recognised in the 2006 balance sheet as detailed in note 18.

21 Cash and cash equivalents

	2007 £000	2006 £000
Cash at bank and in hand	236,417	142,200
Short-term bank deposits	66,325	360,671
	302,742	502,871

22 Share capital

Group	31 December 2007		31 December 2006	
	Number of shares	Share capital £000	Number of shares	Share capital £000
Issued share capital	397,938,305	19,898	393,915,738	19,694

The amounts presented in the equity structure of the Group above relate to Hiscox Ltd, the legal parent Company.

In accordance with the reverse acquisition provisions of IFRS 3 Business Combinations, the amount of issued share capital included in the consolidated balance sheet reflects that of Hiscox plc, the Group's former legal parent company, up until the date of the reverse acquisition on 12 December 2006 together with that issued subsequently by Hiscox Ltd, the new legal parent, up until each respective balance sheet date.

Changes in Group share capital	Note	Ordinary share capital £000	Share premium £000	Contributed surplus £000
At 1 January 2006		19,570	401,365	-
Employee share option scheme – proceeds from shares issued		124	2,829	264
Transfers on reverse acquisition	2.3	-	(404,194)	442,161
At 31 December 2006		19,694	-	442,425
Employee share option scheme – proceeds from shares issued		204	4,955	-
Dividends to shareholders		-	-	(43,591)
At 31 December 2007		19,898	4,955	398,834

22 Share capital continued

In accordance with Bermuda law, an amount of £442,161,000 was reclassified as contributed surplus on completion of the reverse acquisition of Hiscox Ltd. Included in this amount are balances of £4,723,000 and £33,244,000 relating to the previously reported merger reserve and capital redemption reserve respectively.

Equity structure of Hiscox Ltd	Number of 5p ordinary shares in issue (thousands) 2007	Number of 5p ordinary shares in issue (thousands) 2006
At 1 January	393,916	–
Issue of ordinary shares to original subscriber at par value on incorporation	–	140
Issue of ordinary shares on scheme of arrangement	–	393,707
Employee share option scheme – ordinary shares issued	4,022	209
Redemption of subscriber's shares	–	(140)
At 31 December	397,938	393,916

At the date of incorporation of the Company (6 September 2006) the authorised share capital of £7,000 comprised 140,000 ordinary shares of 5p each. On 21 September 2006 the authorised share capital was increased to £30,000,000 comprising 600,000,000 ordinary shares of 5p each. No further changes occurred during the current year under review.

The redemption of the original subscriber's shares was at par value.

393,707,089 shares were issued at fair value to the members of Hiscox plc on 12 December 2006 in consideration for the cancellation of their shareholdings in that company.

All issued shares are fully paid.

Share options and performance share plan awards

Share options and performance share plan awards are granted to Directors and to senior employees. The exercise price of the granted options is equal to the closing mid-market price of the shares on the day before the date of the grant. No exercise price is attached to performance plan awards, although their attainment is conditional on the employee completing three year's service (the vesting period) and the Group achieving targeted levels of returns on equity. Share options are also conditional on the employee completing three years' service (the vesting period) or under exceptional circumstances (death, disability, retirement or redundancy). The options are exercisable starting three years from the grant date only if the Group achieves its targets of profitability; the options have a contractual option term of ten years. The Group has no legal or constructive obligation to re-purchase or settle the options in cash.

In accordance with IFRS 2 the Group recognises an expense for the fair value of share option and performance share plan award instruments issued to employees, over their vesting period through the income statement. The expense recognised in the Consolidated Income Statement during the year was £5,689,000 (2006: £5,238,000). This comprises charges of £4,352,000 (2006: £2,828,000) in respect of performance share plan awards and £1,337,000 (2006: £2,410,000) in respect of share option awards. The amount expensed in the prior year includes £930,000 in respect of modification arising in January 2006, pursuant to the Group's Rights Issue in November 2005. The Group has applied the principles outlined in the Black-Scholes option pricing model when determining the fair value of each share option instrument and discounted cash flow methodology in respect of performance share plan awards. The forfeiture of expected dividends during the vesting period was taken into account when determining the fair value measurement of performance share plan awards.

The range of principal Group assumptions applied in determining the fair value of share based payment instruments granted during the year under review are:

Assumptions affecting inputs to fair value models	2007	2006
Annual risk free rates of return and discount rates (%)	5.5	3.5-5.0
Long-term dividend yield (%)	4.75	2.0-4.0
Expected life of options (years)	3.25	3.25-7.5
Implied volatility of share price (%)	26	32-49
Weighted average share price (p)	268.5	149.5

The weighted average fair value of each share option granted during the year was 67.9p (2006: 95.9p). The weighted average fair value of each performance share plan award granted during the year was 232.8p (2006: 210.0p).

Movements in the number of share options during the year and details of the balances outstanding at 31 December 2007 are shown in the Directors' remuneration report.

The implied volatility assumption is based on historical data for periods of between five and ten years immediately preceding grant date.

For options issued after 1 January 2006 the assumptions regarding long-term dividend yield have been aligned to the progressive dividend policy announced during the 2005 Rights Issue.

Additional details on the Group's share option schemes are shown in the Directors' remuneration report accompanying these financial statements.

23 Retained earnings and other reserves

	2007 £000	2006 £000
Currency translation reserve	(43,265)	(40,396)
Total other reserves at 31 December	(43,265)	(40,396)
Retained earnings at 31 December	443,882	260,362

The currency translation reserve comprises foreign exchange differences arising from the translation of the financial statements of, and investments in, foreign operations.

4,365,305 ordinary shares of 5p each were purchased by Hiscox Ltd in open market transactions during the current year (2006: nil) and are held in treasury. Retained earnings have been reduced by £11,343,000 being the consideration paid. Included within this amount are transaction cost expenses of £23,000 directly related to the purchases.

The highest price paid per share was 265p, the lowest price paid was 247.75p and the average price paid was 259.4p per share. At 31 December 2007 Hiscox Ltd held 4,365,305 shares in treasury. Additional details are shown in note 35 to these financial statements in respect of additional Hiscox Ltd shares held by subsidiaries.

Included within Group retained earnings is an amount of £21,578,000 (2006: £20,578,000), which is not distributable and is held to meet solvency capital requirements to maintain an equalisation provision. The amounts in the equalisation provision are realised when particular entities in the Group have suffered insurance losses in excess of levels set out in the relevant solvency capital regulations.

24 Insurance liabilities and reinsurance assets

	Note	2007 £000	2006 £000
Gross			
Claims reported and loss adjustment expenses		642,252	703,159
Claims incurred but not reported		573,635	425,170
Unearned premiums		498,000	465,772
Total insurance liabilities, gross		1,713,887	1,594,101
Recoverable from reinsurers			
Claims reported and loss adjustment expenses		137,868	214,148
Claims incurred but not reported		84,804	50,925
Unearned premiums		57,416	37,699
Total reinsurers' share of insurance liabilities	17	280,088	302,772
Net			
Claims reported and loss adjustment expenses		504,384	489,011
Claims incurred but not reported		488,831	374,245
Unearned premiums		440,584	428,073
Total insurance liabilities, net		1,433,799	1,291,329

The amounts expected to be recovered and settled before and after one year, based on historical experience, are estimated as follows:

Within one year	844,570	685,409
After one year	589,229	605,920
	1,433,799	1,291,329

The gross claims reported, the loss adjustment expenses liabilities and the liability for claims incurred but not reported are net of expected recoveries from salvage and subrogation. The amounts for salvage and subrogation at the end of 2007 and 2006 are not material.

24.1 Insurance contracts assumptions

(a) Process used to decide on assumptions

The risks associated with insurance contracts and in particular with casualty insurance contracts are complex and subject to a number of variables that complicate quantitative sensitivity analysis.

For all risks, the Group uses several statistical methods to incorporate the various assumptions made in order to estimate the ultimate cost of claims. The reserves for outstanding claims are actuarially estimated primarily by using both the Chain Ladder and Bornhuetter-Ferguson methods. There is close communication between the actuaries involved in the estimation process and the Group's underwriters to ensure that, when applying both estimation techniques, both parties are cognisant of all material factors relating to outstanding claims, and allowance is also made for the rating environment.

24 Insurance liabilities and reinsurance assets continued

24.1 Insurance contracts assumptions continued

(a) Process used to decide on assumptions continued

The Chain Ladder method is adopted for mature classes of business where sufficient claims development data is available in order to produce estimates of the ultimate claims and premiums by actuarial reserving Group and underwriting year or year of account for the managed Syndicate. This methodology produces optimal estimates when a large claims development history is available and the claims development patterns throughout the earliest years are stable.

Where losses in the earliest underwriting years or years of account have yet to fully develop, a 'tail' arises on the reserving data, i.e. a gap between the current stage of development and the fully developed amount. The Chain Ladder methodology is used to calculate average development factors which, by fitting these development factors to a curve, allows an estimate to be made of the potential claims development expected between the current and the fully developed amount, known as a 'tail reserve'. This tail reserve is added to the current reserve position to calculate the total reserve required.

Chain Ladder methods may be applied to premiums, paid claims or incurred claims (i.e. paid claims plus case estimates). The basic technique involves the analysis of historical claims development factors and the selection of estimated development factors based on this historical pattern. The selected development factors are then applied to cumulative claims data for each accident year that is not yet fully developed to produce an estimated ultimate claims cost for each accident year.

Chain Ladder techniques are less suitable in cases in which the insurer does not have developed claims history data for a particular class of business (e.g. in relation to more recent underwriting years or years of account). In these instances the Group's actuaries make reference to the Bornhuetter-Ferguson method.

The Bornhuetter-Ferguson method is based on the Chain Ladder approach but utilises estimated ultimate loss ratios. This method uses a combination of a benchmark or market-based estimate and an estimate based on claims experience. The former is based on a measure of exposure such as premiums; the latter is based on the paid or incurred claims to date. The two estimates are combined using a formula that gives more weight to the experience-based estimate as time passes. This technique has been used in situations in which developed claims experience was not available for the projection (recent accident years or new classes of business).

In exceptional cases the required provision is calculated with reference to the actual exposures on individual policies. Adjustments are made within the claims reserving methodologies to remove distortions in the historical claims development patterns from large or isolated claims not expected to re-occur in the future. In addition, the reserves determined for the managed Syndicate are converted to annually accounted figures using earnings patterns that are consistent with those for the underlying Syndicate business.

The choice of selected results for each accident year of each class of business depends on an assessment of the technique that has been most appropriate to observed historical developments. In certain instances, this has meant that different techniques or combinations of techniques have been selected for individual accident years or groups of accident years within the same class of business.

(b) Claims development tables

The development of insurance liabilities provides a measure of the Group's ability to estimate the ultimate value of claims. The Group analyses actual claims development compared with previous estimates on an accident year basis. This exercise is performed to include the liabilities of Syndicate 33 at the 100% level regardless of the Group's actual level of ownership, which has increased significantly over the last six years. Analysis at the 100% level is required in order to avoid distortions arising from reinsurance to close arrangements which subsequently increase the Group's share of ultimate claims for each accident year three years after the end of that accident year.

The top half of each table, on the following pages, illustrates how estimates of ultimate claim costs for each accident year have changed at successive year ends. The bottom half reconciles cumulative claim costs to the amounts still recognised as liabilities. A reconciliation of the liability at the 100% level to the Group's share, as included in the Group balance sheet, is also shown.

24 Insurance liabilities and reinsurance assets continued

24.1 Insurance contracts assumptions continued

(b) Claims development tables continued

Insurance claims and claims expenses reserves – gross at 100%

Accident year	2001 £000	2002 £000	2003 £000	2004 £000	2005 £000	2006 £000	2007 £000	Total £000
Estimate of ultimate claims costs as adjusted for foreign exchange*								
at end of accident year	582,662	355,086	394,954	588,662	954,388	505,750	685,965	4,067,467
one year later	567,633	376,185	402,951	649,510	1,053,059	488,644	-	3,537,982
two years later	625,822	382,234	379,055	619,682	1,057,875	-	-	3,064,668
three years later	645,088	368,115	389,528	584,437	-	-	-	1,987,168
four years later	681,204	364,306	383,093	-	-	-	-	1,428,603
five years later	678,172	345,767	-	-	-	-	-	1,023,939
six years later	675,393	-	-	-	-	-	-	675,393
Current estimate of cumulative claims	675,393	345,767	383,093	584,437	1,057,875	488,644	685,965	4,221,174
Cumulative payments to date	(550,166)	(289,047)	(298,855)	(434,005)	(735,891)	(261,989)	(153,523)	(2,723,476)
Liability recognised at 100% level	125,227	56,720	84,238	150,432	321,984	226,655	532,442	1,497,698
Liability recognised in respect of prior accident years at 100% level								73,845
Total gross liability to external parties at 100% level								1,571,543

Reconciliation of 100% disclosures above to Group's share – gross

Accident year	2001 £000	2002 £000	2003 £000	2004 £000	2005 £000	2006 £000	2007 £000	Total £000
Current estimate of cumulative claims	675,393	345,767	383,093	584,437	1,057,875	488,644	685,965	4,221,174
Less: Attributable to external Names	(172,846)	(72,228)	(88,261)	(137,166)	(274,629)	(96,871)	(129,038)	(971,039)
Group share of current ultimate claims estimate	502,547	273,539	294,832	447,271	783,246	391,773	556,927	3,250,135
Cumulative payments to date	(550,166)	(289,047)	(298,855)	(434,005)	(735,891)	(261,989)	(153,523)	(2,723,476)
Less: Attributable to external Names	137,450	57,683	66,166	105,140	192,672	49,447	23,560	632,118
Group's share of cumulative payments	(412,716)	(231,364)	(232,689)	(328,865)	(543,219)	(212,542)	(129,963)	(2,091,358)
Liability for 2001 to 2007 accident years recognised on Group's balance sheet	89,831	42,175	62,143	118,406	240,027	179,231	426,964	1,158,777
Liability for accident years before 2001 recognised on Group's balance sheet								57,110
Total Group liability to external parties included in balance sheet – gross**								1,215,887

Insurance claims and claims expenses reserves – net at 100%

Accident year	2001 £000	2002 £000	2003 £000	2004 £000	2005 £000	2006 £000	2007 £000	Total £000
Estimate of ultimate claims costs as adjusted for foreign exchange*								
at end of accident year	287,895	237,401	307,137	492,147	572,367	450,018	593,001	2,939,966
one year later	323,583	258,930	322,020	535,338	653,704	447,659	-	2,541,234
two years later	381,384	265,650	297,150	515,172	649,302	-	-	2,108,658
three years later	413,320	251,537	307,699	481,864	-	-	-	1,454,420
four years later	404,236	245,892	298,719	-	-	-	-	948,847
five years later	392,112	235,466	-	-	-	-	-	627,578
six years later	388,403	-	-	-	-	-	-	388,403
Current estimate of cumulative claims	388,403	235,466	298,719	481,864	649,302	447,659	593,001	3,094,414
Cumulative payments to date	(302,120)	(183,245)	(229,114)	(350,961)	(398,400)	(241,053)	(133,857)	(1,838,750)
Liability recognised at 100% level	86,283	52,221	69,605	130,903	250,902	206,606	459,144	1,255,664
Liability recognised in respect of prior accident years at 100% level								34,156
Total net liability to external parties at 100% level								1,289,820

*The foreign exchange adjustment arises from the retranslation of the estimates at each date using the exchange rate ruling at 31 December 2007.
** This represents the claims element of the Group's insurance liabilities.

24 Insurance liabilities and reinsurance assets continued

24.1 Insurance contracts assumptions continued

(b) Claims development tables continued

Reconciliation of 100% disclosures above to Group's share - net

Accident year	2001 £000	2002 £000	2003 £000	2004 £000	2005 £000	2006 £000	2007 £000	Total £000
Current estimate of cumulative claims	388,403	235,466	298,719	481,864	649,302	447,659	593,001	3,094,414
Less: Attributable to external Names	(93,570)	(47,506)	(67,445)	(114,287)	(160,471)	(90,264)	(113,637)	(687,180)
Group's share of current ultimate claims estimate	294,833	187,960	231,274	367,577	488,831	357,395	479,364	2,407,234
Cumulative payments to date	(302,120)	(183,245)	(229,114)	(350,961)	(398,400)	(241,053)	(133,857)	(1,838,750)
Less: Attributable to external Names	69,063	33,405	48,666	84,617	96,884	46,210	21,091	399,936
Group's share of cumulative payments	(233,057)	(149,840)	(180,448)	(266,344)	(301,516)	(194,843)	(112,766)	(1,438,814)
Liability for 2001 to 2007 accident years recognised on Group's balance sheet	61,776	38,120	50,826	101,233	187,315	162,552	366,598	968,420
Liability for accident years before 2001 recognised on Group's balance sheet								24,795
Total net liability to external parties included in the balance sheet*								993,215

*This represents the claims element of the Group's insurance liabilities and reinsurance assets.

24.2 Movements in insurance claims liabilities and reinsurance claims assets

Year ended 31 December	2007			2006		
	Gross £000	Reinsurance £000	Net £000	Gross £000	Reinsurance £000	Net £000
Total at beginning of year	(1,128,329)	265,073	(863,256)	(1,322,493)	467,800	(854,693)
Claims and claims adjustment expense for year	(498,568)	75,203	(423,365)	(395,497)	13,156	(382,341)
Cash paid for claims settled in the year	452,235	(131,505)	320,730	504,656	(193,527)	311,129
Exchange differences and other movements	(41,225)	13,901	(27,324)	85,005	(22,356)	62,649
Total at end of year	(1,215,887)	222,672	(993,215)	(1,128,329)	265,073	(863,256)
Notified claims	(642,252)	137,868	(504,384)	(703,159)	214,148	(489,011)
Incurred but not reported	(573,635)	84,804	(488,831)	(425,170)	50,925	(374,245)
Total at end of year	(1,215,887)	222,672	(993,215)	(1,128,329)	265,073	(863,256)

The insurance claims expense reported in the consolidated income statement is comprised as follows:

	2007			2006		
	Gross £000	Reinsurance £000	Net £000	Gross £000	Reinsurance £000	Net £000
Current year claims and loss adjustment expenses	(562,223)	78,953	(483,270)	(353,895)	3,275	(350,620)
(Under)/over provision in respect of prior year claims and loss adjustment expenses	63,655	(3,750)	59,905	(41,602)	9,881	(31,721)
Total claims and claims handling expense	(498,568)	75,203	(423,365)	(395,497)	13,156	(382,341)

25 Trade and other payables

	Note	2007 £000	2006 £000
Creditors arising out of direct insurance operations		30,353	33,473
Creditors arising out of reinsurance operations		114,317	126,319
		144,670	159,792
Obligations under finance leases	34	457	442
Share of Syndicate's other creditors' balances		2,681	15,481
Social security and other taxes payable		4,067	5,846
Other creditors		13,704	8,049
		20,909	29,818
Reinsurers' share of deferred acquisition costs	8	5,639	6,529
Accruals and deferred income		64,657	58,686
Total		235,875	254,825

The amounts expected to be settled before and after one year are estimated as follows:

Within one year		234,828	252,298
After one year		1,047	2,527
		235,875	254,825

The amounts expected to be settled after one year of the balance sheet date primarily relate to finance leases and the Group's provision of sabbatical leave employee benefits.

26 Tax expense

The amounts charged in the consolidated income statement comprise the following:

	Note	2007 £000	2006 £000
Current tax expense		26,891	8,770
Deferred tax expense	27	19,060	28,446
		45,951	37,216

The tax expense on the Group's profit before tax differs from the theoretical amount that would arise using the average tax rate applicable to profits of the consolidated companies as follows:

	2007 £000	2006 £000
Profit before tax	237,199	201,062
Tax calculated at the standard corporation tax rate applicable in the UK* of 30% (2006: 30%)**	71,160	60,319
Effects of:		
Expenses not deductible for tax purposes	(1,296)	652
Income not subject to tax	-	(10,264)
Group entities subject to overseas tax at lower rates	(24,843)	(18,121)
Tax losses for which no deferred tax asset is recognised	1,092	4,351
Other items	(2,064)	(75)
Change of deferred tax rate	(1,374)	-
Prior year tax adjustments	3,276	354
Tax charge for the period	45,951	37,216

*The principal charge to current tax arises in respect of the Group's UK subsidiaries.
**The UK corporation tax rate will be changed from 30% to 28% from April 2008.

27 Deferred tax

	2007 £000	2006 £000
Deferred tax assets	40,153	24,945
Deferred tax liabilities	(49,904)	(33,412)
Total net deferred tax liability	(9,751)	(8,467)

All material tax assets and liabilities relate to the same tax authority.

27 Deferred tax continued

The movement on the total net deferred tax liability is as follows:

	2007 £000	2006 £000
At 1 January	(8,467)	(15,193)
Income statement charge	(19,060)	(28,446)
Transfer from deferred tax to current tax	19,850	31,805
(Charge to)/released from equity	(2,074)	3,367
At 31 December	(9,751)	(8,467)

The applicable rate for deferred tax from April 2008 is 28%.

(a) Group deferred tax assets analysed by balance sheet headings

At 31 December	2006 £000	Income statement (charge)/credit £000	Transfer to current tax £000	Transfer from equity £000	2007 £000
Tangible assets	1,344	(121)	–	–	1,223
Trade and other payables	8,991	6,471	–	–	15,462
Retirement benefit obligations	6,876	2,600	–	–	9,476
Losses	–	4,151	–	–	4,151
Other items	7,734	4,181	–	(2,074)	9,841
Total deferred tax assets	24,945	17,282	–	(2,074)	40,153

(b) Group deferred tax liabilities analysed by balance sheet headings and Syndicate participation

At 31 December	2006 £000	Income statement (charge)/credit £000	Transfer to current tax £000	Transfer from equity £000	2007 £000
Intangible assets	(377)	25	–	–	(352)
Investment in associated enterprises	(191)	13	–	–	(178)
Financial assets	(3,785)	(2)	–	–	(3,787)
Insurance contracts – equalisation provision*	(6,064)	21	–	–	(6,043)
Other items	(3,654)	3,654	–	–	–
	(14,071)	3,711	–	–	(10,360)
Open years of account and Section 107 disclaimers	(19,341)	(40,053)	19,850	–	(39,544)
Total deferred tax liabilities	(33,412)	(36,342)	19,850	–	(49,904)

*The solvency regulations in the UK require certain entities within the Group to establish an equalisation provision, to be utilised against abnormal levels of future losses in certain lines of business. The regulations prescribe that the provision is increased every year by an amount that is calculated as a percentage of net premiums written for those lines of business during the financial year subject to a maximum percentage. The amount of each annual increase is a deductible expense for tax purposes, and the equalisation provision is taxed when released. The entities within the Group that are affected by this requirement continue to prepare their individual financial statements, for statutory filing and tax purposes, in accordance with UK GAAP which permits the recognition of equalisation provisions on the balance sheet. Equalisation provisions are not permitted under IFRS which therefore results in the temporary difference for tax purposes.

Deferred income tax assets are recognised for tax losses carried forward to the extent that the realisation of the related tax benefit through the future taxable profits is probable. During the period, management revised its assumptions about the recoverability of carried forward unused tax losses to be recognised as deferred tax assets. Management's assessment is that it is now probable that enough taxable profit will be available to allow part of the benefit to be utilised. Part of the balance has therefore now been provided. The Group has not provided for deferred tax assets totalling £8,104,000 (2006: £7,023,000) in relation to losses in overseas companies of £23,667,000 (2006: £20,064,000). The aggregate amount of temporary differences associated with investments in subsidiaries and associates for which no deferred tax liability has been recognised is £nil (2006: £73,855,000). This is as a result of the transfer of these subsidiaries to Hiscox Ltd from Hiscox plc. In accordance with IAS 12, all deferred tax assets and liabilities are classified as non-current.

28 Employee retirement benefit obligations

The Company's subsidiary, Hiscox plc, operates a defined benefit pension scheme based on final pensionable salary. The scheme closed to future accrual with effect from 31 December 2006 and active members were offered membership of a defined contribution scheme from 1 January 2007. The funds of the defined benefit scheme are controlled by the trustee and are held separately from those of the Group.

The gross amount recognised in the Group balance sheet in respect of the defined benefit scheme is determined as follows:

	2007 £000	2006 £000
Present value of funded obligations	106,793	137,461
Fair value of scheme assets	(127,576)	(133,660)
Present value of unfunded obligations	(20,783)	3,801
Unrecognised net actuarial gains	18,817	–
Unrecognised surplus deemed irrecoverable	1,966	–
Gross liability in the balance sheet	–	3,801

The unrecognised net actuarial gains are the net cumulative gains and losses on both the scheme's obligations and underlying assets.

28 Employee retirement benefit obligations continued

Included within loans and receivables for the Group (note 19) at 31 December 2006 was a right to reimbursement of £1,163,000 recoverable from third party Names in Syndicate 33, representing their contribution to funding the defined benefit scheme obligation (2007: £nil). The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit actuarial cost method. A formal full actuarial valuation is performed on a triennial basis, most recently at 31 December 2005, and updated at each intervening balance sheet date by the actuaries. The present value of the defined benefit obligation is determined by discounting the estimated future cash flows using interest rates of AA rated corporate bonds that have terms to maturity that approximate to the terms of the related pension liability.

The plan assets are invested as follows:

At 31 December	2007 £000	2006 £000
Equities	57,716	98,738
Debt and fixed income assets	69,702	10,098
Cash	158	24,824
	127,576	133,660

During the current year under review a series of changes to the scheme's investment mix were executed by Trustees so as to achieve a greater degree of protection against interest rate volatility following the scheme's recent closure. These changes resulted in the majority of the scheme's debt and fixed income assets at 31 December 2007 now being held through the ownership of equity units in liability managed credit funds issued by Standard Life Assurance Limited which invest in a broad spread of high quality corporate bonds with derivatives used in controlled conditions to extend durations in some cases.

The amounts recognised in the Group's income statement are as follows:

	Note	2007 £000	2006 £000
Current service cost		200	4,191
Interest cost		6,657	6,397
Expected return on scheme assets		(7,711)	(6,431)
Net actuarial losses including curtailment charges recognised		-	7,355
Past service cost		-	668
Settlement gain recognised		(4,913)	-
Effect of deemed irrecoverability of surplus		1,966	-
Total included in staff costs	10	(3,801)	12,180

The reduction in current service cost is attributable to the scheme's closure to future accrual on 31 December 2006.

The actual return on scheme assets was £7,786,000 (2006: £12,911,000).

The movement in liability recognised in the Group's balance sheet is as follows:

	Note	2007 £000	2006 £000
At beginning of year		3,801	16,677
Total expense charged/(credited) in the income statement of the Group	10	(3,801)	12,180
Contributions paid		-	(25,056)
At end of year		-	3,801

A reconciliation of the fair value of the scheme assets is as follows:

	2007 £000	2006 £000
Opening fair value of scheme assets	133,660	101,409
Expected return on scheme assets	7,711	6,431
Difference between expected and actual return on scheme assets	75	6,480
Contributions by the employer	-	25,056
Settlements with scheme members	(11,687)	-
Benefits paid	(2,183)	(5,716)
Closing fair value of scheme assets	127,576	133,660

28 Employee retirement benefit obligations continued

A reconciliation of the present value of funded obligations of the scheme is as follows:

	2007 £000	2006 £000
Benefit obligation at beginning of year	137,461	137,533
Current service cost	200	4,191
Interest cost	6,657	6,397
Actuarial gains	(18,742)	(5,917)
Benefits paid from scheme	(2,183)	(5,716)
Curtailements and amendments	-	973
Settlements with scheme members	(16,600)	-
Closing present value of funded obligations	106,793	137,461

A summary of the scheme's recent experience is shown below:

	2007 £000	2006 £000	2005 £000	2004 £000
Experience gains/(losses) on scheme liabilities	2,783	(3,310)	(1,223)	992
Experience gains on scheme assets	75	6,480	10,764	1,316

Assumptions regarding future mortality experience are set based on professional advice, published statistics and actual experience.

The average life expectancy in years of a pensioner retiring at age 60 on the balance sheet date is as follows:

	2007 years	2006 years
Male member	24.5	24.5
Female member	27.6	27.6

The average life expectancy in years of a pensioner retiring at 60, 15 years after the balance sheet date is as follows:

	2007 years	2006 years
Male member	25.6	25.6
Female member	28.6	28.6

Other principal actuarial assumptions are as follows:

	2007 %	2006 %
Discount rate	5.80	5.10
Expected return on plan assets	6.09	6.09
Future salary increases	4.60	4.30
Inflation assumption	3.60	3.30
Pension increases	3.60	3.30

During the year the Group made no contributions to the defined benefit scheme (2006: contribution rate of 33.3% of pensionable salaries). No additional contributions were paid during 2007 (2006: £20,570,000). The Group has agreed that further additional contributions will be made if necessary although no contributions are currently expected to be made in 2008 given the current level of underlying scheme surplus. 61% of the deficit calculated is recharged or refunded to Syndicate 33.

The expected return on scheme assets is based on historical data and management's expectations of long-term future returns.

29 Earnings per share

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of shares in issue during the year, excluding ordinary shares purchased by the Group and held in treasury as own shares.

Basic

	2007	2006
Profit attributable to the Company's equity holders (£000)	191,248	163,846
Weighted average number of ordinary shares (thousands)	395,308	392,558
Basic earnings per share (pence per share)	48.4p	41.7p

Diluted

Diluted earnings per share is calculated adjusting for the assumed conversion of all dilutive potential ordinary shares. The Company has one category of dilutive potential ordinary shares, share options and awards. For the share options, a calculation is made to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options.

29 Earnings per share continued

Diluted continued

	2007	2006
Profit attributable to the Company's equity holders (£000)	191,248	163,846
Weighted average number of ordinary shares in issue (thousands)	395,308	392,558
Adjustments for share options (thousands)	13,530	12,449
Weighted average number of ordinary shares for diluted earnings per share (thousands)	408,838	405,007
Diluted earnings per share (pence per share)	46.8p	40.5p

Diluted earnings per share has been calculated after taking account of 13,014,000 (2006: 11,806,000) options and awards under employee share option and performance plan schemes and 516,000 (2006: 643,000) options under SAYE schemes.

30 Dividends paid to external shareholders

	2007 £000	2006 £000
Interim dividend for the year ended:		
31 December 2007 of 4.0p (net) per share	15,868	–
31 December 2006 of 3.0p (net) per share	–	11,789
Final dividend for the year ended:		
31 December 2006 of 7.0p (net) per share	27,723	–
31 December 2005 of 4.75p (net) per share	–	18,639
	43,591	30,428

A final dividend in respect of 2007 of 8p per share, amounting to a total dividend of 12p for the year, is to be proposed at the Annual General Meeting on 4 June 2008. These financial statements do not reflect this final dividend as a distribution or liability in accordance with IAS 10 Events after the Balance Sheet Date.

31 Acquisitions during the financial year

On 16 August 2007, the Group acquired 100% of the share capital of ALTOHA Inc. in the USA. The total consideration was £29,052,000 which includes contingent consideration of £7,530,000 as outlined below. No goodwill arose on acquisition.

Intangible assets of £5,083,000 have been recognised in respect of the US State authorisation licences held by ALTOHA Inc.'s consolidated operations.

	Book value 2007 £000	Adjustments 2007 £000	Fair value 2007 £000
Identifiable assets and liabilities acquired			
Investments	18,942	–	18,942
Intangible assets	–	5,083	5,083
Cash and cash equivalents	17,919	–	17,919
Other assets	4,473	–	4,473
Insurance contract liabilities	(4,617)	–	(4,617)
Other liabilities	(3,710)	(9,038)	(12,748)
Net identifiable assets	33,007	(3,955)	29,052
Cash consideration paid on business combination including acquisition related transaction costs of £197,000			(21,522)
Contingent cash consideration on business combination paid into escrow facility			(7,530)

Goodwill on acquisition

–

The adjustments made to book values recognise an additional pre-acquisition dividend payable to the former shareholders, and the recognition of intangible assets in the form of US State authorisation licences.

If the acquisition had occurred on 1 January 2007, Group net revenue for the year would have increased by £6,895,000 and Group profit after tax for the year would have increased by £1,373,000.

The total consolidated profit after tax of the acquired entity since the acquisition date included in the Group's profit or loss for the period was £472,000.

The intangible assets shown above arose from the licences held by the acquired group which strengthens the Group's market position in targeted business segments.

The contingent consideration with regard to ALTOHA Inc. is provisional and dependent on certain criteria including the non-emergence of any material unidentified pre-acquisition liabilities over a period of two years from the date of acquisition up to 16 August 2009.

32 Disposals during the financial year

The Group's wholly owned subsidiary, Hiscox Investment Management Limited was sold on 5 December 2007. This business did not constitute a discontinued operation as defined by IFRS 5 Non Current Assets Held for Sale and Discontinued Operations due to its relative insignificance to the Group and the fact that it did not represent a major line of business or operating segment.

Cash consideration of £300,000 was received in respect of this disposal. The Group also received a 40% equity stake in the acquiror, HIM Capital Holdings Ltd, which is incorporated on the Group's balance sheet at 31 December 2007 as an equity accounted associate, as part of the consideration. The fair value of this holding at the date of transaction approximated to the Group's retained interest in 40% of the pre-transaction carrying values of Hiscox Investment Management Limited's tangible net assets.

The total fair value of the consideration received was £420,000. The net assets disposed at the date of sale totalled £420,000 and included cash and cash equivalents of £1,236,000.

No profit or loss therefore arose on this transaction.

33 Contingencies and guarantees

The Group's subsidiaries are like most other insurers, continuously involved in legal proceedings, claims and litigation in the normal course of business. The Group does not believe that such actions will have a material effect on its profit or loss and financial condition.

The Group is subject to insurance solvency regulations in all the territories in which it issues insurance contracts, and it has complied with all the local solvency regulations. There are no contingencies associated with the Group's compliance or lack of compliance with these regulations.

The following guarantees have also been issued:

(a) Hiscox plc has entered into a deed of covenant in respect of its corporate member subsidiary, Hiscox Dedicated Corporate Member Limited, to meet the subsidiaries' obligations to Lloyd's. The total guarantee given by the Company under this deed of covenant (subject to limited exceptions) amounts to £118,831,798 (2006: £118,831,798). The obligations in respect of this deed of covenant are secured by a fixed and floating charge over certain of the investments and other assets of the Company in favour of Lloyd's. Lloyd's has a right to retain the income on the charged investments in circumstances where it considers there to be a risk that the covenant might need to be called and may be met in full.

(b) Hiscox plc has an agreement with Lloyds TSB Bank, an agent for a syndicate of banks, for a £137,500,000 irrevocable standby Letter of Credit Facility and a US\$225,000,000 Term and Revolving Credit Facility. Commencing 7 November 2005 £137,500,000 was drawn down on the Letter of Credit Facility to support part of the Group's underwriting activities. The Group has given a fixed and floating charge over certain assets as a guarantee to the group of banks led by Lloyds TSB Bank in connection with their Letter of Credit. At 31 December 2007, US\$182,000,000 of the term and revolving credit facility was available and fully drawn (2006: US\$182,000,000).

(c) Hiscox Insurance Company Limited has arranged a Letter of Credit of £50,000 (2006: £325,000) with NatWest Bank plc to support its consortium activities with Lloyd's.

(d) The managed syndicate is subject to the New Central Fund annual contribution, which is an annual fee calculated on capacity for 2007 and on gross premiums written for 2008. This fee was 1.0% for 2007 and 0.5% for 2008. 0.75% was loaned to the central fund for 2007 which was repaid during the year. No loan

exists for 2008. In addition to this fee, the Council of Lloyd's has the discretion to call a further contribution of up to 3% of capacity if required.

(e) As Hiscox Bermuda is not an admitted insurer or reinsurer in the US, the terms of certain US insurance and reinsurance contracts require Hiscox to provide Letters of Credit or other terms of collateral to clients. On 1 December 2006, Hiscox entered into a Letter of Credit Reimbursement and Pledge Agreement with Citibank for the provision of a Letter of Credit facility in favour of US ceding companies. The agreement was a three year secured facility that allowed Hiscox to request the issuance of up to US\$300 million in Letters of Credit. Letters of Credit issued under these facilities are collateralised by pledged cash and cash equivalents of Hiscox Bermuda. Letters of Credit under this facility totalling approximately US\$38 million were issued with an effective date of 31 December 2007.

34 Capital and lease commitments

Capital commitments

The Group's capital expenditure contracted for at the balance sheet date but not yet incurred for property, plant and equipment was £165,000 (2006: £161,000).

Operating lease commitments

The Group acts as both lessee and lessor in relation to various offices in the UK and overseas which are held under non-cancellable operating lease agreements. The leases have varying terms, escalation clauses and renewal rights. The Group also has payment obligations in respect of operating leases for certain items of office equipment. Operating lease rental expenses for the year totalled £4,691,000 (2006: £4,859,000). Operating lease rental income for the year totalled £468,000 (2006: £675,000).

34 Capital and lease commitments continued

Operating lease commitments continued

The aggregate minimum lease payments required by the Group under non-cancellable operating leases, over the expected lease terms, are as follows:

	2007 £000	2006 £000
No later than one year		
Land and buildings	4,705	4,553
Office equipment	141	129
Later than one year and no later than five years		
Land and buildings	14,032	14,687
Office equipment	199	246
Later than five years		
Land and buildings	19,714	22,917
	38,791	42,532

The total future aggregate minimum lease rentals receivable by the Group as lessor under non-cancellable operating property leases are as follows:

	2007 £000	2006 £000
No later than one year	468	513
Later than one year and no later than five years	1,872	1,974
Later than five years	117	1,027
	2,457	3,514

Obligations under finance leases

It is the Group's policy to lease certain of its motor vehicles under finance lease arrangements. The leases have a typical term of three years and are on a fixed repayment basis with a final lump sum component at the end of each agreement should the Group decide to acquire ownership of the vehicle. Interest rates are fixed at the contract commencement date. The Group's obligations under leases are secured by the lessors' charges over the leased assets.

Finance lease interest expense for the year totalled £54,000 (2006: £41,000).

The finance lease obligations to which the Group is committed include the following minimum lease payments:

	2007 £000	2006 £000
Current liabilities due for settlement within one year	246	233
Non-current liabilities due for settlement after one year and no later than five years	261	273
	507	506
Less: future finance lease interest charges	(50)	(64)
	457	442

The present value of the minimum lease payments is not materially different to the currently disclosed obligation.

35 Principal subsidiary companies of Hiscox Ltd at 31 December 2007

Company	Nature of business	Country
Hiscox plc*	Holding company	Great Britain
Hiscox Insurance Company Limited	General insurance	Great Britain
Hiscox Insurance Company (Guernsey) Limited*	General insurance	Guernsey
Hiscox Inc.	Underwriting agent	USA (Delaware)
Hiscox Holdings Inc.	Insurance holding company	USA (Delaware)
ALTOHA Inc.	Holding company	USA (Delaware)
American Live Stock Inc.	Underwriting agent	USA (Illinois)
Hiscox Insurance Company Inc.	General insurance	USA (Illinois)
Hiscox ASM Limited	Underwriting agent	Great Britain
Hiscox Insurance Company (Bermuda) Limited*	General insurance and reinsurance	Bermuda
Hiscox Dedicated Corporate Member Limited	Lloyd's corporate Name	Great Britain
Hiscox Select Insurance Fund PLC	Insurance holding company	Great Britain
Hiscox Select Holdings Limited	Insurance holding company	Great Britain
Hiscox Select A to J Limited	Lloyd's corporate Names	Great Britain
Hiscox Holdings Limited**	Insurance holding company	Great Britain
Hiscox Insurance Holdings Limited	Insurance holding company	Great Britain
Hiscox Assurances Services SARL	Underwriting agent	France
Hiscox International Holdings B.V.	Insurance holding company	Netherlands
Hiscox Syndicates Limited	Lloyd's managing agent	Great Britain
Hiscox Underwriting Ltd	Underwriting agent	Great Britain
Hiscox AG	Underwriting agent	Germany
Hiscox Overseas Holdings B.V.*	Holding company	Netherlands
Hiscox bv	Underwriting agent	Netherlands
Hiscox Connect Limited	Online intermediary	Great Britain
Hiscox Underwriting Group Services Limited	Service company	Great Britain
Hiscox NV	Underwriting agent	Belgium
Hiscox Trustees Limited†	Corporate trustee	Great Britain
Hiscox Pension Trustees Limited	Pension trustee	Great Britain
Hiscox Qualifying Employees Share Ownership Trustees Limited	Share scheme trustee	Great Britain

*Held directly.

**Hiscox Holdings Limited held 54,560 shares in Hiscox Ltd (2006: 54,560) at 31 December 2007.

†Hiscox Trustees Limited is the trustee of the Hiscox Employee Share Ownership Plan (ESOP). The ESOP owned 132,399 shares in Hiscox Ltd (2006: 135,782) at 31 December 2007. The shares have been purchased by the ESOP for future use in employee share option schemes and are held as own shares. None of these shares are currently under option to employees, nor have any been conditionally gifted to them.

All companies are wholly owned. The proportion of voting rights of subsidiaries held is the same as the proportion of equity shares held.

36 Related-party transactions

Details of the remuneration of the Group's key personnel are shown in the Directors' remuneration report on pages 54 to 59.

A number of the Group's key personnel hold insurance contracts and investment management agreements with the Group, all of which are on normal commercial terms and are not material in nature.

The following transactions were conducted with related parties during the year.

(a) Syndicate 33 at Lloyd's

Hiscox Syndicates Limited, a wholly owned subsidiary of the Company, received management fees and profit commissions for providing a range of management services to Syndicate 33 in which Hiscox Dedicated Corporate Member Limited, and in the prior year the corporate member subsidiaries of Hiscox Select Insurance Fund PLC also participated.

	2007 £000	2006 £000
Value of services provided by Hiscox Syndicates Limited to Syndicate 33	41,466	19,877
Amounts receivable from Syndicate 33 at 31 December excluding profit commission	1,402	1,695

(b) Transactions with associates

Certain companies within the Group conduct insurance and other business with associates. These transactions arise in the normal course of obtaining insurance business through brokerages, and are based on arm's length arrangements.

	Total 2007 £000	Total 2006 £000
Gross premium income achieved through associates	7,290	2,325
Commission expense charged by associates	1,342	503
Amounts payable to associates at 31 December	120	48
Amounts receivable from associates at 31 December	47	16

Details of the Group's associates are given in note 16.

36 Related-party transactions continued**(c) Internal reinsurance arrangements**

During the current and preceding year, there were reinsurance arrangements between Hiscox Dedicated Corporate Member Limited, Hiscox Insurance Company Limited, Hiscox Insurance Company (Guernsey) Limited and Hiscox Insurance Company (Bermuda) Limited.

(d) Other

Blyth Valley Ltd was the Group's sole associate during the prior year. BE Masojada was a non-executive Director of Ins-sure Holdings Limited and its subsidiaries throughout the prior year until resignation on 31 December 2006. These companies operate in a joint venture between Lloyd's, the International Underwriting Association (IUA) and Xchanging. These companies provide policy issuance, premium collection, claims settlement and clearing services to Lloyd's and the London insurance company markets. Hiscox Underwriting Group Services Limited received the annual fee of £nil (2006: £20,000) in relation to this directorship. The balance due at 31 December 2007 was £nil (2006: £20,000).

BE Masojada was also Deputy Chairman of Lloyd's in the prior year. Hiscox Underwriting Group Services Limited received the annual fee of £nil (2006: £46,250) in relation to his services. There were no amounts outstanding at 31 December 2007 (2006: £nil).

Five year summary

	2007 £000	2006 £000	2005 £000	2004 £000	2003 £000
Results					
Gross premiums written	1,198,949	1,126,164	861,174	816,609	797,380
Net premiums written	974,910	975,397	681,236	704,085	660,966
Net premiums earned	965,190	888,828	693,299	714,852	547,451
Results of operating activities	245,295	201,062	70,221	89,522	83,408
Profit for the year after tax	191,248	163,846	48,630	63,948	60,491
Assets employed					
Intangible assets	40,452	33,212	33,099	29,989	21,753
Financial assets carried at fair value	1,747,827	1,241,910	1,237,778	980,731	773,289
Cash and cash equivalents	302,742	502,871	413,759	119,563	52,945
Insurance liabilities and reinsurance assets	(1,433,799)	(1,291,329)	(1,216,624)	(1,008,032)	(845,450)
Other net assets	167,082	195,421	110,001	246,575	327,300
Net assets	824,304	682,085	578,013	368,826	329,837
Net asset value per share (p)	209.5	173.2	147.7	125.7	113.5
Key statistics					
Basic earnings per share (p)	48.4	41.7	15.6	21.3	20.9
Diluted earnings per share (p)	46.8	40.5	15.1	21.0	20.6
Combined ratio (%)	84.4	89.1	96.0	92.6	87.2
Return on equity (%)	28.8	28.9	12.8	20.6	21.7
Dividends per share (p)	12.00	10.00	7.00	5.00	4.20
Share price – high* (p)	304.5	280.25	234.5	180.5	170.5
Share price – low* (p)	246.75	193.75	152.25	143.5	137.0

*Closing mid market prices.

The amounts and ratios for 2003 are those previously published on a UK GAAP basis, the Group's primary reporting framework at that time. The figures reported for 2004 to 2007 are prepared in accordance with IFRS.

Glossary

Binder (or binding authority)

An authority granted by an underwriter to an agent (known as a coverholder) whereby that agent is entitled to accept, within certain limits, insurance business on behalf of the underwriter.

Cedant

An insurer that transfers insurance risk to another insurer under a reinsurance contract.

Claims ratio

Net claims incurred, including IBNR, as a percentage of net earned premiums.

Combined ratio

The total of the claims and expenses ratios.

E&O

Errors and omissions, liability insurance for businesses.

Expense ratio

Net operating expenses as a percentage of net earned premiums.

Gross premiums written

Premiums contracted for before any deductions.

Incurred loss ratio

Paid and outstanding losses as a percentage of premiums. Gross incurred loss ratio is before deducting any reinsurance; the net loss ratio is after deducting reinsurance.

Individual capital assessments

Risk-based calculations of the capital required by each FSA-authorized insurance entity in accordance with FSA regulations.

Long-tail

A term used to describe an insurance risk that has the potential for claims development or new claims to be reported a number of years after expiry of the term of the policy.

Member or Lloyd's Member

An underwriting member of Lloyd's. Members collectively accept insurance risks through a Lloyd's syndicate. Members are required to meet certain Lloyd's solvency requirements and are responsible for their share of any losses made by the syndicates on which they participate, and are entitled to an equivalent share of any profits.

Names

Individual Members of Lloyd's.

Net premiums written

Premiums received after the cost of reinsurance and adjustment for unearned premium. Unearned premium covers the future period of risk of an insurance policy.

Net written premium

Premiums received after the cost of reinsurance.

Open year

A year of account of a syndicate which has not been closed by reinsurance to close ('RITC'). RITC usually occurs at the end of the third year. A year of account can be left open beyond the third year if the extent of the future liability cannot be accurately quantified.

PSC

Professions and Specialty Commercial division (commercial lines).

Qualifying quota share reinsurance (QQS)

These are quota share reinsurance policies, which Lloyd's allow in certain circumstances, that enable a syndicate to write gross premium in excess of its authorised stamp capacity.

Quota shares

Where insurance risks are re-insured on a proportional basis, premiums and claims are divided in the same proportions between the insurer and re-insurer.

Re-domicile

The establishment of a new parent company for the Hiscox Group, based in Bermuda.

Return on Equity (ROE)

Net profit after tax expressed as a percentage of adjusted opening equity. This percentage measures profitability by expressing the efficiency of the Group's utilisation of shareholders' funds.

Reinsurance to Close (RITC)

The reinsurance to close of a syndicate comprises a premium payable by the closing year to the members on the next open year of account and a contract which transfers the liability for all claims in respect of the closing year to the next open year.

Short-tail

A term used to describe an insurance risk where claims are expected to arise near to the dates on which a policy was current.

Sidecar

A limited lifespan insurance company formed to give its investors access to the insurance market, and its cedants access to capital.

Specie

The line of business that covers cash and valuables in vaults, premises or transit.

Stamp capacity or syndicate capacity

The maximum amount of business that a syndicate in Lloyd's can write per year, aggregated from all its members.

Syndicate

A grouping of Lloyd's underwriters. Each syndicate has an active underwriter who is authorised to accept business on behalf of each underwriting member participating therein. A member of a syndicate is still a principal in his own right and is personally liable for his agreed share of each risk that is accepted by the syndicate. He is not liable for the debts of other syndicate members and thus the liability is several but not joint.

Year of account

The year to which risk is allocated and to which all premiums and claims in respect of that risk are attributed. The year of account of a risk is determined by the calendar year in which it incepts. A syndicate year of account is normally closed by reinsurance at the end of 36 months.

Credits

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Design by Browns
Print by St Ives Westerham Press
Photography (Chairman/Chief Executive) by John Ross
Photography (portraits) by John Ross and Stephen Raynor

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