

Date: 5 March 2010
On behalf of: Hardy Underwriting Bermuda Limited (“Hardy” or “the Group”)
Embargoed until: 0700hrs

Hardy Underwriting Bermuda Limited

■ Financial Results for the year ended 31 December 2009

Hardy Underwriting Bermuda Limited (“Hardy” or “The Group”), the specialist insurer, today announced its financial results for the year ended 31 December 2009.

FINANCIAL HIGHLIGHTS

- Profit before tax and foreign exchange movements of £26.7m. (2008: £4.4m)
- Profit before tax of £20.1m. (2008: £23.1m)
- Combined ratio before foreign exchange movements of 78.1%. (2008: 91.2%)
- Net tangible assets growing to 266p. (2008: 245p)
- Dividend for the year will be 13.3p: 2nd interim dividend of 9.3p per share to be paid on April 1st. (2008: 12.1p per share)

OPERATIONAL HIGHLIGHTS

- Business volumes up by 40%
- Hardy Bermuda Limited commenced underwriting in May 2009
- HAIM the Middle Eastern joint venture successfully launched
- Board strengthened with new non-executive appointments

Commenting on the Group’s results, David Mann, Chairman of Hardy Underwriting Bermuda Limited, said:

“I am pleased to report that the Hardy group has maintained its record of profitability, returning a profit of £20.1m, after taking into account a foreign exchange loss which partly reverses last year’s gain. The profit before tax and foreign exchange was £26.7m (2008: £4.4m). Just as importantly, we have made good progress in implementing some of the key elements of the strategic growth plan on which continuing profitability and success are based.”

“The effect of the global recession and the turmoil in financial services indicate challenging times ahead. Challenging conditions, however, create opportunities and we believe that Hardy has the ideal base from which to take full advantage.”

Barbara Merry, Hardy’s Chief Executive, added:

“Hardy has performed consistently well during a tough year for insurers and reinsurers. We achieved more than our targeted growth in 2009 . This phase of our development has been very much associated with putting new skills and building blocks in place. We now seek to exploit these advantages.”

“The Hardy team that we have assembled certainly gives us grounds for optimism about the longer term future of our business.”

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CHAIRMAN'S REPORT

I am pleased to report that the Hardy group has maintained its record of profitability, returning a profit of £20.1m, after taking into account a foreign exchange loss which partly reverses last year's gain. The profit before tax and foreign exchange was £26.7m (2008: £4.4m). Just as importantly, we have made good progress in implementing some of the key elements of the strategic growth plan on which continuing profitability and success are based.

Following the merger of syndicates 382 and *38Twenty* last year, we announced a new syndicate management structure comprising four business units (non-marine property, marine and aviation, specialty lines and property treaty). The senior underwriters leading these business units, have responsibility for both business development and for the professional development of their teams, and they have all embraced these challenges with enthusiasm and dedication.

The maxim, 'think global, act local', has a particular resonance for Hardy and is reflected in our strategy for the future. Hardy has a strong and continuing commitment to the Lloyd's market, but we also attach great importance to enhancing our presence in local markets around the world, so wherever possible we are choosing to utilise the Lloyd's platform to support our overseas growth, rather than establishing separately capitalised companies.

During the year, Hardy Bermuda Limited began writing business on the island, focusing on property treaty business. This has helped deliver some further diversity to our account in a class which remains better rated than most. We are looking forward to building on this, as the team in Bermuda consolidates its position in that market.

In the autumn we announced the formation of our joint venture in the Middle East with the Arab Insurance Group (Arig). Hardy Arig Insurance Management, (HAIM), is based in Bahrain and is a coverholder for syndicate 382, focused on reinsurance business from the Middle East and North Africa in both the construction and property sectors.

Other overseas initiatives are in prospect. The Board has decided to establish an office in Singapore, to be located in the Lloyd's Asia office, from where Hardy will underwrite business sourced from the dynamic Asia Pacific region.

Our development plans have been given further impetus with the recently announced appointment of Anthony Taylor and Fiona Luck as non-executive directors of the Group. Both have vast experience of the global market and their contribution to the achievement of our objectives will be invaluable. Adrian Walker, Hardy's Director of Underwriting, has also joined the Board to add further strength to its executive team.

The pre-tax profit of £20.1m (2008: £23.1m) comes despite a challenging rating environment and market conditions that did not favour our low risk investment strategy. In line with our commitment to deliver a 10% increase in dividends year on year, the Board is proposing a second interim dividend of 9.3p (2008 final dividend of 8.5p) to be paid on 1st April 2010 to shareholders on the register on 19th March 2010. The Board is not proposing to pay a final dividend, so total dividends for the year amount to 13.3p, following the interim dividend of 4p (2008: 3.6p) paid in October 2009.

The effect of the global recession and the turmoil in financial services indicate challenging times ahead. The introduction of Solvency II will have resource implications throughout the industry and we are mindful of the recommendations of the *Walker Review of Corporate Governance*. Challenging conditions, however, create opportunities and we believe that we have the ideal base from which to take full advantage.

The Group continues to deliver an exemplary performance grounded upon an ambitious but realistic and robust plan for its growth and development. On behalf of the Board and shareholders, I record our gratitude to the hugely professional team at Hardy for their contribution to the continued success of the business.

David Mann
Chairman

OPERATING AND FINANCIAL REVIEW

Introduction

Last year was one of mixed fortunes for insurers and reinsurers. Soft market conditions along with considerable evidence of recession-related claims have resulted in higher than expected attritional loss levels for certain lines of business. Catastrophe exposed classes, on the other hand, performed exceptionally well, particularly as regards US risks. Underwriting returns are therefore entirely dependent upon the particular mix of business.

Investment returns will mostly be unremarkable, except for insurers or reinsurers with significant equity or corporate bond portfolios which will now be disclosing meaningful unrealised gains.

The rating environment across our book of business was also mixed with some classes stable or weakening and others experiencing robust pricing levels well above benchmark rates even where the rating trend itself was in decline.

Hardy has progressed well throughout 2009. We have achieved more than our original targeted growth for the year, although some of the excess is attributable to sterling weakness. We have also pushed forward with our business development plan creating opportunities which will help to sustain that growth. We have not, however, compromised on underwriting discipline. Although overall profit for 2009 is down on 2008, which was a record year because of a material foreign exchange gain, the 2009 underwriting return is significantly better at £40.4m before foreign exchange (2008: £10.8m) and the combined ratio of 78.1% is evidence of that.

Our performance is consistent and strong. We consolidated recent organisational changes, continuing to make improvements in our working practices, systems and models and building for the future positioning of the business

Review of 2009 performance

The 2009 year saw us make progress towards meeting our corporate objective which is to double the volume and value of the Hardy business in the five year period between 2008 and 2012.

Gross written premiums were increased by 40% to £242.0m (2008: by 17% to £172.8m), the increase being derived principally from the continuing growth in the non-marine property elements of the underwriting portfolio, although all of the business units have advanced in the period. The profit before tax of £20.1m (2008: £23.1m) has once again been impacted by foreign exchange movements and the position on a like for like basis, excluding the effects of foreign exchange, is £26.7m for 2009, as compared to £4.4m for 2008, with combined ratios excluding foreign exchange of 78.1% and 91.2% for 2009 and 2008 respectively.

Hardy's low risk investment strategy produced a return of 1.7% in 2009. Our conservative strategy of holding high quality, short duration assets yielded a high return in 2008 (5.2%). In 2009's investment environment, however, the outcome has reversed. We do not expect to change our approach now and a short position as regards duration will be maintained, since

our investment objectives are biased towards protecting the portfolio against unnecessary losses and avoiding volatility.

The underlying underwriting years of account which have contributed to these results are performing well.

For 2007 and 2008, syndicates 382 and 38*Twenty* were underwriting side by side and for 2009 of course, the underwriting portfolios have been merged. Essentially the traditional Hardy lines of business were in syndicate 382 (aviation, marine, specialty lines and a modest amount of US- based property catastrophe treaty business). The new interest in direct and facultative property risks and in an expanding property treaty book, which includes both US and international risks, were developed in syndicate 38*Twenty*.

The traditional lines have been suppressed by the rating environment and by recession-related claims and although the 2007 year of account will close with a profit of 12.8% of capacity, we are forecasting a smaller profit at the close of the 2008 year in the range 2½% to 7½%. In its start up year in 2007, syndicate 38*Twenty* had lower premium volumes than originally forecast, resulting in a higher proportionate reinsurance cost. It suffered some significant losses but despite all this, it will close with a profit of 4.9%. The 2008 year is doing well and is coming into its own, forecasting a profit on capacity in the range 15% to 20%.

For 2009, the merged syndicate 382 is looking good but it is far too early to make any predictions.

With hindsight, our decision to diversify into non-marine property lines looks to have been the right one and at broadly the right time.

Although our involvement is modest, we continue to be watchful of the potential for deterioration in those classes of business which are susceptible to claims associated with the recession. As a result, we have increased our general margin within the reserves to reflect the weak economic climate. The adequacy of our historic reserving approach is once again demonstrated by the prior year release of reassessed reserves of £9.8m (2008: £6.4m).

Gross Written Premium (£000)

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Year End	49,475	59,176	87,281	111,276	106,066	147,534	172,770	241,996
Half Year	28,229	42,141	51,694	65,577	58,353	88,836	97,048	149,870

Net Earned Premium (£000)

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Year End	35,486	45,334	68,392	85,465	79,994	108,600	120,799	176,630
Half Year	15,846	20,919	32,041	43,773	44,381	48,932	60,922	86,671

Combined Ratio

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Year End	82.7%	81.2%	94.3%	92.7%	76.9%	80.5%	91.2%	78.1%
Half Year	91.2%	79.8%	80.0%	82.7%	84.4%	79.5%	85.0%	75.7%

Net Tangible Assets Per Share (pence)

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Year End	142.0	163.7	156.6	163.8	173.1	198.3	245.4	266.2
Half Year	140.0	156.0	185.0	163.9	166.4	181.7	212.8	247.4

Basic Earnings Per Share (pence)

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Year End	16.2	28.6	27.9	15.3	34.1	38.4	55.4	36.8
Half Year	5.9	12.9	30.0	15.4	11.8	18.8	20.9	15.1

The merger of syndicates 382 and syndicate 38*Twenty* which was effective from the 2009 year onwards has worked well. The creation of the four business units as the focus for performance monitoring and business development has enhanced the overall efficiency and transparency of our business infrastructure.

During 2009, we have continued to push forward across all four business units with a view to securing the growth for which we are now very much ready. While this modernisation is essential to the next phase of our development, the traditional core underwriting philosophies and values which define our culture, are still very much in place, being:

- a desire to show leadership in pricing wherever possible, so as to maximise our ability to influence price;
- a prudent approach to reserving;
- diversification of the portfolio;
- maintenance of a predominantly short tail focus.

Hardy Bermuda Limited commenced underwriting in mid-May. Its primary focus is to enhance the diversification of our US property treaty portfolio and so our underwriting team is targeting accounts which did not otherwise feature in the existing book. We are pleased with the steady but sure progress that we are making and expect to get further traction during 2010. We also plan to underwrite a portfolio of direct and facultative property risks from there, again targeting accounts which would not typically surface in London or which we might not be shown because of greater competition.

We have successfully diversified the non-marine direct property unit further by the recruitment of a lead construction and engineering underwriter who has already made an impact in business terms. He will develop an international portfolio for us but will have a particular interest in the Middle Eastern joint venture company - Hardy Arig Insurance Management Limited (HAIM) - that we have established in conjunction with our Bahraini partner, Arig, since we see many opportunities there for this class of business.

This is an excellent example of how we see the business moving forward – that is, organically, with new lines of business and new geographies being introduced wherever possible, thereby seeking to reduce execution risk by building on what we know already. In this vein, we have decided to establish a footprint in Singapore and also to develop our current modest involvement in liability classes. Our underwriting agency board will work on the detail of these new initiatives during 2010. I should make clear, however, that Hardy is not currently intending to underwrite any US casualty business.

We see the organic route forward as the most effective for a business of our size. Unfortunately, however, our progress towards our planned growth may now, given the current market rating environment, be delayed. We are therefore taking a more proactive approach towards business development, which will be assisted by our head of business development, Tim Griffin, a role that was created during 2009.

Gross Premiums by Year of Account

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Marine & Aviation	48.9	64.5	64.3	62.2	61.6	53.8	45.9	48.0
Non-marine property	0.2	1.7	8.6	7.7	14.5	32.0	28.8	37.2
Specialty Lines	0.9	5.6	21.0	23.2	21.4	24.8	31.3	36.8
Property Treaty	7.3	10.6	10.6	9.3	10.1	31.5	48.2	76.9
Total	57.3	82.3	104.5	102.3	107.7	142.1	154.2	198.8

The extent of the business development and the continued diversification of the Hardy underwriting portfolio in recent years is illustrated above. We have made enormous progress in building underwriting capabilities where previously we had none. The challenge is now on maintaining momentum as we move into phase two of our growth, exploiting the new skill sets and the sophistication of the infrastructure which we have created.

Business Unit Reviews

Marine and Aviation

Head of business unit – Mervyn Sugden

Gross Premium and Ultimate Loss Ratios by Year of Account (£'000)

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>
Gross Written Premium	55,113	59,629	60,259	59,032	48,969	45,254	44,977
Ultimate Loss Ratio	66%	84%	68%	64%	80%	89%	86%

2010(F) Gross Premium for the 2010 Year of Account

Aviation	33%
Cargo and specie	33%
Marine hull	34%

Overview

The marine and aviation business unit embraces the traditional focus of the Hardy business, with Mervyn Sugden, the business unit manager, having underwritten for syndicate 382 since it was established in 1975. The teams for both the marine and aviation elements of the portfolio demonstrate lead underwriting capability and a keen focus on profitability. These market sectors are struggling in pricing terms currently, but growth in world trade and a reduction in available capital triggered by early aviation losses could see that situation change dramatically.

Marine

For the marine hull account, the 2009 year started with promise and clean business was securing rises of 5% or more. As the year progressed, these rises largely disappeared and only risks with a poor claims record received the correction in terms that they deserved. The shipping industry has suffered badly from the effects of the recession, with many vessels either idle or laid up. The resulting dramatic fall in insurable values has eroded premium levels further.

Unfortunately, we see little change in the first half of 2010 with a continuing flat market but our expectation is that there will be a hardening in rates towards the end of the year as the continuing poor market hull results emerge. We intend to strengthen the account by continuing to develop the modest liability and energy books and also broadening further into other marine classes where we currently have little involvement.

The 2009 year was difficult for cargo business, with soft rating levels encouraged by surplus capital. Premium volume is still somewhat depressed following the world wide slump in trading activity. It is, however, expected to pick up again in 2010. Pricing remains critical and in Lloyd's, while some reductions have been given, these have not been as bad as originally feared, possibly due to increased monitoring of rating methodologies by managements and by Lloyd's centrally.

The specie market has been harder in 2009 owing to more volatile loss experience generally. We have not seen any real reductions to speak of and moreover some areas of the account are starting to attract rate rises. The jewellers block account has had a particularly difficult year, largely due to an increase in recession related claims. Rates need to increase or we may not continue writing this business.

Aviation

Once again, aviation insurers have had a challenging year. We anticipated that following several years of losses and an increased cost of capital there would be a significant uplift in rates across the airline insurance sector during the year. The early part of 2009 did indeed show some promise albeit driven by further significant losses. Unfortunately the latter part of the year, during which many of the "major" airlines renew, saw a great reluctance in the market to charge significant rating increases. Given our focus on only writing business at

rates which should return a gross profit, this weakening in the market inevitably restricted the volumes of business written.

The general aviation market continued to suffer from overcapacity during the year which has had the inevitable effect of holding rates down. This has even been the case in areas which have suffered from an exceptionally poor loss experience in the last 12 months. The offshore helicopter sector has suffered a number of major losses and for a brief period this did lead to some sizeable rate increases. As in the case of the airline market, however, by the last quarter, the resolve of underwriters to increase rates seemed to evaporate.

We can only hope that the talk of a focus on better pricing going forward becomes reality, especially following the early 2010 airline fatalities and hull claims, although we will continue to be more than happy to take advantage of one of the curiosities of the market, namely the opportunity to participate at better than leader's terms on many risks.

**Non-marine property
Head of business unit – Patrick Gage**

Gross Premium and Ultimate Loss Ratios by Year of Account (£'000)

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Gross Written Premium	1,584	8,032	6,942	14,175	30,744	28,921	37,148
Ultimate Loss Ratio	64%	128%	64%	96%	74%	49%	62%

2010(F) Gross Premium for the 2010 Year of Account

Direct & fac property	68%
Direct property	32%

Overview

This account comprises direct and facultative property insurance of both industrial and commercial risks (mines, factories, refineries, commercial property portfolios) and residential and small commercial risks. The large risks are written on a worldwide basis and the residential and smaller risks are geographically more focused on the UK. For 2009, a construction and engineering account was introduced for the first time.

2009 started on a generally positive note, with rate increases being applied to the large risk account. As the year developed, however, rates gradually stabilized and we are now seeing a more or less flat position on a risk adjusted basis. We are already experiencing some downwards pressure on rates in 2010 following a relatively benign year with regard to loss activity. Our own claims experience in 2009 has been low and the account has performed extremely well.

The UK property market, both commercial and residential, continued to bump along the bottom of the underwriting cycle during 2009. Promisingly, however, we are now able to

carry selective rate increases on some accounts and have managed to impose a general rate increase on our homeowners business.

During 2009, our high net worth underwriting team was fully integrated into Hardy and into this business unit. We will continue to build our risk profiling and general management information capability during 2010, so as to enhance our control over the data emanating from the coverholders who are the source of this business.

Further expansion last year included the commencement of a construction and engineering account, which will focus on large contracts and infrastructure projects worldwide. We expect to write around £10m of premium income during 2010, with a significant proportion of Middle Eastern business generated from our joint venture initiative with Arig.

We have continued to develop our catastrophe modelling capability and our focus remains firmly on risk selection and rating adequacy. Premium volumes are expected to grow through the addition of new niches such as the construction account, although elsewhere we anticipate volumes to remain more or less the same as for 2009.

Property Treaty
Head of business unit – David Carson

Gross Premium and Ultimate Loss Ratios by Year of Account (£'000)

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Gross Written Premium	9,735	12,370	11,878	9,876	30,430	48,899	74,998
Ultimate Loss Ratio	17%	132%	157%	13%	31%	53%	50%

2010(F) Gross Premium for the 2010 Year of Account

Crops	1%
International Non Marine Cat XL	44%
Kyosai	15%
Proportional Treaty	14%
Risk Excess	3%
US Non Marine Cat XL	23%

Overview

The property reinsurance account generates most of the catastrophe exposures underwritten by the Group. Business is underwritten both in London and through our Bermuda office. The profile of the account is 70% international and 30% US which makes it atypical as compared to the average Lloyd's catastrophe treaty portfolio which is approximately two thirds US orientated. The account is protected with significant amounts of reinsurance, particularly in the form of quota share treaties.

Whilst remaining committed to the UK and US, over the last three years, the Hardy account has broadened its geographical base with much more emphasis on international (that is, non-US) business in order to create a more diversified portfolio. Japan, in particular, has been a focus for development as well as the Caribbean which are both areas in which the team has a strong lead position. Where opportunities have presented themselves elsewhere due to post-loss market dislocation (e.g. Australia), the team has been quick to take advantage. The non-catastrophe portion of the overall portfolio (particularly, the Japanese “Kyosai” book) continues to grow and add balance.

A significant development during 2009 was the commencement of underwriting by Hardy Bermuda Limited in May, concentrating on US catastrophe business produced from US domestic brokers. Whilst we are happy with the progress being made, it is clear that development will initially be slow. There is considerable over-subscription and we are often signed down heavily. This is a long-term commitment, however, and we are prepared to be patient.

2009 was a benign year in terms of catastrophes with the most significant events being the Black Saturday Victorian bushfires in Australia in February, and the Alberta storm in Canada in August. The widely predicted above-average activity for the hurricane season, thankfully, failed to materialise.

Lloyd's (and Hardy in particular) is seen as a secure reinsurer and this has resulted in an improved showing of business and new opportunities as clients continue to seek to increase the syndication of risk worldwide. Written income was ahead of original projections, helped by rate increases and some currency appreciation.

Conditions for 2010 are getting tougher and the 1st January 2010 renewals were much later than usual. The market, however, is not soft. Reinsurance rates have been, and will continue to be, pretty resilient. Whilst we have had to give up some margin, our book is being underwritten at reasonable rates and we remain selective and cautious.

Specialty Lines

Head of business unit – Adrian Daws

Gross Premium and Ultimate Loss Ratios by Year of Account (£'000)

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Gross Written Premium	5,265	21,881	21,991	20,329	21,959	29,411	36,564
Ultimate Loss Ratio	64%	80%	26%	69%	57%	93%	64%

2010(F) Gross Premium for the 2010 Year of Account

Conveyancing	1%
Financial Institutions	33%
Political Risks	11%

Special Risks	28%
Terrorism	27%

Overview

This business unit continues to provide considerable diversification to Hardy's overall risk profile and accordingly, provides benefits from a capital perspective. The key areas remain financial institutions, political risks, terrorism, accident & health and conveyancing, although this latter account will in future reduce in significance and will be underwritten only via a reinsurance treaty. The rating environment for the financial institutions and political risks classes is improving, as a result of the difficult economic climate and related loss activity.

Financial institutions

Claims activity has increased in this class as a direct result of the credit crunch. A conservative and thorough underwriting approach has, however, protected the Hardy account from the worst of the problems. The 2009 year saw a significant improvement in the market environment for this class and we have taken advantage of improving rating conditions to grow the account by more than 20% over the year. A focus on accessing the first party fidelity element of the book remains key to our underwriting philosophy and we continue to avoid writing D&O coverage. We expect favourable conditions to continue in 2010.

Political risks

The political risk and trade credit account continues to be targeted towards doing business with a number of well established and trusted clients, and to risks which are for shorter periods than is the market norm: our average contract duration for 2009 is less than 296 days. Though the market did not harden as we would have wished over the course of 2009, the numbers and quantum of notified loss circumstances, mostly avoided by syndicate 382, make significantly more favourable market conditions inevitable. We therefore envisage some growth in this account for 2010.

Terrorism

The terrorism account has become a significant part of the specialty lines business unit. Increased market capacity has meant that underwriting conditions have continued to deteriorate over the last twelve months and there is no prospect of this changing in the near term, especially given the profitable results. Hardy continues to access the specialised areas of the account, which are seeing less pressure on rates, rather than the commoditised mainstream terrorism book.

Conveyancing

The rate of growth in the conveyancing account has slowed this year due to the performance of the UK residential housing market. This account will become much less significant in 2010 and will be underwritten via a reinsurance treaty.

Accident and health

This has become a more significant part of the business unit with the continued development of a profitable coverholder relationship, focusing on international risks.

Business and Competitive Environment

The broad business environment is one of continued uncertainty but Hardy is, to a large extent, insulated from problems in the UK economy. We are a small specialist business,

competing in an international market and we punch well above our weight because we are part of the Lloyd's franchise. We have been able to grow and to deploy our £40m new capital successfully, taking advantage of business opportunities in spite of excess capital in the sector.

The bigger picture is not as encouraging as we would have hoped for, however, since this capital has been used as a means of maintaining or boosting premium volumes and encouraging competition, which is most marked in non-catastrophe exposed lines.

As well as business challenges from the current rating environment we are also vulnerable to the financial risks of low investment returns and exchange rate volatility.

Perceived wisdom, and indeed the historic data analysis, suggests that in periods of low investment returns, underwriting margins improve, the logic being that with low investment return to supplement overall results, there needs to be a greater focus on underwriting as the means of generating profit. Certainly this will be the case at Hardy. The focus on underwriting discipline will be absolute because with our cautious investment strategy, we expect our investment return to be modest.

Exchange rate volatility has become a significant feature in determining performance and is of particular relevance in Lloyd's given the requirement on us to hold currency in trust funds, limiting our ability to manage these funds actively except as regards an emerging surplus or deficit, albeit that a compulsory matching of assets and liabilities does create a helpful natural hedge. As we have noted before, the treatment of exchange differences on non-monetary balances, imposed by International Financial Reporting Standards, adds a further layer of complexity. In common with other insurers, we have adopted disclosure of key performance metrics both before and after the effects of foreign exchange, in an attempt to show the real performance of the business: the result over which we have control.

One of the key issues for everyone in our industry is the implementation of the Solvency II directive. We are sensibly committing time, money and resource to this project over the next 3 years and our budget is approximately £1m for each of those years over and above the costs of ongoing risk management and other development work. Aside from the obvious risks associated with underwriting, this is the single biggest issue affecting the business environment. It is an imperative for us to secure approval of our internal capital model and to be able to demonstrate the existence of effective and embedded enterprise risk management. The consequence would be that our capital would be determined by reference to the standard formula set out in the Directive, which would most likely have the effect of significantly increasing our regulatory capital requirement. This is not an acceptable alternative so we will do all it takes to secure the necessary approvals, while at the same time, using the Solvency II initiative as an opportunity to deliver significant operational enhancements to the business which will undoubtedly create opportunities for us in the future.

It is to be hoped that this attempt to level the playing field and create consistency across Europe (and more globally) in insurance and reinsurance solvency standards will succeed. We can see a great deal of business benefit and helpful cultural change as a result but would not want to see a gold plated implementation and enforcement regime applied only in the UK.

Current trading and prospects

Our underwriting capacity for 2010 is £300m, up by £50m from the level in 2009, made possible by the capital raised in 2009 which is now fully utilised.

We have already described the patchy condition of the rating environment. The likely net increase in premium volume will therefore be a combination of the new niches which we are developing (eg the construction and engineering portfolio), a retreat from existing business where rates are inadequate and some growth in the lines of business where rating improvements are being seen or where rates are flat or retreating but are nevertheless above the appropriate benchmark.

The rating table below, which summarises the position at 1 January, shows clearly the disparity in rating across the different business units.

Analysis of 1 Jan 2010 renewals gross written premiums, £000's

	<u>2009</u>	<u>2010</u>	<u>Movement</u>	<u>Renewal rate change</u>
Marine & aviation	13.4	12.6	-0.8	-0.4%
Non-marine property	20.1	21.4	1.3	5.4%
Specialty lines	8.1	3.7	-4.4	-2.9%
Property treaty	42.6	42.3	-0.3	2.2%
Total	84.2	80.0	-4.2	2.6%

All figures at Q4 09 rates of exchange
 Premiums include commissions and brokerage

The continued growth in the property lines of business and their significance to the overall underwriting portfolio for syndicate 382 is now quite pronounced. Our original intention had been to maintain the size of each business unit at broadly similar levels, but with property reinsurance pricing in the ascendancy for the last 24 months, and the specialty lines and marine and aviation rates flagging, this did not prove to be possible. The specialty lines unit may, however, be about to have its moment to advance since financial institutions business and the political risks class look promising from a rating perspective. We are ever hopeful of the potential for a hardening of the aviation market, although in recent times, this has been at most inadequate and usually non-existent. While we are still assessing our exposures to the recent Chilean earthquake, it seems clear that it will have a stabilising effect on rating levels in the region and possibly more widely.

A mixed or difficult trading environment does not fill the Hardy team with special concern. The lack of investment return is disappointing but with a predominantly short tail book of business, we have never factored the potential for investment returns into our rating models anyway. Furthermore, Hardy has typically shown more outperformance in challenging market conditions, so a continued focus on underwriting discipline is the order of the day.

Despite the rating environment, we see the scope for Hardy to consolidate recent growth and changes in infrastructure and resources and to push forward into phase two of our development.

We have several opportunities which will assist with that.

Our joint venture with Arig, HAIM, is already delivering new risks from the construction and property sectors in the Middle East. The business plan estimates of volume from this source are modest but the potential is considerable over the coming years. As referred to earlier, we will be researching further and initiating the opening of an office in Singapore during 2010 and also looking closely at the liability sector in the UK. These two agreed initiatives have not been factored into the business plan as yet.

There is also the potential to develop other hubs internationally. Our view is that, amongst other things, technology is making the world a much smaller place and that, over time, it is ever more likely that local markets will gain greater significance. Since we suspect that this will lead to less local business coming to Lloyd's, it will be important, if we wish to sustain our growth, that we go to those markets and underwrite there. Certainly, Bermuda, Bahrain and Singapore fit this template and wherever possible, we will be targeting non-correlating non-catastrophe exposed business.

We are, however, Lloyd's centric and it bears repeating that as far as possible, wherever we locate our business, we will be enhancing syndicate 382's portfolio and offering Lloyd's security. We see no point for a business of our size in capitalising separate companies in local jurisdictions: this is simply inefficient and wastes the opportunity for further capital optimisation from diversification.

Finally, we also see further opportunities to enhance the property treaty portfolio although these will need to be contained, in accordance with our risk appetite, until the other business units move ahead to provide the balance. Alternatively, there are possibilities of underwriting further catastrophe exposures with third party capital: a temporary option until we are satisfied that it would be appropriate in risk appetite terms, to absorb the business back into syndicate 382's portfolio. Following further enhancement of our modelling capabilities, our team offers first class exposure monitoring and where we are able to access well-rated business, we will explore the possibility of writing excess business on behalf of others.

Overall, the prospects for further growth in the business are good. The AM Best affirmation of the A (excellent) rating for syndicate 382 on the basis of, inter alia, good prospective performance reinforces this. There is little doubt that we are seen as an employer of choice and we have every opportunity to recruit or enlarge our business base by selecting from the best available. A year ago, our key assumption was that a recovery in our market would be slow, but sustained. This assumption is looking somewhat stretched but remains valid we believe: certainly in terms of the circumstances of Hardy. Our strategy to grow volume and value is very much intact, albeit that in timetable terms, delivery of the strategy may be delayed slightly.

Capital and dividends

The £40m capital raised in 2009 has been put to use in supporting the 2010 business plan, enabling us to take decisions about reinsurance buying in an environment of rational debate

on expense versus value, as opposed to need. For 2009, our return on equity has inevitably been diluted, but should improve in 2010 as increased volumes begin to flow through.

The letter of credit which we have traditionally used for regulatory capital purposes has been renegotiated and its quantum has been increased from £35m to £50m, albeit that it is in fact denominated in US dollars, being the primary currency of our exposures. There are now three rather than two supporting banks which gives us greater flexibility as we move forward and expand further. The incremental value of the LOC is not currently being fully utilised, which gives us some comfort in the event that sterling weakens further and that capital requirements increase as a result of higher premium volumes. It also means that new opportunities could be factored into the business plan without the need to refer to shareholders for further funds. In this context, we are initiating a detailed review of reinsurance strategy to ensure that the mix of the financial support which we derive from reinsurance as compared to our own capital base is at its most appropriate and efficient. Meanwhile our recoverables as a percentage of net assets are low for the sector, illustrating that there is no excessive reliance on reinsurance.

The Hardy balance sheet is strong and continues to be managed on a prudent basis with a focus on capital discipline. We have undertaken a lot of work during 2009 in clarifying our risk appetite and in satisfying ourselves that we are appropriately geared given that appetite. We are seeking to ensure that the long term growth aspirations of the business are capable of being financed, while at the same time ensuring that shareholders receive appropriate rewards in exchange for their ongoing support. Our progressive dividend policy of increasing the dividend by 10% annually is very much in keeping with this. We will therefore be proposing a total dividend of 13.3p, of which 4p has already been paid as an interim dividend. A further 9.3p will be paid as a second interim dividend on 1st April 2010.

Governance

We recently announced some changes to the composition of our Board, specifically two new non-executive directors, Fiona Luck and Anthony Taylor and also a new executive being Adrian Walker, Hardy's director of underwriting. Adrian had previously been on the Board of the group's holding company but stood down during the Bermuda redomiciliation process. The calibre of these recruits to HUB's Board is a testament to our ambitions for the future of the business.

We have been watching developments on corporate governance and on remuneration policies (from the Walker report and from the FSA) with great interest. Although there is nothing to date which explicitly applies to an insurance business of our size, we have taken the step of embracing what we believe will become best practice in the financial services sector and have introduced a new bonus scheme under which the profit pool available for the scheme will be adjusted by reference to some accepted industry performance metrics and also by reference to individual performance. We have also introduced requirements for compulsory bonus deferral for the senior team together with minimum shareholding requirements. We are more than happy to do the right thing on this front but might find it more difficult if the full weight of Walkers' proposals on non-executive directors were to be applied to us, which would quite likely result in more difficulty in retaining or attracting high calibre individuals going forward. We hope for some proportionality.

Relationships with Intermediaries

We continue to believe in the power of face to face negotiation between our underwriters and the brokers who support us but acknowledge the need for change in both risk

placement and claims handling processes. We have been progressively improving our claims performance and as new business lines emerge, we have been developing our claims expertise in tandem. The team is encouraged to deal with brokers and clients in the way that they themselves would wish to be treated. Nowhere is this more important than for our high net worth retail customers.

As a market, we need to ensure that the London market is not more expensive because it is inefficient, but rather because it truly adds value to complex, large and hard to place business. We are totally committed to participating in the various market projects which will help to identify the most appropriate way forward and to create tangible benefits for the market.

Our view is that, in an attempt to secure growth, the boundaries of the responsibilities between brokers, particularly the small and medium sized ones, and underwriting businesses are becoming blurred, with both seeking to acquire managing general agent capabilities to secure the source of business and to share in the wider spoils of underwriting profits. This will inevitably be an issue for the Hardy group too, and over time it seems more likely that as well as developing hubs in local markets to build business from scratch, we might also contemplate acquiring existing MGA franchises. We are already talking to our key brokers about this issue with a view to finding a route forward which will not disturb the current London market relationships which are so important to us.

The Hardy team

We have made a lot of changes in recent years and 2009 was no exception. The operational and cultural challenges which the entire team have grappled with have been tremendous. Going forward, the team will need to remain focused and enthusiastic and in an attempt to mitigate the dampening effect of the patchy market, there will be renewed encouragement in 2010 on the development of a more customer-orientated culture.

Our continued progress towards meeting our corporate goals will not happen without the effort, goodwill and co-operation of the team, to whom I remain indebted.

Conclusion

Phase one of our growth was very much associated with putting some new skills and building blocks in place. Phase two is now about exploiting these advantages.

We cannot assume, however, that our corporate objectives can be met simply by organic growth of existing lines of business or geographies, and our pipeline of opportunities is therefore being actively progressed.

The Hardy team that we have assembled certainly gives us grounds for optimism about the longer term future of our business.

Barbara J Merry
Chief Executive

FINANCIAL REVIEW

Summary of results

The pre-tax profit for the year of £20.1m (2008: £23.1m) is a strong result, generated from a record underwriting performance for the Group. The result has been materially impacted by foreign exchange movements, and we have experienced a reversal of much of the gain from which we benefited last year.

Notwithstanding the foreign exchange volatility within our results, underwriting performance is very good and the combined ratio excluding foreign exchange effects is 78.1%, compared to 91.2% last year.

Return on equity for the year was 13.4 per cent., bringing the five year weighted average to 16.0 per cent.

	2005	2006	2007	2008	2009
	£'000	£'000	£'000	£'000	£'000
Gross premium written	111,276	106,066	147,534	172,770	241,996
Net insurance premium revenue	85,465	79,994	108,600	120,799	176,630
Total underwriting return	3,834	21,947	19,391	8,667	34,346
Investment income	5,043	6,025	6,234	7,790	5,648
Other income	803	512	587	284	297
Other charges	5,313	6,660	7,445	10,648	11,956
Finance charges	315	640	1,966	1,715	1,594
Profit before tax and foreign exchange	4,052	21,184	16,801	4,378	26,741
Foreign exchange (loss)/ gain	3,422	(4,347)	1,467	18,715	(6,641)
Profit before tax	7,474	16,837	18,268	23,093	20,100
Post tax return on equity	8.3%	17.8%	17.7%	22.9%	13.4%
Basic earnings per share	15.3p	34.1p	38.4p	55.4p	36.8p
Interim dividend per share	-	-	3.3p	3.6p	4.0p
Final / second interim dividend per share	8.25p	10.0p	7.7p	8.5p	9.3p

Return on equity is calculated as profit after tax expressed as a percentage of opening net assets adjusted for the proceeds from the placing and open offer with effect from 1 April 2009.

Underwriting performance

The increase in gross premium volumes by 40% from £172.8m to £242.0m is attributable to further development of the property treaty portfolio and also to the new lines of business that we introduced late in 2008, for 2009, the principal examples of which are the Japanese Kyosai portfolio and the high net worth property account. Some existing business, particularly the catastrophe exposed property classes have also benefited from an improved

rating environment; at least in the early part of the year as a result of the claims activity seen during 2008.

The rating environment in the other two divisions, however, has been less attractive. Marine and aviation, in particular, has been relatively weak and the result has been adversely affected by an increase in attritional claims activity, much of it being driven by the economic environment and recession.

The conservative reserving approach adopted at the year end to address the high levels of attrition in 2008 have protected Hardy from the need to uplift reserves in the period, and therefore, a reassessment of earlier year reserves has resulted in releases across all business units.

Year to 31 December 2009

	Marine and aviation	Specialty lines	Non marine property	Property treaty	Total reportable segments	Effect of foreign exchange on non-monetary items	Other foreign exchange	Total
	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m
Gross written premium	63.9	40.7	53.0	84.4	242.0			242.0
Net earned premium	61.8	34.0	37.5	51.0	184.3	(7.7)		176.6
Current accident year claims	(39.4)	(18.9)	(15.0)	(19.7)	(92.9)			(92.9)
PY claims (release)	0.6	2.3	5.1	1.8	9.8			9.8
Net claims incurred	(38.8)	(16.5)	(9.9)	(17.9)	(83.2)			(83.2)
Insurance expenses (ex FX)	(20.8)	(10.4)	(13.1)	(16.5)	(60.8)	1.7		(59.1)
Underwriting result (ex FX)	2.2	7.0	14.5	16.7	40.4	(6.0)	0.0	34.3
Foreign exchange loss					-	(4.4)	(2.2)	(6.6)
Underwriting result	2.2	7.0	14.5	16.7	40.4	(10.4)	(2.2)	27.7
Claims ratio	62.8%	48.7%	26.5%	35.1%	45.1%			
Current accident year	63.7%	55.5%	40.0%	38.7%	50.4%			
Expense ratio (ex FX)	33.6%	30.8%	34.9%	32.2%	33.0%			
Combined ratio	96.4%	79.5%	61.4%	67.3%	78.1%			

Year to 31 December 2008

	Marine and aviation	Specialty lines	Non marine property	Property treaty	Total reportable segments	Effect of foreign exchange on non-monetary items	Other foreign exchange	Total
	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m
Gross written premium	47.9	48.1	26.2	50.6	172.8			172.8
Net earned premium	43.9	29.5	16.7	33.4	123.5	(2.7)		120.8
Current accident year claims	(27.7)	(19.7)	(12.0)	(16.6)	(76.0)			(76.0)
PY claims (release)	3.3	2.0	(1.0)	2.1	6.4			6.4
Net claims incurred	(24.4)	(17.7)	(13.0)	(14.5)	(69.6)			(69.6)
Insurance expenses (ex FX)	(14.7)	(13.1)	(6.2)	(9.1)	(43.1)	0.6		(42.5)
Underwriting result (ex FX)	4.7	(1.3)	(2.5)	9.9	10.8	(2.2)	0.0	8.7
Foreign exchange loss					-	11.6	7.1	18.7
Underwriting result	4.7	(1.3)	(2.5)	9.9	10.8	9.5	7.1	27.4
Claims ratio	55.8%	59.9%	77.7%	43.2%	56.3%			
Current accident year	63.1%	66.8%	71.9%	49.7%	61.5%			
Expense ratio (ex FX)	33.5%	44.6%	37.1%	27.1%	34.9%			
Combined ratio	89.3%	104.5%	114.8%	70.3%	91.2%			

Foreign exchange

The Group's result for the year has been depleted by a loss on foreign exchange of £6.6m. This includes a loss of £2.3m with respect to differences in the retranslation of monetary assets and liabilities which are denominated in non sterling currencies. The balance of the foreign exchange loss of £4.3m relates to non-monetary items, which are carried at historic rates.

The accounting treatment for non-monetary items under IFRS has a tendency to magnify the impact of movements in foreign exchange rates. This is due to requirements to carry non-monetary items at the foreign exchange rate prevailing at the time of initial recognition without revaluation to the closing exchange rate. There is, therefore, a mismatch between the exchange rates used to convert non-monetary items and monetary items, which generates volatility in the results for the period. The main non-monetary items are unearned premium reserves and deferred acquisition costs.

As at 31 December 2009, the difference between recognising non-monetary items at historic rather than closing rates of exchange was an additional £0.5m net liability. As at 31 December 2008, the additional net liability was £9.8m. The loss in the period reflects the combination of the unwinding of the brought forward difference and the closing position. This notional adjustment for foreign exchange movements on non-monetary items has been

presented to show the effect that the required accounting treatment has on the profit before tax for the period.

Effects of foreign exchange on non-monetary items:	Year ended		Year ended	
	31 December 2009		31 December 2008	
	£'000		£'000	
UEP and DAC items at historic rates	64,902		58,215	
UEP and DAC items at closing rates	64,367		68,064	
Valuation difference in closing balance sheet	(535)		9,849	
Valuation difference in opening balance sheet	(9,849)		(372)	
	<u>(10,384)</u>		<u>9,477</u>	

In addition the group has recognised a foreign exchange loss of £2.3m reflecting the translation of net monetary assets denominated in foreign currencies and trading activities in the normal course of business.

Foreign exchange (losses) / gains arising from:	Year ended		Year ended	
	31 December 2009		31 December 2008	
	£'000		£'000	
Translation of balance sheet and income statement	(2,276)		7,072	
Maintaining UEP and DAC items in the balance sheet at historic rates	(10,384)		9,477	
Maintaining UEP and DAC items in the income statement at historic rates	6,019		2,166	
	<u>(6,641)</u>		<u>18,715</u>	

The element of the foreign exchange loss on non-monetary items relating to the translation of the income statement at average exchange rates is reclassified to premium and insurance expenses and this can be seen in the segmental analysis of the results shown in the above tables.

Investment performance

Investment returns contributed £5.6m (2008: £7.8m) to the result for the year, reflecting a significant reduction in the returns achieved last year, on a pot of investable assets which is considerably larger than before, primarily as a result of the capital raising. The 2009 return also included a profit of just over £1m arising from foreign exchange derivative contracts entered into to hedge foreign exchange risk.

The asset allocation policy remains very conservative, with a significant proportion of fixed income securities. Although Hardy has a long term appetite for equities, there has been no return to that asset class on the grounds of continued material uncertainty and too great a potential for downside risk.

The investment return for the period is set out below.

Investment return	Year to 31 December 2009			Year to 31 December 2008		
	Average balance	Return	Return	Average balance	Return	Return
	£'000	£'000	%	£'000	£'000	%
Equities	-	-	-	1,531	101	6.6%
Fixed income	160,556	3,969	2.5%	116,062	7,160	6.2%

Cash and deposits	104,521	635	0.6%	79,719	2,988	3.7%
	265,077	4,604	1.7%	197,312	10,249	5.2%
Fair value gain / (loss) on foreign exchange contracts		1,044			(2,459)	
		5,648			7,790	

Summary balance sheet

	2005 £'000	2006 £'000	2007 £'000	2008 £'000	2009 £'000
Intangible assets	9,781	15,509	15,509	15,509	15,509
Financial investments and cash	123,472	141,950	173,410	234,828	290,619
Reinsurance assets	33,310	31,330	40,006	59,227	68,019
Other assets	54,530	55,276	80,247	101,430	125,825
Total assets	221,093	244,065	309,172	410,994	499,972
Insurance liabilities	133,708	129,065	173,191	238,624	279,554
Subordinated debt	-	14,851	14,643	20,256	18,136
Other liabilities	19,793	23,352	36,130	50,385	50,191
Total liabilities	153,501	167,268	223,964	309,265	347,881
Total equity	67,592	76,797	85,208	101,729	152,091
Net assets per share	191.4p	216.9p	242.5p	289.5p	296.4p
Net tangible assets per share	163.8p	173.1p	198.3p	245.4p	266.2p

Intangible assets

The Group completed the acquisition of the remaining third party capacity on syndicate 382 during 2006. The total cost to acquire the capacity was £15.5 million, representing an average cost of 6.2 pence per pound of the syndicate 382 capacity for the 2009 year of account.

Financial investments and cash

The Group adopts a conservative investment strategy, which limits exposure by asset class, credit quality and issuer. The application of this policy has meant that at the year end all assets are either held in fixed income securities, money market investments or deposits. All assets are short dated, highly liquid and have a high credit rating.

The day to day management of the fixed income portfolio is undertaken by an outsourced investment manager, Amundi (UK) Limited, previously known as Credit Agricole Asset

Management. The performance of the manager and compliance with the Group's investment guidelines is monitored by the Finance Committee.

The Group has a limited appetite for equity investments and other alternative asset classes, although during 2008 took the decision to exit these asset classes in order to reduce its risk profile.

The allocation over the main asset classes is set out below.

	As at 31 Dec 2009		As at 31 Dec 2008	
	£'000	%	£'000	%
Fixed income	192,365	66%	129,758	55%
Cash and deposits	98,254	34%	105,070	45%
	<u>290,619</u>	<u>100%</u>	<u>234,828</u>	<u>100%</u>

The fixed income portfolios are analysed by asset type and credit rating below.

As at 31 December 2009	Holding		Credit rating		
	£'000	%	AAA	AA	A
Government	109,419	57%	57%	0%	0%
Government agency	29,311	15%	9%	5%	1%
Supranationals	11,302	6%	6%	0%	0%
Corporate	42,333	22%	5%	15%	2%
Fixed income securities	<u>192,365</u>	<u>100%</u>	<u>77%</u>	<u>20%</u>	<u>3%</u>

As at 31 December 2008	Holding		Credit rating		
	£'000	%	AAA	AA	A
Government	78,647	61%	61%	0%	0%
Government agency	25,373	19%	13%	6%	0%
Supranationals	15,064	12%	12%	0%	0%
Corporate	10,674	8%	2%	4%	2%
Fixed income securities	<u>129,758</u>	<u>100%</u>	<u>88%</u>	<u>10%</u>	<u>2%</u>

Given the asset allocation strategy, the main element of risk in the portfolio is interest rate volatility. This risk is managed through the use of short duration benchmarks. The actual durations for the fixed income portfolios were:

	31 December 2009 Years	31 December 2008 Years
Sterling	0.71	1.01

Euro	0.83	1.30
US dollar	0.89	1.02

Reinsurance assets

The Group has a policy of buying reinsurance from entities with a rating of A- or above. Where we deviate from that position additional security is normally provided in the form of a letter of credit. The credit taken for reinsurance recoveries on notified outstanding and IBNR claims represents 27.4 per cent. of the gross insurance liabilities (2008: 25.4 per cent.). The Group has no material exposure to bad debt.

Exposure to reinsurance credit risk may increase over time because the Group's evolving catastrophe profile may require a greater level of reinsurance buying than has historically been the case. The management of this risk, through the selection of high quality security and control over the reinsurance recovery process, remains a key focus for the Group and is designed to ensure that the residual risk to the balance sheet remains low.

	31 December 2009 £'000	31 December 2008 £'000
Reinsurers' share of:		
Recoveries due on paid claims	3,893	12,373
Notified outstanding claims	33,772	28,963
Incurred but not reported claims	11,983	8,204
Reinsurance unearned premium reserve	18,371	9,687
Total reinsurance asset	<u>68,019</u>	<u>59,227</u>

The composition of the security supporting reinsurance recoveries on paid and notified outstanding claims is analysed below:

	31 December 2009 %	31 December 2008 %
Reinsurers rated by S&P:		
AA	20	40
A	72	54
BBB	5	1
BB and lower	3	5
	<u>100</u>	<u>100</u>

Capital management

The capital required to support the Group's underwriting for the 2010 underwriting year is 52.3 per cent. of syndicate capacity of £300m (2009: 47.8 per cent. on £250m).

The following table sets out the composition of the assets supporting the current capital requirement.

Year of account	2010 £'000	2009 £'000
Capital requirement:	156,900	119,600
Satisfied by:		
Investments	110,603	76,312
Letter of credit ("LOC")	31,056	35,000
Solvency credits	17,014	8,935

Total FAL provided

158,673

120,247

The Group's capital requirement has increased in line with the planned growth in the business to be underwritten and the levels of reinsurance protection purchased. The increase has been funded by the placing and open offer which was finalised in the first quarter of 2009. In addition the Group has renegotiated a new LOC facility, which provides up to \$82m for the 2009, 2010 and 2011 underwriting years. As at 31 December 2009, \$50m of this facility has been utilised, leaving an additional \$32m available for further development of the business.

Forward-looking information

The forward-looking statements within this business, operational and financial review have been made by the directors in good faith, based on the information available to them at the time of their approval of this review.

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2009

	Notes	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Insurance premium revenue	4	221,504	153,740
Reinsurance premiums	4	(44,874)	(32,941)
Net insurance premium revenue		176,630	120,799
Financial income	5	5,648	7,790
Other operating income	6	297	284
Net income		182,575	128,873
Claims incurred	7	(110,146)	(89,632)
Reinsurers' share of claims incurred	7	26,957	19,991
Net claims incurred		(83,189)	(69,641)
Expenses incurred in insurance activities	8	(59,095)	(42,491)
Foreign exchange (losses) / gains	9	(6,641)	18,715
Other operating expenses	10	(11,956)	(10,648)
Total operating expenses		(160,881)	(104,065)
Operating profit		21,694	24,808
Finance charges	12	(1,594)	(1,715)
Profit before tax		20,100	23,093
Comprises:			
Underlying profit ¹		30,484	13,616
Notional adjustment for foreign exchange movements on non-monetary items	9	(10,384)	9,477
Income tax expense	13	(2,677)	(3,592)
Profit for the year		17,423	19,501
Earnings per share (pence)			
Basic	14	36.8	55.4
Diluted	14	35.6	53.8

All of the operations relate to continuing activities during the current and previous year.

¹ Underlying profit comprises profit before tax with non-monetary items translated at closing foreign exchange rates (see explanation in note 3 to the financial statements).

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2009

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Profit for the year	17,423	19,501
Other comprehensive income	-	-
Total comprehensive income recognised	17,423	19,501

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2009

	Notes	As at 31 December 2009 £'000	As at 31 December 2008 £'000
Assets			
Intangible assets	16	15,509	15,509
Property, plant and equipment	17	3,075	1,868
Reinsurance assets			
- Reinsurers' share of outstanding claims	26	45,755	37,167
- Reinsurers' share of unearned premium	26	18,371	9,687
Deferred acquisition costs	19	29,544	24,423
Trade and other receivables	20	88,219	83,982
Current income tax assets		4,514	326
Prepayments and accrued income		4,366	3,204
Investments at fair value	21	192,365	129,758
Cash and cash equivalents	22	98,254	105,070
Total assets		499,972	410,994
Equity			
Share capital	23	10,464	7,152
Contributed surplus	23	77,295	42,349
Other reserves	24	3,357	2,348
Retained earnings		60,975	49,880
Total equity		152,091	101,729
Liabilities			
Financial liabilities – subordinated debt	25	18,136	20,256
Insurance liabilities			
- Outstanding claims	26	166,737	146,299
- Unearned premium	26	112,817	92,325
Deferred income tax liabilities	27	9,960	8,471
Trade and other payables	28	40,231	41,914
Total liabilities		347,881	309,265
Total equity and liabilities		499,972	410,994
Net assets per share (£)	29	£2.96	£2.90
Net tangible assets per share (£)	29	£2.66	£2.45

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2009

	Note	Common Shares £'000	Share Premium £'000	Contributed Surplus £'000	Other Reserves £'000	Retained Earnings £'000	Total £'000
Balance at 1 January 2009		7,152	-	42,349	2,348	49,880	101,729
Total comprehensive income for the year							
Profit recognised		-	-	-	-	17,423	17,423
Transactions with owners, recorded directly in equity							
Proceeds of shares issued in relation to share options exercised	23	21	-	178	-	-	199
Placing and open offer	23	3,291	-	34,768	-	-	38,059
Share-based payments	24	-	-	-	1,587	-	1,587
Employee Benefit Trust holding	24	-	-	-	(578)	-	(578)
Dividends	15	-	-	-	-	(6,328)	(6,328)
Balance at 31 December 2009		10,464	-	77,295	3,357	60,975	152,091

For the year ended 31 December 2008

	Note	Common Shares £'000	Share Premium £'000	Contributed Surplus £'000	Other Reserves £'000	Retained Earnings £'000	Total £'000
Balance at 1 January 2008		7,142	42,258	-	1,504	34,304	85,208
Total comprehensive income for the year							
Profit recognised		-	-	-	-	19,501	19,501
Transactions with owners, recorded directly in equity							
Proceeds of shares issued in relation to share options exercised	23	10	91	-	-	-	101
Share-based payments	24	-	-	-	992	-	992
Employee Benefit Trust holding	24	-	-	-	(148)	-	(148)
Transfer on reverse acquisition	23	-	(42,349)	42,349	-	-	-
Dividends	15	-	-	-	-	(3,925)	(3,925)
Balance at 31 December 2008		7,152	-	42,349	2,348	49,880	101,729

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2009

	Year ended 31 December 2009	Year ended 31 December 2008
	£'000	£'000
Profit before tax	20,100	23,093
Depreciation of property, plant and equipment	809	455
Interest and equity dividend income	(6,072)	(8,885)
Net unrealised losses / (gains) on investments	1,412	(2,288)
Foreign exchange losses / (gains)	6,641	(23,625)
Share-based payments	1,587	992
Finance charges	1,594	1,715
Change in underwriting balances	15,486	36,704
(Increase) / decrease in investments	(71,299)	4,564
(Increase) in debtors and prepayments	(2,018)	(2,852)
(Decrease) / increase in creditors and accruals	(6,203)	12,955
Interest received	6,072	8,827
Equity dividend received	-	58
Income tax paid	(4,965)	(2,680)
Net cash generated from operating activities	(36,856)	49,033
Cash flows from investing activities		
Purchase of property, plant and equipment	(2,078)	(674)
Cash used in investing activities	(2,078)	(674)
Cash flows from financing activities		
Dividends paid	(6,328)	(3,925)
Cash received from issue of shares	38,259	101
(Purchase) of own shares	(578)	(148)
Finance charges	(1,594)	(1,715)
Net cash from financing activities	29,759	(5,687)
Net (decrease) / increase in cash and cash equivalents	(9,175)	42,672
Cash and cash equivalents at beginning of year	105,070	63,919
Effect of exchange rate fluctuations on cash and cash equivalents	2,359	(1,521)
Cash and cash equivalents at end of year	98,254	105,070

Change in underwriting balances shows the movement in the underwriting debtors and creditors in the relevant period.

Notes to the consolidated financial statements

1 Summary of significant accounting policies

Hardy Underwriting Bermuda Limited is a company domiciled in Bermuda. The financial statements of the Company for the twelve month period ended 31 December 2009 relate to the Company and its subsidiaries (together referred to as the “Group”). The financial information has been prepared in accordance with Bermudian law.

The financial information set out in this statement is extracted from the Group’s consolidated financial statements for the year ended 31 December 2009. All amounts relate to continuing operations. The auditors have reported on the 2009 financial statements which include comparative amounts for 2008. Their report was unqualified. The extracts from the consolidated financial statements were approved for issue by the board on 3 March 2010.

The principal accounting policies applied in the presentation of these financial statements are set out below. These accounting policies have been consistently applied to all the years presented, unless otherwise stated.

The financial statements are presented in pounds sterling, rounded to the nearest thousand, unless otherwise stated.

a. Basis of preparation

Statement of compliance

The group consolidated financial statements are prepared in accordance with all of the International Financial Reporting Standards (“IFRS”), as adopted by the European Union (“EU”), which are effective at 31 December 2009.

Hardy Underwriting Bermuda Limited was incorporated under the laws of Bermuda on 17 October 2007. With effect from 6 February 2008, under a scheme of arrangement involving a share exchange with the members of Hardy Underwriting Group plc, the company became the new holding company of the Hardy group.

Throughout the period from incorporation to 6 February 2008, Hardy Underwriting Bermuda Limited was a shell company with no material revenues or assets and did not constitute a “business” as defined by IFRS 3 Business Combinations. In effect, the shareholders of Hardy Underwriting Group plc immediately before the share exchange, acquired 100 per cent of the share capital of Hardy Underwriting Bermuda Limited 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 Hardy Underwriting Group plc was deemed to be the acquirer for accounting purposes and the legal parent company, Hardy Underwriting Bermuda Limited was treated as a subsidiary whose identifiable assets and liabilities are incorporated into the Group at fair value.

The Group has implemented the amendments to IFRS 7 Improving Disclosures about Financial Instruments, which requires additional disclosures about fair value measurement and liquidity risk. Consequently, fair value measurements are disclosed by source of inputs using a three level fair value hierarchy, by class of asset, for all financial instruments recognised at fair value. More information can be found in note 21 of this report and accounts. The Group has also adopted IAS 1 (revised) Presentation of Financial Statements which requires the Group to present in the consolidated statement of changes in equity all owner changes in equity. The comparative figures for the prior period have been re-presented. As this only has an impact on presentation there is no effect on earnings per share.

The International Accounting Standards Board (IASB) has released amendments to the following standards. All of the standards shown below have not been early adopted but are expected to be of relevance in future accounting periods. They are not anticipated to have any significant impact on the future consolidated statements of the Group:

IFRS 3 (revised) “Business combinations”

IFRS 5 (amendment) “Non current assets held for sale on discontinued operations”

IFRS 9 (not yet endorsed) “Financial instruments”

IAS 24 (revised) “Related party disclosures”

IAS 27 (amendment) “Consolidated and separate financial statements”

IAS 39 (amendment) “Financial Instruments: Recognition and Measurement – eligible hedged items”

IFRIC 16 “Hedging of a net investment in a foreign operation”

Improvements to IFRS’s (2009)

Measurement convention

The consolidated financial statements are prepared on the historical cost basis, as modified by the revaluation of financial instruments at fair value through the income statement.

Estimates

The preparation of financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. The areas involving a high degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in note 2.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the year in which the estimate is revised if the revision affects only that year, or in the year of the revision and future years, if the revision affects both current and future years.

b. Basis of consolidation

Hardy’s subsidiaries are all entities over which the Group has the power, directly or indirectly, to govern their financial and operating policies so as to obtain benefits from their activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Intra-group transactions, balances and unrealised gains arising from intra-group transactions are eliminated in preparing the consolidated financial statements.

c. Foreign currency translation

The functional currency used in the financial statements is sterling, being the currency of the primary economic environment of the Group. The consolidated financial statements are presented in pounds sterling, being the presentational currency for the Group.

Transactions in US dollars, Canadian dollars and Euros are translated into sterling at the average rates ruling during the reporting period. Underwriting transactions denominated in other foreign currencies are translated into sterling using the exchange rates prevailing at the date of the transaction.

Monetary items are translated at rates of exchange ruling at the balance sheet date. This creates a foreign exchange gain or loss between the net assets translated at closing rates and the profit for the period which is derived by reference to average rates. The foreign exchange gain or loss is credited or charged to the income statement.

Non-monetary assets and liabilities denominated in foreign currencies, including unearned premiums and deferred acquisition costs, are recorded in sterling at the rate prevailing at the time of initial recognition and are not subsequently restated.

The rates of exchange used in these financial statements are as follows:

Average exchange rates	2009	2008
US dollar	1.57	1.85
Canadian dollar	1.78	1.96
Euro	1.12	1.26
Closing exchange rates	2009	2008
US dollar	1.61	1.44
Canadian dollar	1.69	1.77
Euro	1.13	1.03

d. Insurance contracts

Insurance contracts are those contracts that transfer significant insurance risk at the inception of the contract. Insurance risk is transferred when an insurer agrees to compensate a policyholder if a specified uncertain future event adversely affects the policyholder.

Insurance premium revenues

Insurance premium revenues comprise the proportion of premiums written that are earned in the period.

Gross premiums written represent premiums due up to the balance sheet date in respect of contracts incepting in the financial year, and include estimates for pipeline premiums, together with adjustments to premiums written in prior accounting periods. Such premiums written are stated before the deduction of commissions but are exclusive of taxes, duties levied on premiums and other deductions.

Premiums are earned over the period of risk under the policy. The provision for unearned premiums represents the proportion of gross premium written which is estimated to relate to exposures in subsequent financial periods. Where the incidence of risk varies during the term of the contract and where this would have a material effect on earnings, the provision is based upon the estimated risk profile of the business written.

Premiums ceded to reinsurers are accounted for in the same accounting period as the related direct insurance or inwards reinsurance business except in relation to excess of loss contracts, where the

premium is charged over the period of cover. The provision for reinsurers' share of unearned premiums represents that part of reinsurance premiums ceded which is estimated to be earned in subsequent accounting periods.

Claims and reinsurers' share of claims

Claims incurred represent the cost of claims and claims handling expenses paid during the financial year, together with the movement in provisions for outstanding claims and future claims handling provisions. Reinsurance recoveries are accounted for in the same period as the incurred claims for the related business.

The provision for claims outstanding comprises amounts set aside for notified claims and claims incurred but not reported ("IBNR"). The IBNR amount is based on estimates calculated using statistical techniques which are reviewed by external consulting actuaries. The techniques generally use projections, based on past experience of the development of claims over time, to form a view of the likely ultimate claims to be experienced. In addition factors such as knowledge of specific events and terms and conditions of policies are taken into account. For more recent underwriting, consideration is given to the variations in the business portfolio accepted and the underlying terms and conditions. Where a high degree of volatility arises from projections, estimates may be based on rating, on other models of the business accepted and also on assessments of underwriting conditions. The critical assumption used when estimating claims provisions is that past experience is a reasonable predictor of likely future claims development and that the rating and other models used to analyse current business are a fair reflection of the likely level of ultimate claims to be incurred.

The reinsurers' share of provisions for claims is based on calculated amounts for outstanding claims and projections for IBNR, net of estimated irrecoverable amounts, having regard to the reinsurance programme in place for the class of business, the claims experience for the year and also the current security rating of the reinsurance companies involved. Statistical techniques are used to assist in making these estimates.

We seek to ensure that all claims incurred are adequately provided for but adjustments may be necessary in later periods as a result of subsequent information and events. Any adjustments to original provisions are made in the financial period in which the need for a change in provision becomes apparent.

Liability adequacy test

At each reporting date an assessment is made to determine whether recognised insurance liabilities are adequate. If that assessment shows that the carrying amount of insurance liabilities (less related acquisition costs) is inadequate in the light of estimated future cash flows, the entire deficiency is recognised in the income statement as an impairment of any associated deferred acquisition costs and, where these are fully depleted, via the provision for unexpired risks. The provision for unexpired risks is calculated separately by reference to classes of business which are managed together, after taking into account relevant investment return.

e. Financial income

Financial income comprises interest income, dividend income and fair value gains and losses on financial instruments at fair value through profit or loss. Fair value gains and losses include both those realised on disposal of financial instruments and those unrealised, representing the movement in the fair value of financial instruments at fair value through the profit or loss held at the reporting date. Dividend income is recognised when the

shareholder's right to receive the payment is established. Interest income on financial assets that are not classified at fair value through the profit or loss are recognised using the effective interest method.

f. Other operating income

Other operating income includes the fees and profit commission charged by the Group to third party members of syndicate 382. All such income is accounted for in the accounting period in which the service is rendered by reference to the stage of completion of the specific transaction, assessed on the basis of the actual services provided as a proportion of the total services to be provided.

g. Expenses incurred in insurance activities

Expenses incurred in insurance activities are recognised on an accruals basis. These comprise the Group's share of syndicate operating expenses, acquisition costs and the direct costs of membership of Lloyd's and other expenses attributable to the Group's underwriting activities.

Acquisition costs include brokerage and expenses incurred in respect of insurance contracts written and incepting during the financial period. They are allocated in accordance with the earnings pattern of the premiums on the underlying business. Deferred acquisition costs represent the proportion of acquisition costs incurred in respect of unearned premiums at the balance sheet date. Deferred acquisition costs are only deferred to the extent that they are considered recoverable out of future revenues.

h. Other operating expenses

Other operating expenses are recognised on an accruals basis. They comprise operating expenses such as remuneration, office and administrative costs.

i. Leases

Costs in respect of operating leases are charged to the income statement on a straight line basis over the lease term.

j. Finance charges

Finance charges comprise interest payable on loans together with fees and commissions charged for the utilisation of letters of credit. Interest payable on loans is charged to the income statement using the effective interest method. Fees paid for the arrangement of debt and letter of credit facilities are charged to the income statement over the life of the facility.

k. Taxation

The income tax expense comprises both current and deferred tax.

The tax currently payable is based on taxable income for the year. Taxable income differs from profits accounted for in the income statement because it excludes items of income and expenditure that are taxable or deductible in other periods or are not subject to, or allowable for, taxation. The Group's liability for current tax is calculated using tax rates applicable at the balance sheet date.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the tax bases of dealing with assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred tax is not recognised for temporary differences arising on the initial recognition of an asset or a liability in a transaction, other than a business combination, that at the time of the transaction affects neither accounting nor

taxable profit or loss. Deferred income 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 income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

l. Dividend distribution

Dividends payable to the Group's shareholders are recognised as a liability in the period in which the dividend is declared and appropriately approved. Dividends are recognised in the statement of changes in equity. Dividends declared after the balance sheet date, but before the financial statements are authorised, are not recognised but are disclosed in the notes to the financial statements.

m. Employee benefits

(i) Pensions

Contributions to the Group's defined contribution pension scheme are charged to the income statement when payable.

(ii) Share based payments

The Group operates a number of employee and executive share schemes. The details of these schemes can be found in the Directors Remuneration Report. Share options and share awards granted are measured at fair value on the date of grant and are expensed on a straight-line basis over the vesting period, with a corresponding increase in equity. The amount recognised as an expense is based on the Group's estimate of the number of shares that will eventually vest.

The Group uses option pricing models to assess the fair value of options granted to employees for all options issued after 7 November 2002. At each balance sheet date the Group re-assesses the number of share options that are expected to vest. Any adjustments are recognised through the income statement with a corresponding adjustment to equity over the remaining vesting period.

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

n. Intangible assets

Intangible assets comprise the costs of purchased syndicate capacity. This capacity is considered to have an indefinite useful life represented by participation rights to membership of syndicate 382, since it is deemed that the benefits from that capacity have no foreseeable time limit. Purchased syndicate capacity is capitalised at cost and is subsequently measured at cost less any impairment. The Board has considered the future prospects of the London insurance market and consequently believes that the ownership of the capacity by the group will provide economic benefit over an indefinite number of future periods.

Purchased syndicate capacity is subject to an annual impairment test. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount.

o. Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and any impairment. Depreciation has been provided on a straight-line basis to write off the cost of fixed assets, less their residual values, over their estimated useful economic lives. The rates used are as follows:

Office equipment	25%
Computer equipment	33%
Underwriting system	20%

p. Financial assets

Purchases and sales of financial assets are recognised on the trade date, which is when the Group commits to purchase or sell the asset. Financial assets are recognised initially at fair value and, for instruments not at fair value through the income statement, include any directly attributable transaction costs. Subsequent to initial recognition financial assets are measured as described below.

Financial assets are de-recognised when contractual rights to receive cash flows from the investment expire, or where the investments, together with substantially all the risks and rewards of ownership, have been transferred.

Investments

The Group designates its investments as fair value through the income statement. Management determines the designation of investments on initial recognition. Investments are designated at fair value through the income statement because the Group manages its investments on a fair value basis in accordance with its documented risk management and investment strategies.

Financial assets at fair value through the income statement are measured at fair value, with fair value changes being recognised in the income statement. The fair values of listed investments are based on quoted bid prices at the close of business on the balance sheet date.

Trade and other receivables

Trade and other receivables are stated at amortised cost less impairment losses.

Cash and cash equivalents

Cash and cash equivalents represent cash balances, money market deposits lodged with banks and other short-term highly liquid investments purchased within 3 months of maturity.

q. Derivative financial instruments

The Group's only derivatives are forward exchange contracts, which are used to manage exposure to foreign exchange risk arising from insurance operations. Derivatives are recognised initially at fair value and attributable transaction costs are expensed as incurred. Subsequent to initial recognition, derivatives are measured at fair value with fair value changes being recognised in the income statement. Fair value is the rate at which a forward exchange contract with equivalent terms could be entered into at the reporting date. The Group does not use any derivative financial instruments for speculative purposes.

Derivative financial assets and liabilities are included within investments (note 21) and trade and other payables (note 28) respectively.

r. Impairment (non-financial assets)

The carrying amount of the Group's assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the carrying value is reduced to the estimated recoverable amount by means of a charge to the consolidated income statement.

An impairment loss is reversed if there is new information which results in a change in the estimates used to determine the recoverable amount, being the higher of fair value less selling costs and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate which reflects current market assessments of the time value of money and the risks specific to the asset for which the estimate of future cash flows have not been adjusted.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognised.

s. Subordinated debt

The long term loan is recognised initially at fair value, net of transaction costs incurred. The loan is subsequently stated at amortised cost. Any difference between the initial carrying amount and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

t. Provisions

A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation.

u. Own shares

Investments in own shares are valued at their acquisition cost and are deducted from shareholders' equity in the balance sheet.

2 Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities during the financial year. Estimates are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Estimates and judgements in applying accounting policies are continually evaluated for appropriateness.

Certain critical accounting estimates and judgements in applying the Group' accounting policies are described below.

The Group's estimates for reported and unreported losses and the resulting provisions and related reinsurance recoverables are continually monitored and formally reviewed quarterly and updated based on the latest available information. Adjustments resulting from this review are reflected in income. The process relies upon the basic assumption that past experience, adjusted for the effect of current developments and likely trends, is an appropriate basis for predicting future events. Estimation of claims provisions is a complex process, however, and significant uncertainty exists as to the ultimate settlement of these liabilities. Further details of the claims provision estimation process are set out in note 3.

Purchased syndicate capacity is considered to have an indefinite useful economic life as it entitles the Group to participate on the underwriting activities of syndicate 382 and the benefit from such participation has no foreseeable time limit. The carrying value of the intangible asset is reviewed annually for impairment, by assessing the discounted cash flows arising from the asset.

Financial investments held by the group at the reporting date are shown at fair value and the methods and assumptions used by the group to arrive at these values are described in note 21.

3 Segment information

The Group has adopted IFRS 8: Operating Segments in the current period. IFRS 8 requires that reportable segments represent the level at which financial information is reported to the Group Board, being the chief operating decision maker as defined in IFRS 8.

In addition, on the adoption of IFRS 8, foreign exchange gains and losses are no longer reported within the results of each reportable segment, but are instead disclosed separately. This provides a fairer presentation of the performance of each segment, which otherwise would be distorted by the movements in foreign exchange rates. Furthermore the notional foreign exchange differences on non-monetary items are also separately disclosed to highlight the additional volatility which the accounting mismatch arising from IFRS whereby unearned premium and deferred acquisition costs are treated as non-monetary items and claims reserves are treated as monetary items. Non-monetary items are carried at historic rates, while monetary items are translated at closing rates.

The reportable business segments are based upon the different types of insurance risks underwritten and have been identified as follows:

- marine and aviation, which underwrites a broad spectrum of aviation and marine classes including general aviation, airlines, space, cargo, jewellers block, other specie and marine hulls.
- speciality lines, which includes a diverse range of accounts including financial institutions, terrorism, political risks and accident and health insurance.
- non-marine property, which underwrites property risks on both a direct insurance and facultative reinsurance basis.
- property treaty, which underwrites the reinsurance of property risks on both a non-proportional and proportional basis.

Segmental results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. The reporting segments do not cross-sell business between each other and there is no individual policy holder that comprise greater than ten per cent. of the group's total gross premium written.

Financial income, other operating income, other operating expenses, finance costs and taxation are not allocated to business segments as these items are determined by entity level factors and do not relate directly to the performance of each operating segment.

Information regarding the Group's reportable segments is presented below. Comparative information has been restated to reflect the adoption of IFRS 8.

Year ended 31 December 2009

	Marine and aviation	Speciality lines	Non-marine property	Property treaty	Total reportable segments	Effects of foreign exchange on non-monetary items	Other foreign exchange	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Gross premium written	63,858	40,737	52,970	84,431	241,996	-	-	241,996
Net insurance premium revenue	61,820	33,968	37,468	51,050	184,306	(7,676)	-	176,630
Net claims incurred	(38,795)	(16,541)	(9,926)	(17,927)	(83,189)	-	-	(83,189)
Expenses incurred in insurance activities	(20,776)	(10,449)	(13,065)	(16,462)	(60,752)	1,657	-	(59,095)
Total operating expenses	(59,571)	(26,990)	(22,991)	(34,389)	(143,941)	1,657	-	(142,284)
Underwriting return before foreign exchange	2,249	6,978	14,477	16,661	40,365	(6,019)	-	34,346
Foreign exchange losses					-	(4,365)	(2,276)	(6,641)
Underwriting return after foreign exchange					40,365	(10,384)	(2,276)	27,705
Financial income								5,648
Other operating income								297
Other operating expenses								(11,956)
Operating profit								21,694
Finance charges								(1,594)
Profit before tax								20,100
Taxation charge								(2,677)
Profit after tax								17,423
Claims ratio (%)	62.8%	48.7%	26.5%	35.1%	45.1%			
Expense ratio (%)	33.6%	30.8%	34.9%	32.2%	33.0%			
Combined ratio (%)	96.4%	79.5%	61.4%	67.3%	78.1%			

The claims ratio is net claims incurred as a percentage of net insurance premium revenue.

The expense ratio is expenses incurred in insurance activities (excluding other operating expenses) as a percentage of net insurance premium revenue.

The combined ratio which is the sum of the claims ratio and expense ratio.

The segment results for the year ended 31 December 2008 are as follows:

	Marine and aviation	Speciality lines	Non-marine property	Property treaty	Total reportable segments	Effects of foreign exchange on non-monetary items	Other foreign exchange	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Gross premium written	47,866	48,140	26,165	50,599	172,770	-	-	172,770
Net insurance premium revenue	43,862	29,493	16,777	33,469	123,601	(2,802)	-	120,799
Net claims incurred	(24,466)	(17,674)	(13,033)	(14,468)	(69,641)	-	-	(69,641)

Expenses incurred in insurance activities	(14,706)	(13,145)	(6,217)	(9,059)	(43,127)	636	-	(42,491)
Total operating expenses	(39,172)	(30,819)	(19,250)	(23,527)	(112,768)	636	-	(112,132)
Underwriting return before foreign exchange	4,690	(1,326)	(2,473)	9,942	10,833	(2,166)	-	8,667
Foreign exchange gains					-	11,643	7,072	18,715
Underwriting return after foreign exchange					10,833	9,477	7,072	27,382
Financial income								7,790
Other operating income								284
Other operating expenses								(10,648)
Operating profit								24,808
Finance charges								(1,715)
Profit before tax								23,093
Taxation charge								(3,592)
Profit after tax								19,501
Claims ratio (%)	55.8%	59.9%	77.7%	43.2%	56.3%			
Expense ratio (%)	33.5%	44.6%	37.1%	27.1%	34.9%			
Combined ratio (%)	89.3%	104.5%	114.8%	70.3%	91.2%			

The segment assets and liabilities as at 31 December 2009 are as follows:

	Marine and aviation	Speciality lines	Non-marine property	Property treaty	Total
	£'000	£'000	£'000	£'000	£'000
Assets attributable to business segments	102,620	96,054	69,327	101,800	369,801
Other group assets					130,171
Total assets					499,972
Liabilities attributable to business segments	98,969	88,652	62,922	64,265	314,808
Other group liabilities					33,073
Total liabilities					347,881

The segment assets and liabilities as at 31 December 2008 are as follows:

	Marine and aviation	Speciality lines	Non- marine property	Property treaty	Total
	£'000	£'000	£'000	£'000	£'000
Assets attributable to business segments	103,290	102,871	39,050	73,109	318,320
Other group assets					92,674
Total assets					<u>410,994</u>
Liabilities attributable to business segments	83,572	98,010	46,380	39,729	267,691
Other group liabilities					41,574
Total liabilities					<u>309,265</u>

Geographical segments

All business is underwritten in the UK, although the situs of the risk is analysed as follows:

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
UK	35,887	24,543
Other EC member states	9,229	29,618
United States of America	30,957	34,621
Worldwide	165,923	83,988
Gross premiums written	<u>241,996</u>	<u>172,770</u>

The "Worldwide" category does not have any significant concentration in any geographic region.

4 Net insurance premium revenue

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Gross premiums written	241,996	172,770
Change in gross unearned premiums provision (note 26)	(20,492)	(19,030)
Gross earned premiums	<u>221,504</u>	<u>153,740</u>
Premiums ceded to reinsurers	(53,558)	(34,630)
Change in ceded unearned premiums provision (note 26)	8,684	1,689
Ceded earned premiums	<u>(44,874)</u>	<u>(32,941)</u>
Net insurance premium revenue	<u>176,630</u>	<u>120,799</u>

5 Financial income

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Interest income cash and cash equivalents	635	736
Investment income on financial assets designated at fair value through the income statement on initial recognition		
Interest income from fixed income securities	5,437	8,091
Dividend income	-	58
Fair value gains/(losses) on financial assets at fair value through the income statement		
Held for trading (foreign exchange contracts)	1,044	(2,459)

Designated upon initial recognition (realised)	(194)	337
Designated upon initial recognition (unrealised)	(1,274)	1,027
	<u>5,648</u>	<u>7,790</u>

6 Other operating income

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Managing agent fees from third party Names	-	4
Managing agent profit commission	-	230
Other income	297	50
	<u>297</u>	<u>284</u>

7 Net claims incurred

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Claims paid	78,873	71,056
Movement in insurance liabilities (note 26)	31,273	18,576
Gross claims incurred	<u>110,146</u>	<u>89,632</u>
Reinsurers' share of claims paid	(15,776)	(20,020)
Reinsurers' share of movement in insurance liabilities (note 26)	(11,181)	29
Reinsurers' share of claims incurred	<u>(26,957)</u>	<u>(19,991)</u>
Net claims paid	63,097	51,036
Net movement in insurance liabilities	20,092	18,605
Net claims incurred	<u>83,189</u>	<u>69,641</u>

The current period has benefited from a release of claims reserves established in previous reporting periods. This reassessment of claims reserves has contributed £9.7m (2008: £6.4 m) to the profit recognised in the period due to the development of claims being more favourable than previously estimated. The release is analysed by business segments, as follows:

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Marine and aviation	567	3,378
Specialty lines	2,311	1,970
Non-marine property	5,056	(1,016)
Property treaty	1,816	2,055
Total	<u>9,750</u>	<u>6,387</u>

8 Expenses incurred in insurance activities

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Commission expenses payable	48,090	32,908
Other acquisition costs (note 10)	6,160	5,440
Change in deferred acquisition costs	(4,980)	(4,355)
Total acquisition costs	<u>49,270</u>	<u>33,993</u>

Administrative expenses (note 10)	9,825	8,498
Expenses incurred in insurance activities	<u>59,095</u>	<u>42,491</u>

9 Foreign exchange losses

Foreign exchange gains and losses result from the translation of the balance sheet to closing rates and the income statement to average exchange rates. International Accounting Standard 21: The Effects of Changes in Foreign Exchange Rates, however, requires that non-monetary items remain at historic rates. The Group's only non-monetary assets and liabilities denominated in foreign currencies are unearned premiums and deferred acquisition costs ("UEP" and "DAC").

This IFRS accounting treatment creates a mismatch in foreign exchange rates used, the financial effects of which are shown in the table below.

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Foreign exchange (losses) / gains arising from:		
Translation of balance sheet and income statement	(2,276)	7,072
Maintaining UEP and DAC items in the balance sheet at historic rates	(10,384)	9,477
Maintaining UEP and DAC items in the income statement at historic rates	6,019	2,166
	<u>(6,641)</u>	<u>18,715</u>
	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Effects of foreign exchange on non-monetary items:		
UEP and DAC items at historic rates	64,902	58,215
UEP and DAC items at closing rates	64,367	68,064
Valuation difference in closing balance sheet	<u>(535)</u>	<u>9,849</u>
Valuation difference in opening balance sheet	(9,849)	(372)
	<u>(10,384)</u>	<u>9,477</u>

10 Operating expenses

	Acquisition costs (note 8) £'000	2009 Administrative costs (note 8) £'000	Other operating expenses £'000	Total £'000
Other acquisition costs	6,160	-	-	6,160
Administrative expenses	-	9,825	-	9,825
Other operating expenses	-	-	11,956	11,956
	<u>6,160</u>	<u>9,825</u>	<u>11,956</u>	<u>27,941</u>
Employee expense	4,110	3,362	8,943	16,415
External professional consultancy	298	244	723	1,265
Lloyd's' membership costs	-	1,790	-	1,790
IT related expenditure	563	460	322	1,345
Accommodation costs	244	200	480	924
Depreciation	65	53	691	809
Investment management fees	36	30	114	180
Corporate travel and entertaining	149	122	310	581
Auditors remuneration	9	8	373	390
Other administration costs	686	3,556	-	4,242

6,160	9,825	11,956	27,941
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Included in employee expenses within other operating expenses is £2,615,077 which relates to profit related remuneration of staff and directors employed in the underwriting function.

	Acquisition costs (note 8)	2008 Administrative costs (note 8)	Other operating expenses	Total
	£'000	£'000	£'000	£'000
Other acquisition costs	5,440	-	-	5,440
Administrative expenses	-	8,498	-	8,498
Other operating expenses	-	-	10,648	10,648
	<u>5,440</u>	<u>8,498</u>	<u>10,648</u>	<u>24,586</u>
Employee expense	3,457	2,828	9,050	15,336
External professional consultancy	365	299	556	1,220
Lloyd's' membership costs	-	1,670	-	1,670
IT related expenditure	558	457	175	1,190
Accommodation costs	226	185	178	589
Depreciation	62	51	340	453
Investment management fees	44	36	55	134
Corporate travel and entertaining	169	138	211	518
Auditors remuneration	111	91	83	284
Other administration costs	448	2,743	-	3,191
	<u>5,440</u>	<u>8,498</u>	<u>10,648</u>	<u>24,586</u>

Acquisition and administrative expenses are included in the calculation of the Group's combined ratio. Other operating expenses are not included in the combined ratio as these are determined by entity level factors and not allocated to business segments.

	Year ended 31 December 2009	Year ended 31 December 2008
	£'000	£'000
Audit of these financial statements	54	50
Audit of financial statements of subsidiaries pursuant to legislation	181	144
Other services pursuant to such legislation	70	46
Other services relating to tax	44	48
All other services	115	9
	<u>464</u>	<u>297</u>

All the amounts shown above were paid to KPMG with the exception of £13,500 (2008: £12,750) which was paid to Mazars LLP. In 2009 KPMG assisted with the open and placing offer. These fees formed part of a larger legal cost offset against contributed surplus and were not charged against the profit of the current period. The amount of £115,256 is reflected above in the current period.

11 Employee benefit expense

	Year ended 31 December 2009	Year ended 31 December 2008
	£'000	£'000
The aggregate director and staff expense for the group was:		
Wages and salaries	11,402	11,283
Social security costs	1,620	1,543
Share-based payments	1,587	992
Pension costs	1,806	1,518
	<u>16,415</u>	<u>15,336</u>

	<u>16,415</u>	<u>15,336</u>
Average number of employees employed by the Group during the year	84	66

12 Finance charges

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Letter of credit charges	731	579
Subordinated debt interest	863	1,136
	<u>1,594</u>	<u>1,715</u>

13 Income tax expense

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Current tax expense		
Current year	1,643	4,182
Adjustments for prior years	(455)	772
	<u>1,188</u>	<u>4,954</u>
Deferred tax		
Origination and reversal of temporary differences (note 27)	1,489	(1,362)
	<u>2,677</u>	<u>3,592</u>

The tax charge for the year differs from the theoretical amount that would arise using the average UK corporate tax rate of 28%. The difference is explained below.

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Profit before tax	20,100	23,093
Income tax using the average UK corporation tax rate of 28.0% (2008:28.5%*)	5,628	6,582
Non-deductible expenses	327	103
Group entities subject to overseas tax at a lower rate	(2,833)	(5,080)
Temporary timing difference	-	1,215
(Over) / under provision in prior years	(445)	772
Tax charge for the year	<u>2,677</u>	<u>3,592</u>

* The UK corporation tax rate changed from 30% to 28% with effect from April 2008.

14 Earnings per share

Basic

Basic earnings per share is calculated by dividing the profit after tax by the weighted average number of ordinary shares in issue during the year, excluding ordinary shares purchased by the Group and held as treasury shares.

	Year ended 31 December 2009	Year ended 31 December 2008
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Profit for the year (£'000)	17,423	19,501
	£'000	£'000
Issued shares at 1 January	35,760	35,712
Effect of own shares held	(823)	(561)
Effect of shares issued in year	12,457	46
Weighted average number of ordinary shares in issue during year	47,394	35,197
Basic earnings per share (pence per share)	36.8p	55.4p

Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Company has two categories of dilutive potential ordinary shares being share options and rewards of shares under the group share schemes. For 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 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 options. Diluted earnings per share are calculated using the same profits for the year as for basic earnings per share.

	Year ended 31 December 2009 Thousands	Year ended 31 December 2008 Thousands
Weighted average number of ordinary shares in issue during year	47,394	35,197
Adjusted for share options and share schemes	1,596	1,062
Weighted average number of ordinary shares for diluted earnings per share	48,990	36,259
Diluted earnings per share (pence per share)	35.6p	53.8p

15 Dividends per share

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Interim dividend for year ended 31 December 2009 of 4.0p per share	2,027	-
Final dividend for the year ended 31 December 2008 of 8.5p per share	4,301	-
Interim dividend for the year ended 31 December 2008 of 3.6p per share	-	1,242
Final dividend for the year ended 31 December 2007 of 7.7p per share	-	2,683
	6,328	3,925

A second interim dividend of 9.3p per share, amounting to a total dividend of £4.86 million, is to be paid on 1 April 2010. These financial statements do not reflect the accrual of this dividend payable.

16 Intangible assets

Intangible assets comprise purchased capacity on syndicate 382. This capacity is considered to have an indefinite useful economic life.

17 Property, plant and equipment

	Office equipment £'000	Computer equipment £'000	Total £'000
Cost			
As at 1 January 2008	552	2,362	2,914
Additions	54	620	674

As at 31 December 2008	606	2,982	3,588
Additions	1,367	711	2,078
Disposals	(338)	-	(338)
As at 31 December 2009	1,635	3,693	5,328
Depreciation			
As at 1 January 2008	192	1,074	1,266
Charge for the year	141	313	454
As at 31 December 2008	333	1,387	1,720
Charge for the year	274	535	809
Disposal	(276)	-	(276)
As at 31 December 2009	331	1,922	2,253
Carrying amounts			
At 31 December 2008	273	1,595	1,868
At 31 December 2009	1,304	1,771	3,075

18 Reinsurance assets

	As at 31 December 2009 £'000	As at 31 December 2008 £'000
Reinsurers' share of unearned premium	18,371	9,687
Reinsurers' share of outstanding claims	46,800	38,289
Impairment provision	(1,045)	(1,122)
Reinsurance assets (note 26)	64,126	46,854

Amounts due from reinsurers in respect of claims already paid by the Group are included in trade and other receivables.

19 Deferred acquisition costs

	2009 £'000	2008 £'000
As at 1 January	24,423	20,060
Acquisition costs deferred in the year	22,645	18,355
Amortisation charged to income	(17,524)	(13,992)
As at 31 December	29,544	24,423

20 Trade and other receivables

	As at 31 December 2009 £'000	As at 31 December 2008 £'000
Receivables arising from direct insurance operations due from agents, brokers and intermediaries	23,610	17,943
Receivables arising from reinsurance operations due from agents, brokers and intermediaries	59,777	52,651
Reinsurance recoveries due from reinsurers	3,893	12,373
Other receivables	939	1,015
	88,219	83,982

Amounts due from reinsurers are stated after a provision for impairment of receivables from reinsurers of £137,000 (2008: £254,000). All trade and other receivables are due within twelve months of the balance sheet date.

21 Investments

	As at 31 December 2009 £'000	As at 31 December 2008 £'000
Financial assets at fair value through the income statement Designated upon initial recognition	<u>192,365</u>	<u>129,758</u>
Financial assets at fair value through the income statement Debt and other fixed income securities	<u>192,365</u>	<u>129,758</u>

The Group has designated all investments at fair value through the income statement.

Hardy Re Limited (“HRe”), Hardy Underwriting Limited (“HU”) and Hardy Names Limited (“HN”) are wholly owned subsidiaries of Hardy Underwriting Bermuda Limited. They have entered into Lloyd’s Deposit Trust Deeds under the terms of which they have deposited funds (cash and investments) with Lloyd’s, as security in respect of their underwriting business at Lloyd’s. During 2007 all funds were transferred from HN to HU. At the end of April 2008 the assets were then transferred to HRe. At 31 December 2009 the total deposited under the Trust Deeds, including cash, amounted to £110,603,252 (2008: £76,312,269) and the relevant investments together with income thereon represent the maximum contingent liability under the Trust Deeds. HRe, HU and HN may, however, incur further liabilities pursuant to their underwriting activities at Lloyd’s which would need to be met from their other assets.

In addition, on behalf of HU, the Company has deposited letters of credit with Lloyd’s totalling US\$50m (2008: £35m). These letters of credit have been issued by Lloyds TSB Bank, Calyon and Barclays Bank and are secured on the assets of the Group. This facility gives the Group access to US\$82m to support underwriting on the 2009, 2010 and 2011 years of account.

Total investments for the year ended 31 December 2009 have increased by £62,607,000 (2008: £20,267,000) and a breakdown of the increase is shown below:

	2009 £'000	2008 £'000
As at 1 January	129,758	109,491
Exchange differences on monetary assets	(7,280)	22,543
Additions	174,533	281,150
Sales and redemptions	(103,234)	(285,713)
Fair value unrealised gains and losses	(1,412)	2,287
As at 31 December	<u>192,365</u>	<u>129,758</u>

Fair value measurement

The table below summarises the fair value hierarchy for the group in accordance with revised IFRS 7 – Financial Instruments : Disclosures. As this is the first time for adoption of this standard, no comparative is required.

The levels of the fair value hierarchy are defined as follows:

Level 1 – fair values measured using quoted prices in active markets for identical instruments. An active market is a market in which transactions for the instrument occur with sufficient frequency and volume on an ongoing basis such that quoted prices reflect prices at which an orderly transaction would take place between market participants at the measurement date.

Level 2 – fair values measured using directly or indirectly observable inputs or other similar valuation techniques for which all significant inputs are based on observable market data.

Level 3 – fair values measured using valuation techniques for which significant inputs are not based on market observable data.

The group measures the fair value of its financial assets based on prices provided by investment managers who obtain market data from independent pricing services. The pricing services used by the investment manager obtain actual

transaction prices for holdings that have quoted prices in active markets. For those securities which are not actively traded, the pricing services use common market valuation pricing models. Observable inputs used in common market valuation pricing models include, but are not limited to, broker quotes, credit ratings, interest rates and yield curves, prepayment speeds, default rates and other such inputs which are available from market sources.

Included within Level 1 of the hierarchy are Government bonds and Treasury bills, which are measured using quoted prices.

Level 2 of the hierarchy includes Government agencies, Supranationals and Corporate securities. The fair values of these assets are based on prices obtained from both investment managers and investment custodians as discussed above. The Group records the unadjusted price provided and validates the price through a number of methods, including a comparison of the prices provided by the investment manager with the investment custodian and the valuation used by external parties to derive fair value.

As at 31 December 2009

	Level 1 £'000	Level 2 £'000	Level 3 £'000	Total £'000
Financial assets:				
Debt and fixed income	51,727	140,638	-	192,365

22 Cash and cash equivalents

	As at 31 December 2009 £'000	As at 31 December 2008 £'000
Short-term bank deposits	93,001	82,195
Deposits with credit institutions	5,253	22,875
	<u>98,254</u>	<u>105,070</u>

Included in cash and cash equivalents held by the Group are balances totalling £82,163,917 (2008: £77,149,769) which are not available to the Group because they are held within syndicate premium trust funds.

23 Common shares, share premium and contributed surplus

	Number of shares Thousands	Common shares £'000	Share premium £'000	Contributed surplus £'000
As at 1 January 2008	35,712	7,142	42,258	-
Issues in relation to share options exercised	48	10	91	-
Transfer on reverse acquisition	-	-	(42,349)	42,349
As at 31 December 2008	<u>35,760</u>	<u>7,152</u>	<u>-</u>	<u>42,349</u>
Issues in relation to share options exercised	102	21	-	178
Issued in relation to placing and open offer	16,456	3,291	-	34,768
As at 31 December 2009	<u>52,318</u>	<u>10,464</u>	<u>-</u>	<u>77,295</u>

The total authorised number of common shares is 75 million (2008: 50 million), with a par value of 20 pence per share. All issued shares are fully paid. On 1 April 2009 the Group raised £38.1 million, net of expenses, by way of a placing and open offer of new common shares at 245 pence per share on the basis of 46 new common shares for every 100 existing common shares.

24 Other reserves

	Own Shares £'000	Merger Reserve £'000	Other Reserve £'000	Share-based Payments £'000	Total £'000
As at 1 January 2008	(1,561)	2,441	75	549	1,504
Share-based payments (note 30)	-	-	-	992	992
Employee benefit trust holding	(148)	-	-	-	(148)
As at 31 December 2008	(1,709)	2,441	75	1,541	2,348
Share-based payments (note 30)	-	-	-	1,587	1,587
Employee benefit trust holding	(578)	-	-	-	(578)
As at 31 December 2009	(2,287)	2,441	75	3,128	3,357

The merger reserve relates to the merger of HUG with HU on formation of the Group in 1996. Other reserves were created following the capitalisation of reserves in HUA during 1998.

25 Financial liabilities – subordinated debt

	As at 31 December 2009 £'000	As at 31 December 2008 £'000
Subordinated debt	18,136	20,256

The Group issued a \$30m subordinated bond on 19 September 2006. The bond bears a variable interest rate set at three month US dollar LIBOR plus 3.3%. The bond must be redeemed by no later than 15 September 2036 at the principal plus any accrued interest. The Group has the option to redeem all or some of the bond at any time on or after 15 December 2011. The subordinated debt is carried at amortised cost. As the debt is held in US\$ the movement in the exchange rate has meant that when re-valued to the reporting currency the subordinated debt is held on the balance sheet at a lower value than the previous reporting period. No further capital has been added to the loan.

26 Insurance liabilities and reinsurance assets

	As at 31 December 2009 £'000	As at 31 December 2008 £'000
Gross		
Claims reported	107,628	98,664
Loss adjustment expenses	4,001	2,818
Claims incurred but not reported	55,108	44,817
Unearned premiums	112,817	92,325
Total gross insurance liabilities	279,554	238,624
Recoverable from reinsurers		
Claims reported	33,772	28,963
Claims incurred but not reported	11,983	8,204
Unearned premiums	18,371	9,687
Total reinsurers' share of insurance liabilities	64,126	46,854
Net		
Claims reported	73,856	69,701
Loss adjustment expenses	4,001	2,818
Claims incurred but not reported	43,125	36,613
Unearned premiums	94,446	82,638
Total net insurance liabilities	215,428	191,770

The gross liabilities for claims reported, loss adjustment expenses and claims incurred but not reported are net of expected recoveries from salvage and subrogation. The amounts for salvage and subrogation at the end of 2009 and 2008 are not material.

Movement in outstanding claims reserves

	Gross £'000	Reinsurance £'000	Net £'000
Claims reported	62,986	(25,035)	37,951
Loss adjustment expenses	2,045	-	2,045
Claims incurred but not reported	34,866	(5,205)	29,661
Total as at 1 January 2008	<u>99,897</u>	<u>(30,240)</u>	<u>69,657</u>
Increase in year	18,576	29	18,605
Net exchange adjustments	27,826	(6,956)	20,870
Total as at 31 December 2008	<u>146,299</u>	<u>(37,167)</u>	<u>109,132</u>
Claims reported	98,664	(28,963)	69,701
Loss adjustment expenses	2,818	-	2,818
Claims incurred but not reported	44,817	(8,204)	36,613
Total as at 31 December 2008	<u>146,299</u>	<u>(37,167)</u>	<u>109,132</u>
Increase in year	31,273	(11,181)	20,092
Net exchange adjustments	(10,835)	2,593	(8,242)
Total as at 31 December 2009	<u>166,737</u>	<u>(45,755)</u>	<u>120,982</u>
Claims reported	107,628	(33,772)	73,856
Loss adjustment expenses	4,001	-	4,001
Claims incurred but not reported	55,108	(11,983)	43,125
Total as at 31 December 2009	<u>166,737</u>	<u>(45,755)</u>	<u>120,982</u>

Movement in provision for unearned premiums

	Gross £'000	Reinsurance £'000	Net £'000
As at 1 January 2008	73,294	(7,999)	65,295
Movement during 2008	19,031	(1,688)	17,343
As at 31 December 2008	<u>92,325</u>	<u>(9,687)</u>	<u>82,638</u>
Movement during 2009	20,492	(8,684)	11,808
As at 31 December 2009	<u>112,817</u>	<u>(18,371)</u>	<u>94,446</u>

27 Deferred income tax liability

	2009 £'000	2008 £'000
As at 1 January	8,471	9,833
Charge/ (credit) in year (note 13)	1,489	(1,362)
As at 31 December	<u>9,960</u>	<u>8,471</u>

28 Trade and other payables

	As at 31 December 2009 £'000	As at 31 December 2008 £'000
Arising out of direct insurance operations	3,367	3,870
Arising out of reinsurance operations	27,089	25,325
Other creditors	9,775	10,080
Derivative liabilities (foreign exchange contracts)	-	2,639
	<u>40,231</u>	<u>41,914</u>

All trade and other payables are due within twelve months of the balance sheet date.

Trade and other payables (excluding derivative liabilities) are initially recognised at fair value and subsequently measured at amortised cost. Derivative liabilities are trading financial instruments and are measured at fair value.

29 Net assets per share

Net assets and net tangible assets per share are calculated based on the number of ordinary shares in issue at the year end, excluding ordinary shares purchased by the Group and held as treasury shares.

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Net assets	152,091	101,729
Intangible asset	<u>(15,509)</u>	<u>(15,509)</u>
Net tangible assets	136,582	86,220
Issued shares at 31 December (number of shares '000s)	52,318	35,760
Effect of own shares held (number of shares '000s)	<u>(1,001)</u>	<u>(623)</u>
Issued shares after adjustment (number of shares '000s)	<u>51,317</u>	<u>35,137</u>
Net assets per share	£2.96	£2.90
Net tangible assets per share	£2.66	£2.45

30 Share-based payments

During the year ended 31 December 2009, the Group had a number of long-term employee incentive schemes which are classified as equity settled share-based payments.

The compensation cost recognised in the income statement under IFRS2, Share-based payments, is as follows:

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Deferred annual bonus scheme awards	633	429
SAYE options scheme	17	12
Performance share plan	937	551
	<u>1,587</u>	<u>992</u>

Deferred annual bonus (“DAB”) scheme

The DAB scheme was approved by shareholders in June 2005 and first launched in March 2006. Awards of deferred shares and matching shares are made under the scheme. Awards will be satisfied by the transfer of shares from the Group's

Employee Benefit Trust, which may acquire shares for this purpose by buying shares in the market. The Trustees have waived their entitlement to dividends on any shares acquired.

Awards of deferred shares are granted equivalent to the value of the annual bonus deferred divided by the share price on the date of grant. Under the scheme all employees have the opportunity to defer up to 30% of their annual bonus. During the vesting period each participant is entitled to instruct the Trustee to vote on the deferred shares held on his or her behalf and is entitled to receive dividends, or dividend equivalent payments, which are paid in respect of deferred share awards.

Up to one matching share is awarded for every deferred share. Matching shares will vest partly or in full on the third anniversary of the date of grant to the extent that certain performance conditions are met. The performance conditions are described in full in the Directors' Remuneration Report. Matching shares do not receive the right to vote or receive dividends during the vesting period.

The fair value of the matching share awards is measured as the market share price, adjusted to take into account the terms and conditions on which the shares are granted. The fair value of the matching share awards granted during the year was £831,600 (2008: £700,112).

Save as you earn ("SAYE") share option scheme

The SAYE scheme was approved by shareholders in June 2005 and first launched in May 2006.

Under the scheme all employees have the opportunity to participate in a 3 year savings plan. Participants can save up to £250 per month, which is used to purchase shares at a pre-determined discounted fixed option price. For all scheme years to date, the discount was 10% off the market value of the group's shares on the launch date.

The fair value of the options granted under the scheme is estimated using the Black-Scholes option-pricing model. The fair value of the options granted during the year was £43,808 (2008: £6,349).

The significant inputs into the Black-Scholes model are as follows:

Share options granted on	2 May 2007	30 April 2008	30 April 2009
Number of options issued	15,697	17,338	78,948
Share price at the date of grant	£2.83	£2.83	£2.92
Exercise price	£2.61	£2.66	£2.46
Standard deviation of expected share price returns	20%	20%	27%
Option life	3 years	3 years	3 years
Annual risk free interest rate	4.5%	4.5%	1.7%
Dividend yield	3.7%	3.7%	3.7%

Performance share plan ("PSP")

The PSP scheme was approved by shareholders in May 2007 and first launched later that month.

Under the scheme some senior employees receive awards of free shares, which will vest after three years subject to performance conditions and continued employment.

The performance measure is split into two separate and equal parts; one part having a net tangible asset ("NTA") value condition and the other having a total shareholder return ("TSR") condition.

For the NTA condition full vesting will only occur at NTA per share growth of 45% above the Retail Price Index ("RPI") over three years. No vesting will occur below a 15% growth level, with a pro-rata vesting between these points. The NTA per share is adjusted to add back dividends paid in the performance period.

For the TSR condition, performance is measured over three years against a comparator group of other insurance companies. Full vesting will occur on achievement of upper quartile performance. No vesting will occur at median performance, with pro-rata vesting between upper quartile and median performance.

The fair value of the awards granted under the scheme has been estimated using appropriate valuation methodologies. With respect to the NTA condition the fair value has been calculated using assumptions about the likelihood of meeting the performance criteria based on the Director's expectations in light of the Group's business model and market conditions.

The fair value of the awards under the TSR condition has been estimated using a Monte-Carlo simulation model, which calculates a fair value based on a large number of randomly generated simulations of the Company's share price.

The fair value of the awards granted during the year was £1,243,704 (2008: £1,016,574).

The significant inputs into the valuation model are as follows:

Awards granted on	2 May 2007		26 Mar 2008		26 Mar 2009	
	NTA condition	TSR condition	NTA condition	TSR condition	NTA condition	TSR condition
Number of awards granted	214,001	214,001	242,909	242,909	279,484	279,484
Share price at the date of grant	£2.78	£2.78	£2.71	£2.71	£2.71	£2.71
Volatility of expected share price returns	N/A	19%	N/A	21%	N/A	27%
– company						
Volatility of expected share price returns	N/A	26%	N/A	31%	N/A	38%
– comparator group						
Correlation with comparator group	N/A	11%	N/A	20%	N/A	16%
Expected life	3 years	3 years	3 years	3 years	3 years	3 years
Annual risk free interest rate	N/A	5.4%	N/A	4.0%	N/A	1.7%

31 Commitments

Non-cancellable operating lease rentals are payable as follows:

	Year ended 31 December 2009 £'000	Year ended 31 December 2008 £'000
Less than one year	199	159
Between one and five years	1,428	199
	<u>1,627</u>	<u>358</u>

During 2009 the UK operation moved to a new premises. The commitments shown above reflect the future rental obligations for the new office and also the ongoing obligations associated with the old premises. The old premises is being actively marketed which could reduce the commitment in future accounting periods.

IAS 12 – Provisions, contingent assets and contingent liabilities requires disclosure of amounts recognised for provisions for an onerous lease. Due to the above mentioned lease commitment the group has recognised an expense of £259,532 (2008: £nil), along with a corresponding liability, in respect of the creation of the onerous lease. This amount is determined using the best estimates available at the time of creation. The liability recognised will be amended in future reporting periods dependent on market changes and any sub-lease that may be in force.

32 Contingencies

The managed syndicates are subject to the New Central Fund annual subscription, which is an annual fee calculated on gross premiums written by the syndicates. This fee was 0.5% for 2008 and 2009. In addition to this fee, the Council of Lloyd's has the discretion to call a further contribution of up to 3% of the syndicate's managed capacity if required.

33 Related parties

Directors of the Company and their immediate relatives control 4.07% (2008: 3.78%) of the voting shares of the Company. This includes the shares held in the Hardy EBT. The company considers that the directors are the key management personnel of the company in the context of the IAS 24 definition.

In addition to salaries, the Group also provides non-cash benefits to directors and executive officers, and contributes to a post-employment defined contribution pension plan on their behalf. Directors participated in the Group's share option schemes. Full details of all the elements of remuneration payable to the directors are contained in the Directors' Remuneration Report. No other transactions took place between the Company and key management personnel.

34 Principal subsidiary companies of Hardy Underwriting Bermuda Limited

The Company owns 100% of the ordinary share capital in the following subsidiaries.

Hardy Underwriting Group Plc*	UK Holding company
Hardy Re Limited*	Bermudian Reinsurance company
Hardy Bermuda Limited*	Bermudian managing general agent
Hardy Underwriting Limited	UK corporate member of Lloyd's
Hardy Names Limited	UK corporate member of Lloyd's
Hardy (Underwriting Agencies) Limited	UK managing agent
Hardy Insurance Services Limited	UK Service company

* held directly

The company also owns 50% of the ordinary share capital in Hardy Arig Insurance Management (HAIM), a joint venture with Arig Insurance. HAIM, which was established in 2009 and is based in Bahrain, focuses on construction, property and on shore energy. Primarily HAIM writes business from the Middle East and North African regions but also considers business from other parts of Asia and Africa. Both Hardy and Arig have equal representation on the board of directors of HAIM.

Financial Calendar

17 March 2010	Ex-dividend date for second interim dividend
19 March 2010	Record date for the second interim dividend
1 April 2010	Payment of second interim dividend
August 2010	Announcement of interim results for the period ending 30 June 2010
September 2010	Payment of dividend for interim period ending 30 June 2010