VALIDUS HOLDINGS LTD
Form 10-Q
May 11, 2009

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2009
Commission file number 001-33606

VALIDUS HOLDINGS, LTD.
(Exact name of registrant as specified in its charter)

BERMUDA	**98-0501001**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

19 Par-La-Ville Road, Hamilton, Bermuda HM 11
(Address of principal executive offices and zip code)
(441) 278-9000
(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer , accelerated filer and small reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer þ	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No þ

As of May 11, 2009, there were 76,143,925 outstanding Common Shares, $0.175 par value per share, of the registrant.

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PART I. FINANCIAL INFORMATION

ITEM I. FINANCIAL STATEMENTS

Validus Holdings, Ltd.

Consolidated Balance Sheets

As at March 31, 2009 (unaudited) and December 31, 2008

(Expressed in thousands of U.S. dollars, except share and per share amounts)

	March 31, 2009 (unaudited)	December 31, 2008
Assets		
Fixed maturities, at fair value (amortized cost: 2009 - $2,712,715; 2008 - $2,553,018)	$ 2,644,496	$ 2,454,501
Short-term investments, at fair value (amortized cost: 2009 - $283,806; 2008 - $379,537)	282,363	377,036
Cash and cash equivalents	535,798	449,848
Total investments and cash	3,462,657	3,281,385
Premiums receivable	600,943	408,259
Deferred acquisition costs	143,510	108,156
Prepaid reinsurance premiums	59,510	22,459
Securities lending collateral	99,727	98,954
Loss reserves recoverable	204,197	208,796
Paid losses recoverable	4,438	1,388
Net receivable for investments sold		490
Income taxes recoverable	1,244	1,365
Intangible assets	126,177	127,217
Goodwill	20,393	20,393
Accrued investment income	20,511	20,433
Other assets	19,491	23,185
Total assets	$ 4,762,798	$ 4,322,480
Liabilities		
Reserve for losses and loss expenses	$ 1,318,732	$ 1,305,303
Unearned premiums	795,233	539,450
Reinsurance balances payable	66,180	33,042
Securities lending payable	105,369	105,688
Deferred income taxes	20,914	21,779
Net payable for investments purchased	57,434	
Accounts payable and accrued expenses	71,650	74,184
Debentures payable	304,300	304,300
Total liabilities	2,739,812	2,383,746
Commitments and contingent liabilities		

Shareholders equity		
Common shares, 571,428,571 authorized, par value $0.175 Issued and outstanding (2009 - 75,828,922; 2008 - 75,624,697)	13,271	13,235
Additional paid-in capital	1,419,602	1,412,635
Accumulated other comprehensive (loss)	(8,054)	(7,858)
Retained earnings	598,167	520,722
Total shareholders equity	2,022,986	1,938,734
Total liabilities and shareholders equity	$ 4,762,798	$ 4,322,480

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

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Validus Holdings, Ltd.
Consolidated Statements of Operations and Comprehensive Income
For the Three Months Ended March 31, 2009 and 2008 (Unaudited)

(Expressed in thousands of U.S. dollars, except share and per share amounts)

	March 31, 2009 (Unaudited)	March 31, 2008 (Unaudited)
Revenues		
Gross premiums written	$ 609,892	$ 521,594
Reinsurance premiums ceded	(72,512)	(84,900)
Net premiums written	537,380	436,694
Change in unearned premiums	(218,621)	(144,830)
Net premiums earned	318,759	291,864
Net investment income	26,772	36,043
Net realized (losses) gains on investments	(23,421)	7,744
Net unrealized gains (losses) on investments	22,153	(14,977)
Other income	757	935
Foreign exchange (losses) gains	(4,200)	8,179
Total revenues	340,820	$ 329,788
Expenses		
Losses and loss expenses	131,834	140,024
Policy acquisition costs	61,449	56,701
General and administrative expenses	38,079	37,107
Share compensation expense	7,354	6,535
Finance expenses	7,723	21,517
Total expenses	246,439	261,884
Net income before taxes	94,381	67,904
Income tax benefit (expense)	526	(1,429)
Net income	$ 94,907	$ 66,475
Comprehensive income		
Foreign currency translation adjustments	(196)	67
Comprehensive income	$ 94,711	$ 66,542
Earnings per share		

Weighted average number of common shares and common share equivalents outstanding				
Basic		75,744,577		74,209,371
Diluted		79,102,643		78,329,727
Basic earnings per share	$	1.23	$	0.87
Diluted earnings per share	$	1.20	$	0.85
Cash dividends declared per share	$	0.20	$	0.20

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

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Validus Holdings, Ltd.
Consolidated Statements of Shareholders Equity

For the Three Months Ended March 31, 2009 and 2008 (Unaudited)
(Expressed in thousands of U.S. dollars, except share and per share amounts)

	March 31, 2009 (Unaudited)	March 31, 2008 (Unaudited)
Common shares		
Balance Beginning of period	$ 13,235	$ 12,985
Issue of common shares	36	5
Balance End of period	$ 13,271	$ 12,990
Additional paid-in capital		
Balance Beginning of period	$ 1,412,635	$ 1,384,604
Issue of common shares, net of expenses	(387)	164
Share compensation expense	7,354	6,535
Balance End of period	$ 1,419,602	$ 1,391,303
Accumulated other comprehensive income (loss)		
Balance Beginning of period	$ (7,858)	$ (49)
Currency translation adjustments	(196)	67
Balance End of period	$ (8,054)	$ 18
Retaining earnings (deficit)		
Balance Beginning of period	$ 520,722	$ 537,260
Dividends	(17,462)	(17,388)
Net income	94,907	66,475
Balance End of period	$ 598,167	$ 586,347
Total shareholders equity	$ 2,022,986	$ 1,990,658

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

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Validus Holdings, Ltd.
Consolidated Statements of Cash Flows

For the Three Months Ended March 31, 2009 and 2008 (Unaudited)
(Expressed in thousands of U.S. dollars, except share and per share amounts)

	March 31, 2009 (Unaudited)	March 31, 2008 (Unaudited)
Cash flows provided by (used in) operating activities		
Net income for the period	$ 94,907	$ 66,475
Adjustments to reconcile net income to cash provided by (used in) operating activities:		
Share compensation expense	7,354	6,535
Net realized losses (gains) on sales of investments	23,421	(7,744)
Net unrealized (gains) losses on investments	(22,153)	14,977
Amortization of intangible assets	1,040	1,040
Foreign exchange losses (gains) on cash and cash equivalents included in net income	559	(5,701)
Amortization of premium on fixed maturities	1,702	226
Change in:		
Premiums receivable	(193,076)	(170,863)
Deferred acquisition costs	(35,344)	(30,318)
Prepaid reinsurance premiums	(37,160)	(48,992)
Loss reserves recoverable	4,413	15,782
Paid losses recoverable	(3,051)	811
Income taxes recoverable	(653)	4,701
Accrued investment income	(86)	(2,226)
Other assets	3,083	85
Reserve for losses and loss expenses	15,064	51,935
Unearned premiums	255,782	193,221
Reinsurance balances payable	33,260	51,447
Deferred income taxes	93	(3,242)
Accounts payable and accrued expenses	(1,288)	(7,009)
Net cash provided by operating activities	147,867	131,140
Cash flows provided by (used in) investing activities		
Proceeds on sales of investments	873,352	573,454
Proceeds on the maturities of investments	222,402	66,540
Purchases of fixed maturities	(1,232,740)	(973,142)
Sales (purchases) of short-term investments, net	94,644	117,157
Decrease (increase) in securities lending payable	319	(28,144)
Net cash used in investing activities	(42,023)	(244,135)
Cash flows provided by (used in) financing activities		

Issue of common shares, net of expenses		(351)		169
Dividends paid		(17,462)		(17,388)
(Increase) decrease in securities lending collateral		(319)		28,144
Net cash (used in) provided by financing activities		(18,132)		10,925
Effect of foreign currency rate changes on cash and cash equivalents		(1,762)		4,719
Net increase (decrease) in cash		85,950		(97,351)
Cash and cash equivalents Beginning of period		449,848		444,698
Cash and cash equivalents End of period	$	535,798	$	347,347
Taxes paid (recovered) during the period	$	299	$	(114)
Interest paid during the period	$	6,672	$	7,641

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

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Validus Holdings, Ltd.

Notes to Consolidated Financial Statements (Unaudited)

(Expressed in thousands of U.S. dollars, except share and per share amounts)

1. Basis of preparation and consolidation

These unaudited consolidated financial statements include Validus Holdings, Ltd. and its wholly owned subsidiaries (together, the Company) and have been prepared in accordance with U.S. Generally Accepted Accounting Principles (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In addition, the year-end balance sheet data was derived from audited financial statements but does not include all disclosures required by U.S. GAAP. This Quarterly Report should be read in conjunction with the Company s Annual Report on Form 10-K for the year ended December 31, 2008, as filed with the U.S. Securities and Exchange Commission (the SEC).

In the opinion of management, these unaudited consolidated financial statements reflect all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the Company s financial position and results of operations as at the end of and for the periods presented. Certain amounts in prior periods have been reclassified to conform to current period presentation. All significant intercompany accounts and transactions have been eliminated. The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. The major estimates reflected in the Company s consolidated financial statements include the reserve for losses and loss expenses, premium estimates for business written on a line slip or proportional basis, the valuation of goodwill and intangible assets, reinsurance recoverable balances including the provision for unrecoverable reinsurance recoverable balances and investment valuation. Actual results could differ from those estimates. The results of operations for any interim period are not necessarily indicative of the results for a full year. The terms FAS and FASB used in these notes refer to Statements of Financial Accounting Standards issued by the United States Financial Accounting Standards Board.

2. Recent accounting pronouncements

In December 2007, the FASB issued Statements No. 141(R), Business Combinations (FAS 141(R)) and No. 160, Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51 (FAS 160) which are effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. In April 2009, the FASB issued FASB Staff Position FAS 141(R)-1 Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies (FSP FAS 141(R)-1). FSP FAS 141(R)-1 has amended FAS 141(R) s guidance on the initial recognition and measurement, subsequent measurement and accounting, and disclosure of assets acquired and liabilities assumed in a business combination that arise from contingencies.

Significant changes arising from FAS 141 (R) and FSP FAS 141(R)-1 which will impact any future acquisitions include the determination of the purchase price and treatment of transaction expenses, restructuring charges and negative goodwill as follows;

Purchase Price Under FAS 141(R), the purchase price is determined as of the acquisition date, which is the date that the acquirer obtains control. Previously, the date the business combination was announced was used as the effective date in determining the purchase price;

Transactions Expenses Under FAS 141(R), all costs associated with purchase transactions must be expensed as incurred. Previously, all such costs could be capitalized and included as part of transaction purchase price, adding to the amount of goodwill recognized;

Restructuring Costs Under FAS 141(R), expected restructuring costs are not recorded at the closing date, but rather after the transaction. The only costs to be included as a liability at the closing date are those for which an

Validus Holdings, Ltd.

Notes to Consolidated Financial Statements (Unaudited)

(Expressed in thousands of U.S. dollars, except share and per share amounts)

acquirer is obligated at the time of the closing. Previously, restructuring costs that were planned to occur after the closing of the transaction were recognized and recorded at the closing date as a liability;

Negative Goodwill/Bargain Purchases Under FAS 141(R), where total fair value of net assets acquired exceeds consideration paid (creating negative goodwill), the acquirer will record a gain as a result of the bargain purchase, to be recognized through the income statement at the close of the transaction. Previously, negative goodwill was recognized as a pro rata reduction of the assets assumed to allow the net assets acquired to equal the consideration paid; and

Noncontrolling Interests Under FAS 141(R), in a partial or step acquisition where control is obtained, 100% of goodwill and identifiable net assets are recognized at fair value and the noncontrolling (sometimes called minority interest) interest is also recorded at fair value. Previously, in a partial acquisition only the controlling interest s share of goodwill was recognized, the controlling interest s share of identifiable net assets was recognized at fair value and the noncontrolling interest s share of identifiable net assets was recognized at carrying value. Under FAS 160, a noncontrolling interest is now recognized in the equity section, presented separately from the controlling interest s equity. Previously, noncontrolling interest in general was recorded in the mezzanine section.

The adoption of FAS 141(R) and FSP FAS 141(R)-1 are not expected to have a material impact on the Company s consolidated financial statements, but will impact any future acquisitions.

In June 2008, the FASB issued FASB Staff Position EITF 03-6-1, Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities (FSP EITF 03-6-1). FSP EITF 03-6-1 addresses whether instruments granted in share-based payment transactions may be participating securities prior to vesting and, therefore, need to be included in the earnings allocation in computing basic earnings per share (EPS) pursuant to the two-class method described in paragraphs 60 and 61 of FASB Statement No. 128, Earnings per Share. FSP EITF 03-6-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008. The adoption of FSP EITF 03-6-1 has not had a material impact on the Company s consolidated financial statements.

In August 2008, the FASB issued proposed amendments to FAS 128, Earnings per Share (proposed amendments to FAS 128). The proposed amendments to FAS 128 reflect the FASB s efforts to converge with International Financial Reporting Standards and to improve the guidance on earnings per share (EPS). The proposed amendments to FAS 128 would be retrospectively applied to all prior-period EPS data. An effective date has not been established. The Company will continue to evaluate the potential impact of this guidance.

In January 2009, the FASB issued FASB Staff Position EITF 99-20-1 Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests That Continue to Be Held by a Transferor in Securitized Financial Assets (FSP EITF 99-20-1). FSP EITF 99-20-1 amends certain recognition aspects of other-than-temporary impairments (OTTI). FSP EITF 99-20-1 is effective prospectively for interim and annual periods ending after December 15, 2008. Retrospective application of FSP EITF 99-20-1 to a prior interim or annual period is prohibited. As the Company s investment portfolio is classified as trading, the adoption of the FSP EITF 99-20-1 has not had a material impact on the Company s consolidated financial statements.

In April 2009, the FASB issued FASB Staff Positions FAS 157-4 Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly (FSP FAS 157-4) and FAS 115-2 and FAS 124-2 Recognition and Presentation of Other-Than-Temporary Impairments (FSP FAS 115-2 and FAS 124-2). FSP FAS 157-4 provides additional guidance for estimating fair value in accordance with FAS 157, Fair Value Measurements, specifically; (1) estimating the fair value of an asset or liability (financial and nonfinancial) when the volume and level of activity for the asset or liability have significantly decreased; and (2) identifying transactions that are not orderly. The primary change to the OTTI model for debt securities, as a result of FSP FAS 115-2 and FAS 124-2, is the change in focus from an entity s intent and ability to hold a security until recovery. Instead, an OTTI is triggered if; (1) an entity has the intent to sell the security; (2) it is more likely than not that it will be required to sell the security before recovery; or (3) it does not expect to recover the entire amortized cost basis of the security. Both FSPs are effective for interim and annual periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. However, FSP FAS 157-4 and FSP FAS 115-2 and FAS 124-2 must be adopted concurrently. The Company has not elected to early adopt these two FASB Staff Positions. The adoption of proposed FSP FAS 157-4 and FSP FAS 115-2 and FAS 124-2 are not expected to have a material impact on the Company s consolidated financial statements.

Validus Holdings, Ltd.
Notes to Consolidated Financial Statements (Unaudited)

(Expressed in thousands of U.S. dollars, except share and per share amounts)

In April 2009, the FASB issued FASB Staff Position FAS 107-1 and APB 28-1 Interim Disclosures about Fair Value of Financial Instruments (FSP FAS 107-1 and APB 28-1). FSP FAS 107-1 and APB 28-1 expands the fair value disclosures required for all financial instruments within the scope of Statement 107 to interim periods for publicly traded entities. The FSP also requires entities to disclose the method(s) and significant assumptions used to estimate the fair value of financial instruments in financial statements on an interim basis and to highlight any changes of the methods and significant assumptions from prior periods. FSP FAS 107-1 and APB 28-1 is effective for interim and annual periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. However, an entity that chooses to early adopt FSP FAS 107-1 and APB 28-1 must also early adopt FSP FAS 157-4 and FSP FAS 115-2 and FAS 124-2. The Company has not elected to early adopt this FASB Staff Position. As FSP FAS 107-1 and APB 28-1 only expands certain disclosures requirements, its adoption is not expected to have a material impact on the Company s consolidated financial statements.

3. Investments

During the first quarter of 2007, the Company adopted FAS 157 and FAS 159. Prior to January 1, 2007, the Company s investments in fixed maturities were classified as available-for-sale and carried at fair value, with related net unrealized gains or losses excluded from earnings and included in shareholders equity as a component of accumulated other comprehensive income. The Company believes that accounting for its investment portfolio as trading more closely reflects its investment guidelines. Beginning on January 1, 2007, the Company s investments in fixed maturities were classified as trading and carried at fair value, with related net unrealized gains or losses included in earnings.

During the third quarter of 2008, the Company adopted FSP FAS 157-3. Consistent with this statement, certain market conditions allow for fair value measurements that incorporate unobservable inputs where active market transaction based measurements are unavailable.

(a) Classification within the fair value hierarchy under FAS 157

Under FAS 157, a company must determine the appropriate level in the fair value hierarchy for each fair value measurement. The fair value hierarchy in FAS 157 prioritizes the inputs, which refer broadly to assumptions market participants would use in pricing an asset or liability, into three levels. It gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The level in the fair value hierarchy within which a fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices within Level 1 that are observable for the asset or liability, either directly or indirectly. A significant adjustment to a Level 2 input could result in the Level 2 measurement becoming a Level 3 measurement. Level 3 inputs are unobservable inputs for the asset or liability.

Level 1 primarily consists of financial instruments whose value is based on quoted market prices or alternative indices but for which the Company typically obtained independent external valuation information including U.S. and U.K. Treasuries, overnight repos and commercial paper. Level 2 includes financial instruments that are valued through independent external sources using models or other valuation methodologies. These models are primarily industry-standard models that consider various assumptions, including time value, yield curve, prepayment speeds, default rates, loss severity, current market and contractual prices for the underlying financial instruments, as well as other relevant economic measures. Sustainably all of these assumptions are observable in the marketplace, can be derived from observable data or are supported by observable levels at which transactions are executed in the marketplace. The Company performs internal procedures on the valuations received from independent external sources. Financial instruments in this category include U.S. Treasuries, sovereign debt, corporate debt and U.S.

agency and non-agency mortgage and asset-backed securities. Level 3 includes financial instruments that are valued using market approach and income approach valuation techniques. These models incorporate both observable and unobservable inputs. Financial instruments in this category include certain residential mortgage-backed securities.

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Validus Holdings, Ltd.
Notes to Consolidated Financial Statements (Unaudited)

(Expressed in thousands of U.S. dollars, except share and per share amounts)

At March 31, 2009, the Company s investments are allocated between levels 1, 2 and 3 as follows:

	Level 1	Level 2	Level 3	Total
U.S. Government and Government Agency	$	$ 937,973	$	$ 937,973
Non-U.S. Government and Government Agency		86,222		86,222
States, municipalities, political subdivision		15,618		15,618
Agency residential mortgage-backed securities		533,923		533,923
Non-Agency residential mortgage-backed securities		107,619	99,739	207,358
U.S. corporate		541,819		541,819
Non-U.S. corporate		113,369		113,369
Catastrophe bonds		24,636		24,636
Asset-backed securities		95,109		95,109
Commercial mortgage-backed securities		88,469		88,469
Total fixed maturities		2,544,757	99,739	2,644,496
Total short-term investments	275,775	6,588		282,363
Total	$ 275,775	$ 2,551,345	$ 99,739	$ 2,926,859

At December 31, 2008, the Company s investments are allocated between Levels 1, 2 and 3 as follows:

	Level 1	Level 2	Level 3	Total
U.S. Government and Government Agency	$	$ 768,344	$	$ 768,344
Non-U.S. Government and Government Agency		96,073		96,073
States, municipalities, political subdivision		15,516		15,516
Agency residential mortgage-backed securities		433,736		433,736
Non-Agency residential mortgage-backed securities		119,813	111,318	231,131
U.S. corporate		443,847		443,847
Non-U.S. corporate		125,700		125,700
Catastrophe bonds		10,872		10,872
Asset-backed securities		137,023		137,023
Commercial mortgage-backed securities		192,259		192,259
Total fixed maturities		2,343,183	111,318	2,454,501
Total short-term investments	365,357	11,679		377,036
Total	$ 365,357	$ 2,354,862	$ 111,318	$ 2,831,537

Validus Holdings, Ltd.
Notes to Consolidated Financial Statements (Unaudited)

(Expressed in thousands of U.S. dollars, except share and per share amounts)

At March 31, 2009, Level 3 investments totaled $99,739, representing 3.4% of total investments measured at fair value on a recurring basis. At December 31, 2008, Level 3 investments totaled $111,318, representing 3.9% of total investments measured at fair value on a recurring basis.

The following table presents a reconciliation of the beginning and ending balances for all investments measured at fair value on a recurring basis using Level 3 inputs as at March 31, 2009 and December 31, 2008:

	Residential mortgage-backed securities	
	Three months ended March 31, 2009	**Year ended December 31, 2008**
Level 3 investments Beginning of period	$ 111,318	$
Net payments, purchases , sales and maturities	(822)	(59)
Realized losses	(1,284)	
Unrealized losses	(6,870)	(14,603)
Amortization	(2,603)	(4,048)
Net transfers in		130,028
Level 3 investments End of period	$ 99,739	$ 111,318

(b) Net investment income

Net investment income is derived from the following sources:

	March 31, 2009	**March 31, 2008**
Fixed maturities and short-term investments	$ 26,517	$ 31,691
Cash and cash equivalents	761	4,838
Securities lending income	339	435
Total gross investment income	27,617	36,964
Investment expenses	(845)	(921)
Net investment income	$ 26,772	$ 36,043

The following represents an analysis of net realized (losses) gains and the change in unrealized gains (losses) of investments:

	March 31, 2009	**March 31, 2008**
Fixed maturities, short-term investments and cash equivalents		
Gross realized gains	$ 9,453	$ 8,356
Gross realized losses	(32,874)	(612)

Net realized (losses) gains on investments	(23,421)	7,744
Change in unrealized gains (losses) of investments	21,061	(13,765)
Change in unrealized gains (losses) of securities lending	1,092	(1,212)
Total net realized (losses) gains and change in unrealized gains (losses) of investments	$ (1,268)	$ (7,233)

Validus Holdings, Ltd.
Notes to Consolidated Financial Statements (Unaudited)

(Expressed in thousands of U.S. dollars, except share and per share amounts)

(c) Fixed maturity and short-term investments

The amortized cost, gross unrealized gains and losses and estimated fair value of investments at March 31, 2009 are as follows:

	Amortized Cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
U.S. Government and Government Agency	$ 912,457	$ 25,516	$	$ 937,973
Non-U.S. Government and Government Agency	98,604	3,015	(15,397)	86,222
States, municipalities, political subdivision	14,864	754		15,618
Agency residential mortgage-backed securities	521,339	12,976	(392)	533,923
Non-Agency residential mortgage-backed securities	282,583	42,681	(117,906)	207,358
U.S. corporate	549,414	6,022	(13,617)	541,819
Non-U.S. corporate	123,325	1,920	(11,876)	113,369
Catastrophe bonds	25,011		(375)	24,636
Asset-backed securities	96,100	523	(1,514)	95,109
Commercial mortgage-backed securities	89,018	24	(573)	88,469
Total fixed maturities	2,712,715	93,431	(161,650)	2,644,496
Total short-term investments	283,806	28	(1,471)	282,363
Total	$ 2,996,521	$ 93,459	$ (163,121)	$ 2,926,859

The amortized cost, gross unrealized gains and losses and estimated fair value of investments at December 31, 2008 are as follows:

	Amortized Cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
U.S. Government and Government Agency	$ 732,155	$ 36,189	$	$ 768,344
Non-U.S. Government and Government Agency	115,389	4,403	(23,719)	96,073
States, municipalities, political subdivision	14,954	562		15,516
Agency residential mortgage-backed securities	425,533	8,358	(155)	433,736

Non-Agency residential mortgage-backed securities	299,346	47,276	(115,491)	231,131
U.S. corporate	454,810	2,126	(13,089)	443,847
Non-U.S. corporate	140,807	1,696	(16,803)	125,700
Catastrophe bonds	11,012	2	(142)	10,872
Asset-backed securities	141,209		(4,186)	137,023
Commercial mortgage-backed securities	217,803		(25,544)	192,259
Total fixed maturities	2,553,018	100,612	(199,129)	2,454,501
Total short-term investments	379,537	55	(2,556)	377,036
Total	$ 2,932,555	$ 100,667	$ (201,685)	$ 2,831,537

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Validus Holdings, Ltd.
Notes to Consolidated Financial Statements (Unaudited)

(Expressed in thousands of U.S. dollars, except share and per share amounts)

The following table sets forth certain information regarding the investment ratings of the Company s fixed maturities portfolio as at March 31, 2009 and December 31, 2008. Investment ratings are the lower of Moody s or Standard & Poor s rating for each investment security, presented in Standard & Poor s equivalent rating. For investments where Moody s and Standard & Poor s ratings are not available, Fitch ratings are used and presented in Standard & Poor s equivalent rating.

	March 31, 2009		December 31, 2008	
	Estimated fair value	% of total	Estimated fair value	% of total
AAA	$ 1,909,626	72.1%	$ 1,941,349	79.1%
AA	194,649	7.4%	146,923	6.0%
A	422,700	16.0%	338,966	13.8%
BBB	17,805	0.7%	12,427	0.5%
Investment grade	2,544,780	96.2%	2,439,665	99.4%
BB	31,659	1.2%	7,416	0.3%
B	44,280	1.7%	7,420	0.3%
CCC	23,777	0.9%		
Non-Investment grade	99,716	3.8%	14,836	0.6%
Total	$ 2,644,496	100.0%	$ 2,454,501	100.0%

The amortized cost and estimated fair value amounts for fixed maturity securities held at March 31, 2009 and December 31, 2008 are shown by contractual maturity. Actual maturity may differ from contractual maturity because certain borrowers may have the right to call or prepay certain obligations with or without call or prepayment penalties.

	March 31, 2009		December 31, 2008	
	Amortized cost	Estimated fair value	Amortized cost	Estimated fair value
Due in one year or less	$ 264,071	$ 264,589	$ 277,137	$ 279,727
Due after one year through five years	1,436,408	1,432,819	1,143,494	1,134,275
Due after five years through ten years	20,821	19,518	17,451	17,493
Due after ten years	2,375	2,711	31,045	28,858
	1,723,675	1,719,637	1,469,127	1,460,353
Asset-backed and mortgage-backed Securities	989,040	924,859	1,083,891	994,148
Total	$ 2,712,715	$ 2,644,496	$ 2,553,018	$ 2,454,501

The Company has a five year, $500,000 secured letter of credit facility provided by a syndicate of commercial banks. At March 31, 2009, approximately $272,779 (December 31, 2008: $199,186) of letters of credit were issued and outstanding under this facility for which $354,805 of investments were pledged as collateral (December 31, 2008: $258,573). In 2007, the Company entered into a $100,000 standby letter of credit facility which provides Funds at Lloyd s. At March 31, 2009, $100,000 (December 31, 2008: $100,000) of letters of credit were issued and outstanding under this facility for which $125,345 of investments were pledged as collateral (December 31, 2008: $144,149). In addition, $1,155,934 of investments are held in trust at March 31, 2009 (December 31, 2008: $1,100,235). Of those, $1,088,319 are held in trust for the benefit of Talbot s cedants and policyholders, and to facilitate the accreditation as an alien insurer/reinsurer by certain regulators (December 31, 2008: $1,032,267).

Validus Holdings, Ltd.
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(d) Securities lending

The Company participates in a securities lending program whereby certain securities from its portfolio are loaned to third parties for short periods of time through a lending agent. The Company retains all economic interest in the securities it lends and receives a fee from the borrower for the temporary use of the securities. Collateral in the form of cash, government securities and letters of credit is required at a rate of 102% of the market value of the loaned securities and is held by a third party. As at March 31, 2009, the Company had $103,099 (December 31, 2008: $103,266) in securities on loan. During the three months ended March 31, 2009, the Company recorded a $1,092 unrealized gain on this collateral on its Statements of Operations (March 31, 2008: unrealized loss $1,212).

Securities lending collateral reinvested is primarily comprised of corporate floating rate securities with an average reset period of 24.3 days (December 31, 2008: 26.7 days). As at March 31, 2009, the securities lending collateral reinvested by the Company in connection with its securities lending program is allocated between Levels 1, 2 and 3 as follows:

	Level 1	Level 2	Level 3	Total
Corporate	$	$ 29,837	$	$ 29,837
Asset-backed securities		14,029		14,029
Short-term investments	10,321	45,540		55,861
	$ 10,321	$ 89,406	$	$ 99,727

As at December 31, 2008, the securities lending collateral reinvested by the Company in connection with its securities lending program are allocated between Levels 1, 2 and 3 as follows:

	Level 1	Level 2	Level 3	Total
Corporate	$	$ 57,574	$	$ 57,574
Asset-backed securities		18,228		18,228
Short-term investments	7,390	15,762		23,152
	$ 7,390	$ 91,564	$	$ 98,954

The following table sets forth certain information regarding the investment ratings of the Company s securities lending collateral reinvested as at March 31, 2009 and December 31, 2008. Investment ratings are the lower of Moody s or Standard & Poor s rating for each investment security, presented in Standard & Poor s equivalent rating. For investments where Moody s and Standard & Poor s ratings are not available, Fitch ratings are used and presented in Standard & Poor s equivalent rating.

	March 31, 2009		December 31, 2008	
	Estimated fair value	% of total	Estimated fair value	% of total
AAA	$ 64,474	64.7%	$ 45,137	45.7%
AA	20,128	20.2%	37,608	37.9%
A	4,684	4.7%	8,729	8.8%

NR	120	0.1%	90	0.1%
	89,406	89.7%	91,564	92.5%
NR- Cash (1)	10,321	10.3%	7,390	7.5%
Total	$ 99,727	100.0%	$ 98,954	100.0%

(1) This amount relates to cash and is therefore not a rated security.

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The amortized cost and estimated fair value amounts for securities lending collateral reinvested held at March 31, 2009 and December 31, 2008 are shown by contractual maturity below. Actual maturity may differ from contractual maturity because certain borrowers may have the right to call or prepay certain obligations with or without call or prepayment penalties.

	March 31, 2009		December 31, 2008	
	Amortized cost	Estimated fair value	Amortized cost	Estimated fair value
Due in one year or less	$ 57,325	$ 55,861	$ 24,390	$ 23,152
Due after one year through five years	48,044	43,866	81,298	75,802
Total	$ 105,369	$ 99,727	$ 105,688	$ 98,954

4. Reinsurance

The Company enters into reinsurance and retrocession agreements in order to mitigate its accumulation of loss, reduce its liability on individual risks, enable it to underwrite policies with higher limits, and increase its aggregate capacity. The cession of insurance and reinsurance does not legally discharge the Company from its primary liability for the full amount of the policies, and the Company is required to pay the loss and bear collection risk if the reinsurer fails to meet its obligations under the reinsurance or retrocession agreement. Amounts recoverable from reinsurers are estimated in a manner consistent with the underlying liabilities.

a) Credit risk

The Company evaluates the financial condition of its reinsurers and monitors concentration of credit risk arising from its exposure to individual reinsurers. The reinsurance program is generally placed with reinsurers whose rating, at the time of placement, was A- or better rated by Standard & Poor s or the equivalent with other rating agencies. Exposure to a single reinsurer is also controlled with restrictions dependent on rating. 99.5% of reinsurance recoverables (which includes loss reserves recoverable and recoverables on paid losses) at March 31, 2009 were from reinsurers rated A- or better and included $65,588 of IBNR recoverable (December 31, 2008: $71,580). Reinsurance recoverables by reinsurer are as follows:

	March 31, 2009		December 31, 2008	
	Reinsurance recoverable	% of Total	Reinsurance recoverable	% of Total
Top 10 reinsurers	$ 194,753	93.4%	$ 198,403	94.4%
Other reinsurers balances > $1 million	9,627	4.6%	8,987	4.3%
Other reinsurers balances < $1 million	4,255	2.0%	2,794	1.3%
Total	$ 208,635	100.0%	$ 210,184	100%

Validus Holdings, Ltd.
Notes to Consolidated Financial Statements (Unaudited)

(Expressed in thousands of U.S. dollars, except share and per share amounts)

		March 31, 2009	
Top 10 Reinsurers	**Rating**	**Reinsurance recoverable**	**% of Total**
Fully collateralized reinsurers	NR	$ 77,937	39.9%
Hannover Re	AA-	34,078	17.5%
Lloyd s syndicates	A+	27,561	14.2%
Munich Re	AA-	13,680	7.0%
Allianz	AA	13,100	6.7%
Swiss Re	A+	12,023	6.2%
Aspen	A	6,390	3.3%
Transatlantic Re	A+	3,460	1.8%
Platinum Underwriters	A	3,459	1.8%
Axa	AA	3,065	1.6%
		$ 194,753	100.0%

		December 31, 2008	
Top 10 Reinsurers	**Rating**	**Reinsurance recoverable**	**% of Total**
Fully collateralized reinsurers	NR	$ 83,511	41.9%
Hannover Re	AA-	32,855	16.6%
Lloyd s syndicates	A+	25,533	12.9%
Allianz	AA	14,988	7.6%
Swiss Re	AA-	13,207	6.7%
Munich Re	AA-	12,813	6.5%
Aspen	A	6,040	3.0%
Platinum Underwriters	A	3,270	1.6%
Transatlantic Re	A+	3,096	1.6%
Axa	AA	3,090	1.6%
		$ 198,403	100.0%

At March 31, 2009 and December 31, 2008, the provision for uncollectible reinsurance relating to losses recoverable was $3,333, and $3,228, respectively. To estimate the provision for uncollectible reinsurance recoverable, the reinsurance recoverable must first be allocated to applicable reinsurers. This determination is based on a process rather than an estimate, although an element of judgment must be applied. As part of this process, ceded IBNR is allocated by reinsurer. Of the $208,635 reinsurance recoverable at March 31, 2009, $77,937 was fully collateralized (December 31, 2008: $83,511).

The Company uses a default analysis to estimate uncollectible reinsurance. The primary components of the default analysis are reinsurance recoverable balances by reinsurer and default factors used to determine the portion of a reinsurer s balance deemed to be uncollectible. Default factors require considerable judgment and are determined using the current rating, or rating equivalent, of each reinsurer as well as other key considerations and assumptions.

b) Collateralized quota share retrocession treaties

On December 22, 2007, Validus Re entered into a collateralized retrocessional reinsurance agreement with an unaffiliated third party whereby the Company cedes certain business underwritten in the marine offshore energy lines. For the three months ended March 31, 2009 and 2008, Validus Re ceded $891 and $11,731, respectively of premiums written through this agreement. The earned portion of premiums ceded for the three months ended March 31, 2009 and 2008 were $1,071 and $2,764, respectively.

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5. Share capital

a) Authorized and issued

The Company s authorized share capital is 571,428,571 voting and non-voting shares with a par value of $0.175 each. The holders of common voting shares are entitled to receive dividends and are allocated one vote per share, provided that, if the controlled shares of any shareholder or group of related shareholders constitute more than 9.09 percent of the outstanding common shares of the Company, their voting power will be reduced to 9.09 percent.

The following table is a summary of the common shares issued and outstanding:

	March 31, 2009	December 31, 2008
Balance- beginning of period	75,624,697	74,199,836
Restricted share awards vested	187,146	777,953
Employee seller shares vested	17,079	515,103
Options exercised		112,825
Warrants exercised		18,980
Balance- end of period	75,828,922	75,624,697

b) Warrants

During the three months ended March 31, 2009, no warrants were exercised.

c) Deferred Share Units

Under the terms of the Company s Director Stock Compensation Plan, non-management directors may elect to receive their director fees in deferred share units rather than cash. The number of shares units distributed in case of election under the plan is equal to the amount of the annual retainer fee otherwise payable to the director on such payment date divided by 100% of the fair market value of a share on such payment date. Additional deferred share units are issued in lieu of dividends that accrue on these deferred share units. The total outstanding deferred share units at March 31, 2009 were 4,468 (December 31, 2008 : 4,430)

d) Dividends

On February 12, 2009, the Company announced a quarterly cash dividend of $0.20 (2008: $0.20) per common share and $0.20 per common share equivalent for which each outstanding warrant is then exercisable, payable on March 31, 2009 to holders of record on March 16, 2009.

6. Stock plans

a) Long-term incentive plan

The Company s Long Term Incentive Plan (LTIP) provides for grants to employees of any option, stock appreciation right (SAR), restricted share, restricted share unit, performance share, performance unit, dividend equivalent or other share-based award. The total number of shares reserved for issuance under the LTIP is 13,126,896 shares. The LTIP is administered by the Compensation Committee of the Board of Directors. No SARs, performance shares, performance units or dividend equivalents have been granted to date. Grant prices are established at the estimated fair market value of the Company s common shares at the date of grant.

b) LTIP options

Options granted under the LTIP may be exercised for voting common shares upon vesting. Options have a life of 10 years and vest ratably over five years from the date of grant. Grant prices are established at the estimated fair value of the Company s common shares at the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions used for all grants to date: risk free interest rates of 3.5% (2008: 3.53%), expected life of 7 years (2008: 7 years), expected volatility of 30.0% (2008: 30%)

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and a dividend yield of 3.20% (2008: 3.20%). Expected volatility is based on stock price volatility of comparable publicly-traded companies. The Company uses the simplified method outlined in the SEC Staff Accounting Bulletin 110 to estimate expected lives for options granted during the period as historical exercise data is not available and the options met the requirement as set out in the bulletin. Share expense of $1,057 was recorded for the three months ended March 31, 2009 (2008: $1,023) related to options, with a corresponding increase to additional paid-in capital. The expense represents the proportionate accrual of the fair value of each grant based on the remaining vesting period. Activity with respect to the options for the three months ended March 31, 2009 is as follows:

	Options	Weighted average grant date fair value	Weighted average grant date exercise price
Options outstanding, December 31, 2008	2,799,938	$ 7.57	$ 18.23
Options granted			
Options exercised			
Options forfeited	(4,070)	10.30	20.39
Options outstanding, March 31, 2009	2,795,868	$ 7.56	$ 18.23
Options exercisable at March 31, 2009	1,494,872	$ 7.45	$ 17.84

Activity with respect to options for the year ended December 31, 2008 is as follows:

	Weighted	Weighted average

