2000

XL CAPITAL

ANNUAL REPORT

We have effectively produced not only a much more focused business structure but also one that demonstrates a greater level of accountability in each of our core segments.

Brian M. O Hara

STREAMLINED

During the past year XL Capital has continued the process of creating a more streamlined business structure. Our success in an ever-changing marketplace relies on ensuring that each of our centers of excellence is equipped with the tools to anticipate and adapt profitably to change. By building on our inherent core strengths, XL will optimize shareholder value and become stronger in the process.

Just as a seedling is planted and carefully nurtured to maturity, so XL has grown from a small company to the multinational business it is today. The trees featured in this year's Report illustrate how the Company has successfully controlled its expansion, has remained responsive to changes in its external environment and is positioned to show healthy performance now and in the future.

XL's new structure organizes business in three principal operating segments: Insurance, Reinsurance, and Financial Products and Services.

"We have effectively produced not only a much more focused business structure but also one that demonstrates a greater level of accountability in each of our core segments." Brian M. O'Hara

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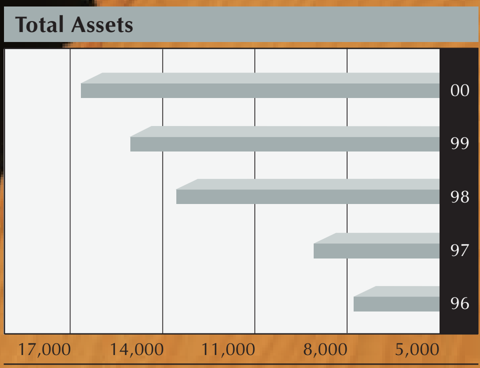
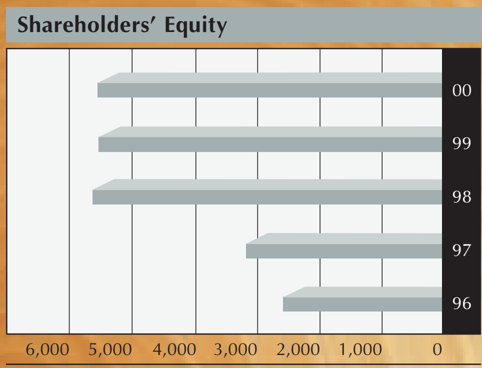
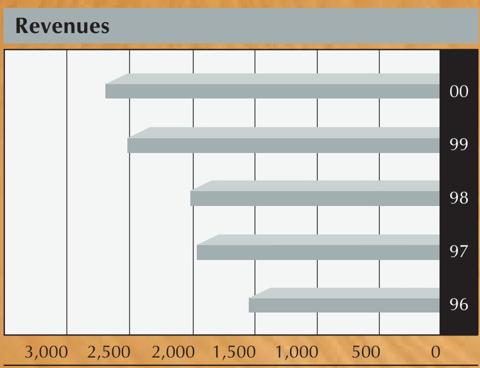
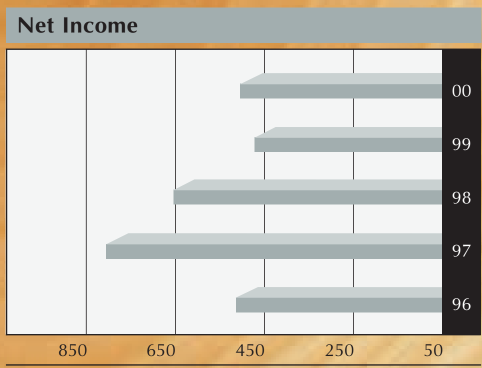
FINANCIAL HIGHLIGHTS

(at December 31, in millions U.S. Dollars)







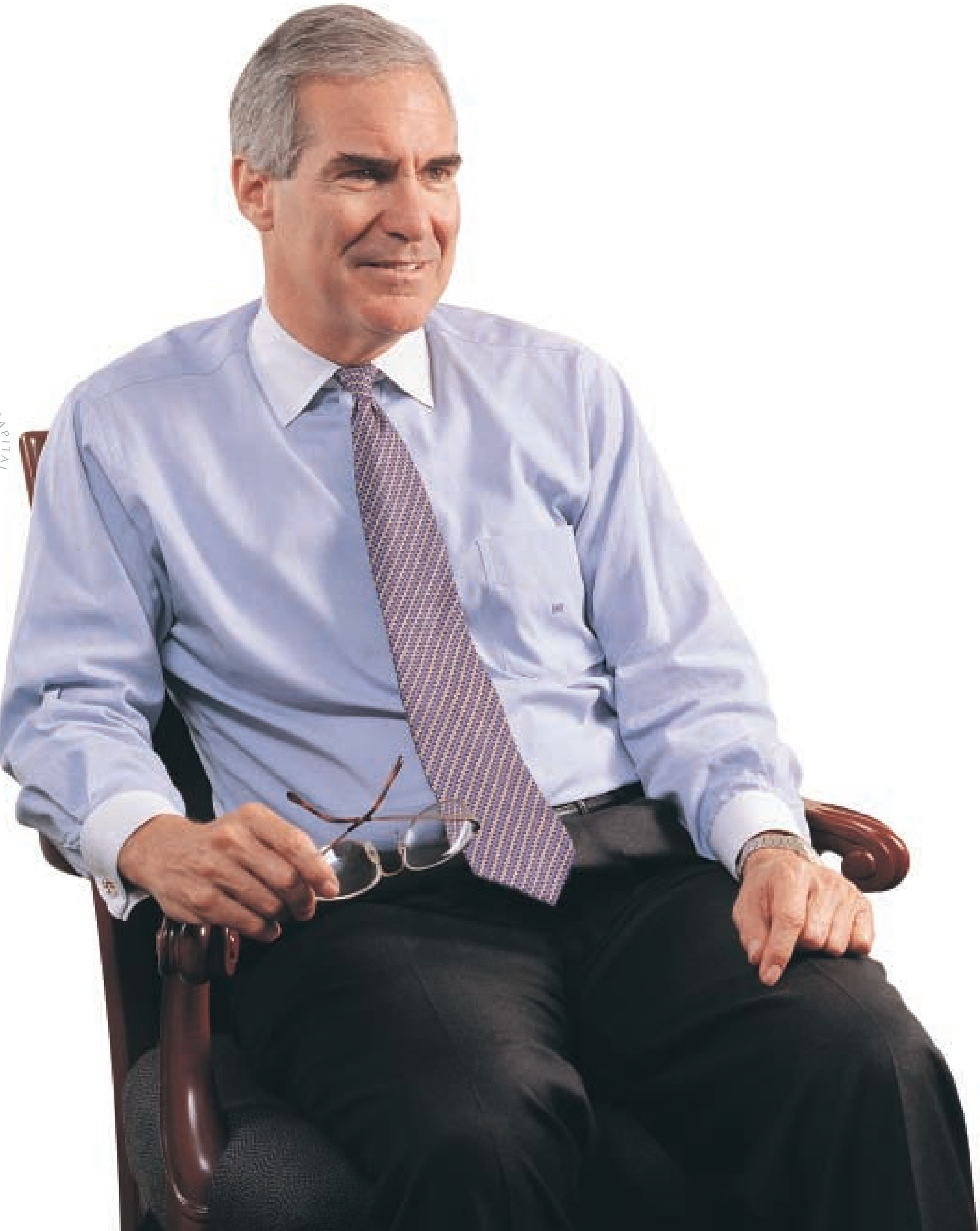


CONTENTS

This annual report contains "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995. A non-exclusive list of the important factors that could cause actual results to differ materially from those in such forward looking statements is set forth herein under the caption "Management's Discussion and Analysis of Results of Operations and Financial Condition – Cautionary Note Regarding Forward-Looking Statements".

LETTER TO SHAREHOLDERS

President and Chief Executive Officer Brian M. O'Hara



By focusing on our core operations in 2000, XL Capital Ltd had another year of strong growth both in our business and capabilities.

Our increased capabilities position us to expect in 2001 even greater growth and profitability in the ongoing market recovery in virtually all of our insurance and reinsurance business lines. A notable contribution to our enhanced position is the anticipated addition of Winterthur International, a recently announced acquisition, which will expand greatly our multi-national risk management capabilities and provide us with a significant presence in many European countries. This is our Company's best outlook for revenue growth since going public ten years ago.

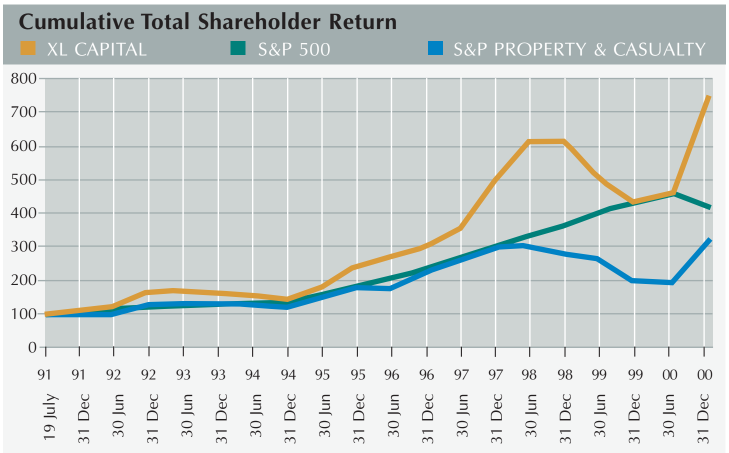
Our financial results demonstrate the Company's focus on performance, with increases in most business areas. Gross premiums written increased 28 percent from $2.4 billion in 1999 to $3.1 billion in 2000. Net premiums earned exceeded $2 billion for the first time, increasing 16 percent from $1.7 billion a year ago. Total revenues reached a record $2.7 billion, up 8 percent from last year's $2.5 billion. Total assets at the end of 2000 were $16.9 billion, up 12 percent from $15.1 billion at year-end 1999, while shareholders' equity remained constant at $5.6 billion. Fully diluted book value per share reached $44.78 at the end of 2000 up from $43.13 at December 31, 1999.

Net income increased to $506.3 million, or $4.03 per share, from $470.5 million, or $3.62 per share, despite the impact of realignment charges taken in the fourth quarter of 2000. Economic operating income, which excludes the amortization of intangible assets and net realized investment gains, increased nearly 20 percent to $626.2 million in 2000 from $523.4 million a year ago. Total economic return on equity, excluding goodwill, was 15.8 percent in 2000.

HIGHLIGHTS OF THE YEAR IN REVIEW

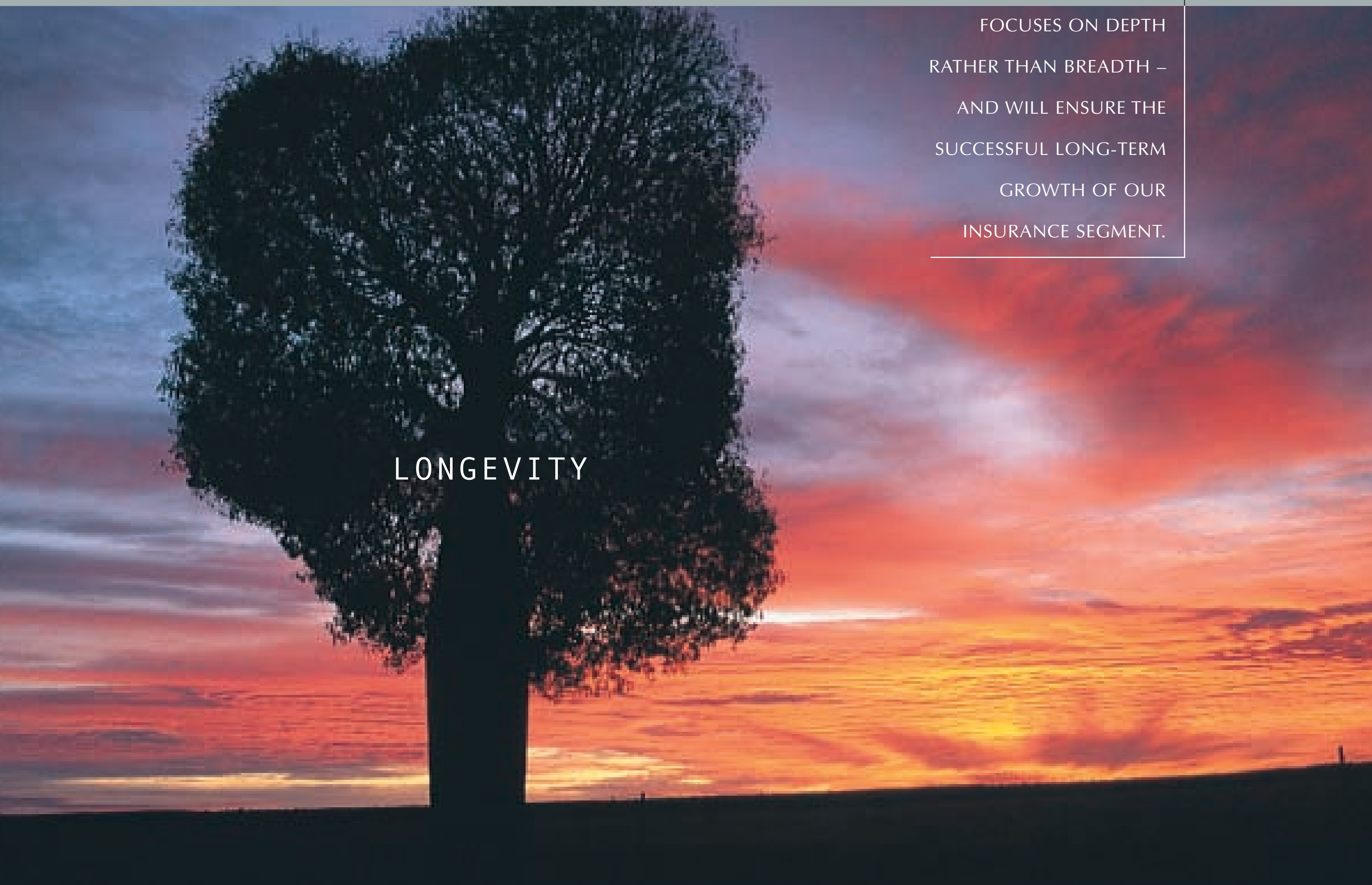
We have used trees as the theme of this year's report to shareholders. Each of the tree images illustrates how the Company has successfully grown, remained responsive to changes in its environment and positioned itself to show healthy performance now and in the future. There were a number of key accomplishments and actions taken this year which this theme reflects:

- We realigned the Company along three product lines: Insurance, Reinsurance and Financial Products and Services, appointing three chief executives of the new units. We created and filled a new position of Group Underwriting Officer.
- Our insurance business enjoyed significant growth in the United States, notably through premium contributions from ECS, our specialist environmental underwriting unit.
- We continued the expansion of our financial services capabilities. XL Capital Assurance, our financial guaranty insurance business unit, established itself in New York City.
- Our financial guaranty companies received AAA credit ratings from both Standard & Poor's and Fitch.
- We added to our growing portfolio additional strategic equity investments in the alternative investment management arena.
- We established Element Re to provide weather risk management products.
- We doubled our presence in the specialty surety market through the acquisition of CGU's surety operations.
- We consolidated the management of our reinsurance operations and established a unified brand "XL Re".
- We repurchased more than 5.1 million shares in 2000 and increased our annual dividend from $1.76 to $1.80 per share.
- Early in 2001 we announced the acquisition of Winterthur International, accomplishing our goal of becoming a truly global insurance organization.



Strategic
management

CAREFUL NURTURING HAS ENABLED US TO MAINTAIN A DISCIPLINED, TARGETED APPROACH TO BUSINESS – ONE THAT BUILDS ON OUR SPECIALTY EXPERTISE AND FOCUSES ON DEPTH RATHER THAN BREADTH – AND WILL ENSURE THE SUCCESSFUL LONG-TERM GROWTH OF OUR INSURANCE SEGMENT.



The Baobab tree is renowned for its longevity. Individual trees can live more than 1,000 years.

FROM LEFT: Fiona E. Luck, K. Bruce Connell and Paul S. Giordano

Our increased capabilities position us to expect even greater growth and prosperity in the ongoing market recovery in virtually all of our lines...

Product Focus

We realigned our business operations along product lines designating a Chief Executive for each of our three principal operating units, thus bringing accountability for each area under a strategic business leader and returning our focus to the Company's core products. Nick Brown, previously Chief Executive of NAC Re, was named Chief Executive for Insurance Operations, including our Lloyd's Syndicates. Henry Keeling, in addition to his duties at the former XL Mid Ocean Re, was given responsibility as Chief Executive of Reinsurance Operations for the Company's reinsurance businesses. Rob Lusardi moved from Chief Financial Officer to become Chief Executive of Financial Products and Services.

I am pleased to report that Jerry M. de St. Paer recently joined the Company as Executive Vice President and Chief Financial Officer. He has an extensive background in both the financial services and insurance industries, serving for many years as a senior executive of The Equitable (now AXA Financial Advisors) and the AXA Groupe.

Bruce Connell was made Group Underwriting Officer, a newly created position reporting directly to me. He will be responsible for overseeing underwriting practices and policies, and for coordinating the management of XL's aggregate loss exposures company wide.

Regrettably, Mark Brockbank retired as Chief Executive of The Brockbank Group plc. His daily presence at Lloyd's will be missed, but we are fortunate to continue to have Mark's services and vast experience as a consultant to XL Capital. He has been succeeded as Chief Executive Officer of the renamed XL Brockbank by Nicholas Metcalf who was previously the Active Underwriter of Syndicate 588.

We believe that these changes have effectively produced not only a much more focused business structure, but also one that assumes a greater level of accountability in each of our core business segments.

Growth of U.S. Operations

ECS, our environmental insurance specialist acquired in 1999, first wrote business for XL's account in 2000. We are continuing to expand our United States activities and have given Bill Kronenberg, President and Chief Executive Officer of ECS, expanded responsibility for all of XL's specialty program business in the U.S.

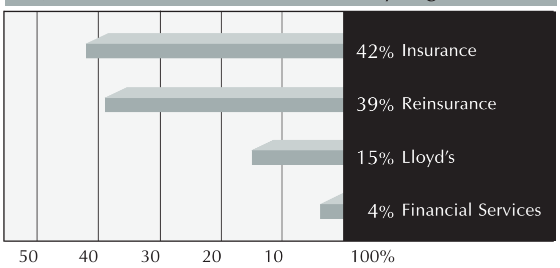
Strategic Investments

The Company continued to add to its strategic investment portfolio, expanding the Company's strategic equity investments in the alternative investment management business.

Element Re

Element Re was formed within our Financial Products and Services segment during 2000. Element Re will offer customers a range of non-catastrophic weather mitigation products designed to protect against the negative impact

Adjusted Gross Premiums Written by Segment



that normal weather fluctuations can have on the financial performance of companies operating in a variety of industries.

Increasingly, XL's customers are looking for sophisticated insurance and financial solutions to their risk management challenges. Beginning with weather, Element Re presents an opportunity to combine capital market expertise with the financial and underwriting strength of XL Capital. In the future, we believe that the integration of insurance and capital market products will become increasingly important in serving our customers' needs.

Financial Guaranty Units Receive Highest Ratings

One of our goals this past year was to obtain the highest credit ratings for our two financial guaranty companies. This was accomplished when XL Capital Assurance and XL Financial Assurance received AAA ratings from both Standard & Poor's and Fitch. We expect that these ratings will allow these two companies to compete effectively with all of the major competitors in this sector.

David Stevens was named President and Chief Executive Officer of XL Capital Assurance, which is headquartered in New York City. Jim McNichols was appointed Chief Operating Officer of XL Financial Assurance in Bermuda.

Expense Reduction Initiatives and Realignment of Operations

Last year, I initiated a company-wide expense reduction initiative. In a second phase of our desire to concentrate the Company's business and product lines in areas where XL is a leader, we exited several unprofitable lines of business and, for the first time, found it necessary to reduce staff. As a result, in the fourth quarter, the Company took a one-time charge of approximately $125.0 million, but we expect annual expense and other cost savings as we move forward.

Rebranding Business Units

As part of our goal to bring most of our units under a common XL brand identity, we renamed several units during the year. The principal reinsurance units of the Company will generally operate under a common brand, "XL Re". The Brockbank Group plc, the Company's Lloyd's operation, has become XL Brockbank and Brockbank Insurance Services, based in California, will become XL Aerospace, reflecting its main area of underwriting expertise. Many of the Company's insurance operations are also being realigned along major product lines and rebranded, incorporating the XL name tied to their respective areas of focus.

Share Repurchase

In January 2000, our Board authorized the repurchase of up to $500 million of the Company's shares as part of a continuing program of capital management. The Company repurchased 5.1 million of its shares for $247.7 million during 2000 at an average price of $48.82 per share.

Dividends paid to shareholders in 2000 totaled $1.80 per share, an increase of $0.04 per share from 1999, reflecting our desire to maintain a solid dividend payout ratio while practising good capital management. In February 2001, we again increased the dividend per share by a further $0.04 per annum. Having achieved one of the highest dividend payout ratios in our industry, we believe that an improved way to return excess capital to our shareholders in the future is through repurchases of our shares.

WINTERTHUR INTERNATIONAL

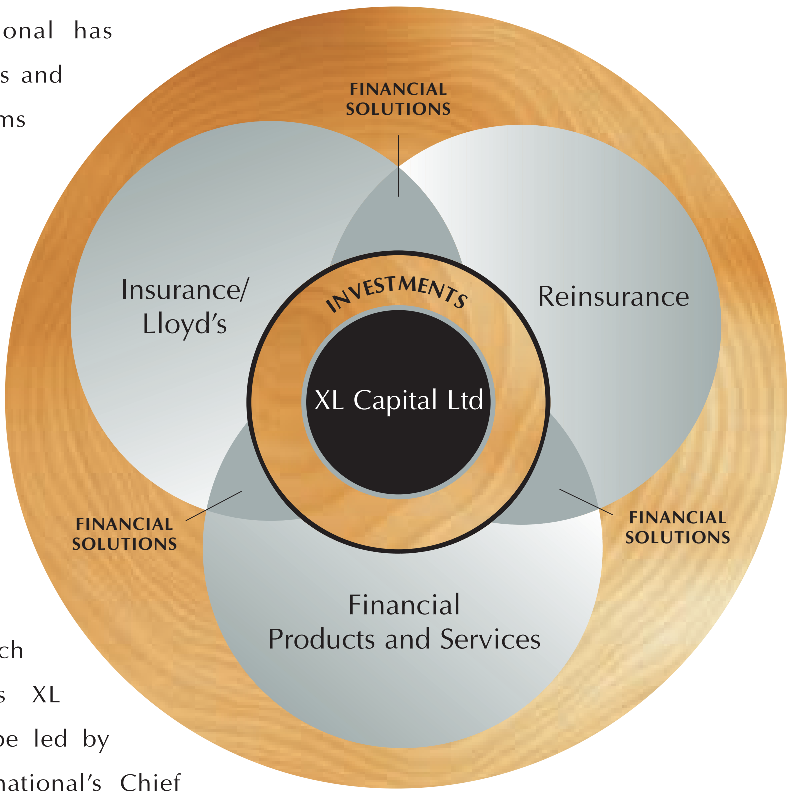
Our risk management strategy has been to build out XL in Europe and to develop in the U.S. on a primary basis. The acquisition of Winterthur International allows us to greatly accelerate these expansion goals. It provides us with primary capabilities in key geographic markets and complements our large account risk management business around the world.

Winterthur International operates in 27 countries, with relationships in approximately 40 additional countries and jurisdictions. Winterthur International has particularly strong business relationships with a large number of European customers and an excellent reputation for providing quality service in their markets. Winterthur International has approximately 1,100 employees and in 2000, had gross premiums written of approximately $1.4 billion with net premiums earned of approximately $600.0 million.

We expect the transaction, valued at approximately $600 million, to close in mid-2001. As an organization, we are excited about the prospects for the future of our combined risk management businesses, which will be known initially as XL Winterthur International and be led by Willi Sutter, Winterthur International's Chief Executive Officer. Clive Tobin, President and CEO of XL Insurance, will become Deputy Chief Executive and Chief Underwriting Officer of the new unit and will be responsible for the Americas region.

Many thanks must be given again this year to our Chairman, Mike Esposito, who along with the Board of Directors, has provided superior oversight and guidance at an important time in the Company's growth and development.

Ian R. Heap, one of our longest serving directors is retiring from the Board this year. Ian was XL's first Chief Executive Officer and has remained keenly involved in the Company's growth and development over his many years



of service. I am especially pleased that he has agreed to join our Advisory Council and look forward to many more years of valued advice. Dan McNamara, who came to our Board through the acquisition of NAC Re will also be retiring this year. He has provided valuable advice to the Company during the transition period and will continue to be of counsel in our continued development of our global insurance activities.

Once again, our employees have risen to the occasion as one of the toughest underwriting cycles in the industry's history bottomed out and has begun to turn. Without them and the brokers and other producers of our business, we would not have achieved the strong and growing market position and reputation we enjoy today.

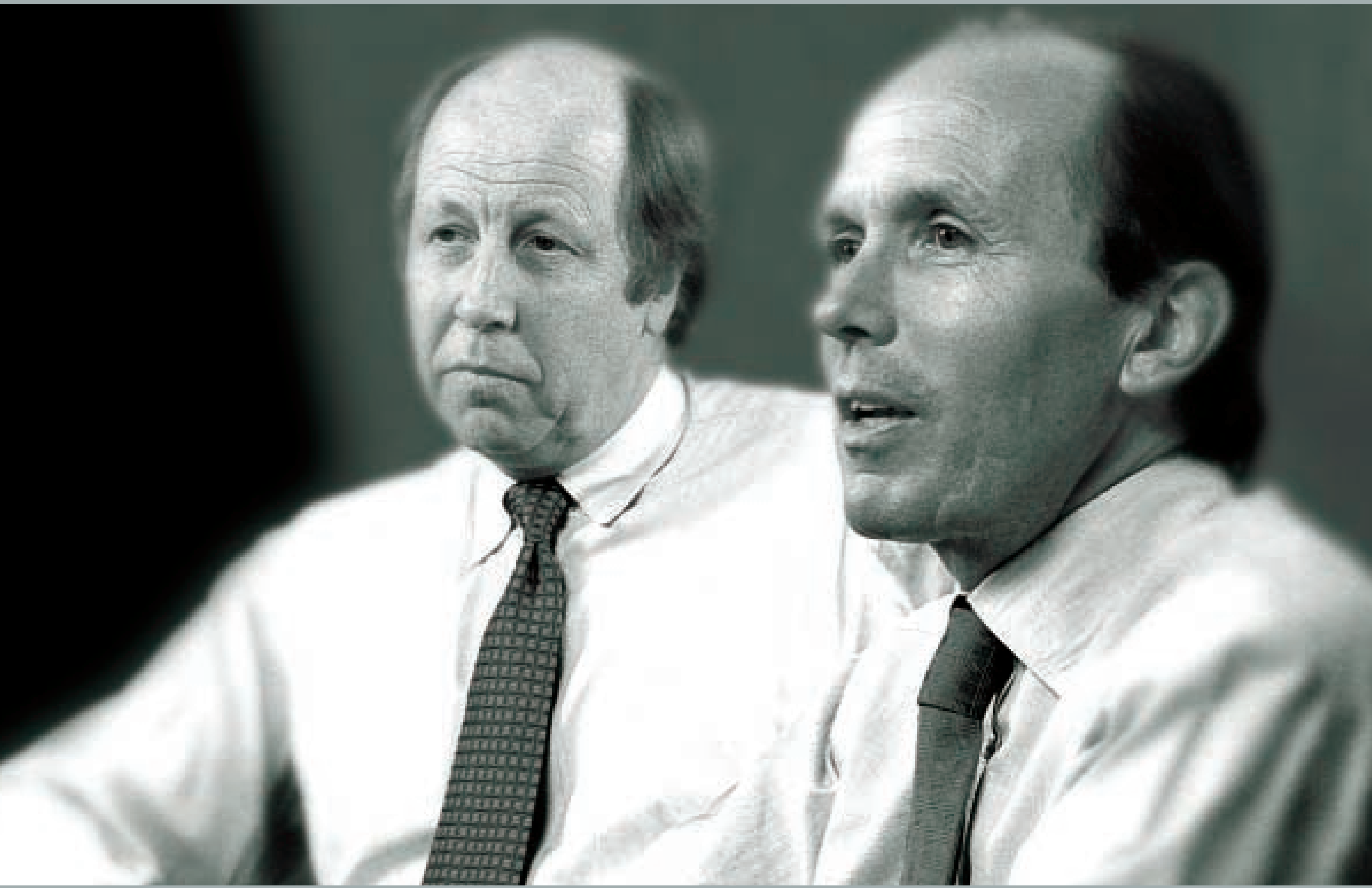
As this report goes to press, the Company is moving into its new world headquarters, XL House, in Bermuda. It is an exciting new era for XL Capital as we look forward to expanding our international operations with Winterthur International and to taking advantage of opportunities created by the improving insurance and reinsurance markets.

Our consolidated balance sheet is solid. Our business units are recognized specialists in their fields and leaders in their markets.

In 2001 we will celebrate both the 15th anniversary of our founding and our 10th year as a publicly traded company – and yet for us we view it as only the beginning!

BRIAN M. O'HARA
President and Chief Executive Officer

FROM LEFT: Clive Tobin and Christopher V. Greetham



The Company has successfully controlled its expansion, has remained responsive to changes in its environment…

FROM LEFT: Henry C.V. Keeling, Robert R. Lusardi and Nicholas M. Brown, Jr.

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OPERATIONS REVIEW

This report should be read in conjunction with Management's Discussion and Analysis of Results of Operations and Financial Condition and the Consolidated Financial Statements and the Notes thereto which are presented on pages F1 through F62 of this Annual Report.

In July 2000, the Company realigned the management of its operations along its three principal operating segments: Insurance, Reinsurance and Financial Products and Services. Three senior executives were appointed to lead these areas. These executives respond to questions about their respective operating segments below.

INSURANCE

Q. What businesses are you in?

NICHOLAS M. BROWN, JR., Chief Executive, Insurance Operations: Our group is responsible for XL's insurance operations worldwide. This includes the Company's Lloyd's syndicates, which I will discuss separately. While the scope of our operations includes all insurance opportunities, our strategy is clearly focused on commercial insurance markets and, within that segment, on large, complex risks and specialty lines of business which best capitalize on XL's expertise.

Q. In which markets do you operate?

BROWN: While we write business in many jurisdictions worldwide, our focus to date has been on three major markets: 1) the Bermuda market, where our operations started in the mid-80s; 2) the European market, where we have had a presence for over ten years; and 3) the North American market, which XL entered in the last three years through a series of start-up operations and acquisitions.

With the anticipated completion of the Winterthur International transaction, we will become truly global through the inclusion of Winterthur International's locations in 27 countries and relationships in many others.

Q. Can you describe the current operating environment and market conditions?

BROWN: The market over the past several years has been difficult. We have seen steadily declining pricing, putting pressure on profitability and causing a number of companies to pull out of certain markets and lines of business. The good news is that currently we are seeing increased prices in almost all lines. We think that the improvement in pricing bodes well for industry results as it continues and works its way through to the income statement over time.

Q. Who are your customers?

BROWN: Our customers range from XL's original large account market – often referred to as the Fortune 1000 – down to medium sized companies which are primarily interested in our specialty lines. While we write for a wide range of industry groups, we have strict underwriting guidelines, particularly for industry groups that have the most complex types of risks.

Q. What is your brand strategy?

BROWN: We offer products through a number of different entities, each with its own expertise. Our branding objective is to capitalize on the positive market reputation of our business units, represented by their individual names, while clearly identifying them as members of the XL family. We will be enhancing our marketing efforts significantly in this regard in 2001.

Q. Can you describe your key operating units?

BROWN: Other than our Lloyd's operations, which I will describe separately, our major business units and their most significant lines of businesses include:

- XL Insurance (risk management, Bermuda), which will be combined with Winterthur International and rebranded XL Winterthur International following the anticipated acquisition of Winterthur International
- ECS, which specializes in environmental insurance coverages
- Executive Liability Underwriters (professional lines, including directors & officers)
- XL Aerospace (satellite and aviation)
- XL Europe (risk management, Europe)
- XL Marine and Energy – North American (marine)
- XL Programs (specialty program business)
- XL Surety (surety bonds)

In addition, XL owns 50% of Sovereign Risk Insurance Ltd., one of the world's leading writers of political risk insurance.

Q. What were your key accomplishments during the past year?

BROWN: Clearly our major accomplishment was our ability to produce a combined ratio of under 90% (excluding one-time charges) in 2000 for the insurance segment in the midst of a very difficult market. This is the result of hard work and thorough underwriting discipline on the part of our staff.

Another of our major accomplishments last year was the restructuring of insurance operations. As we have matured as a company, it was clear that a purely geographically-driven organization limited our ability to meet the needs of our customers. We now have a group that is focused exclusively on insurance and an organization that stresses product and underwriting expertise over geography, meaning we can make our best expertise available to more of our customers. Further, in the case of our recent acquisitions, the restructuring has accelerated the process of moving towards a larger, global presence.

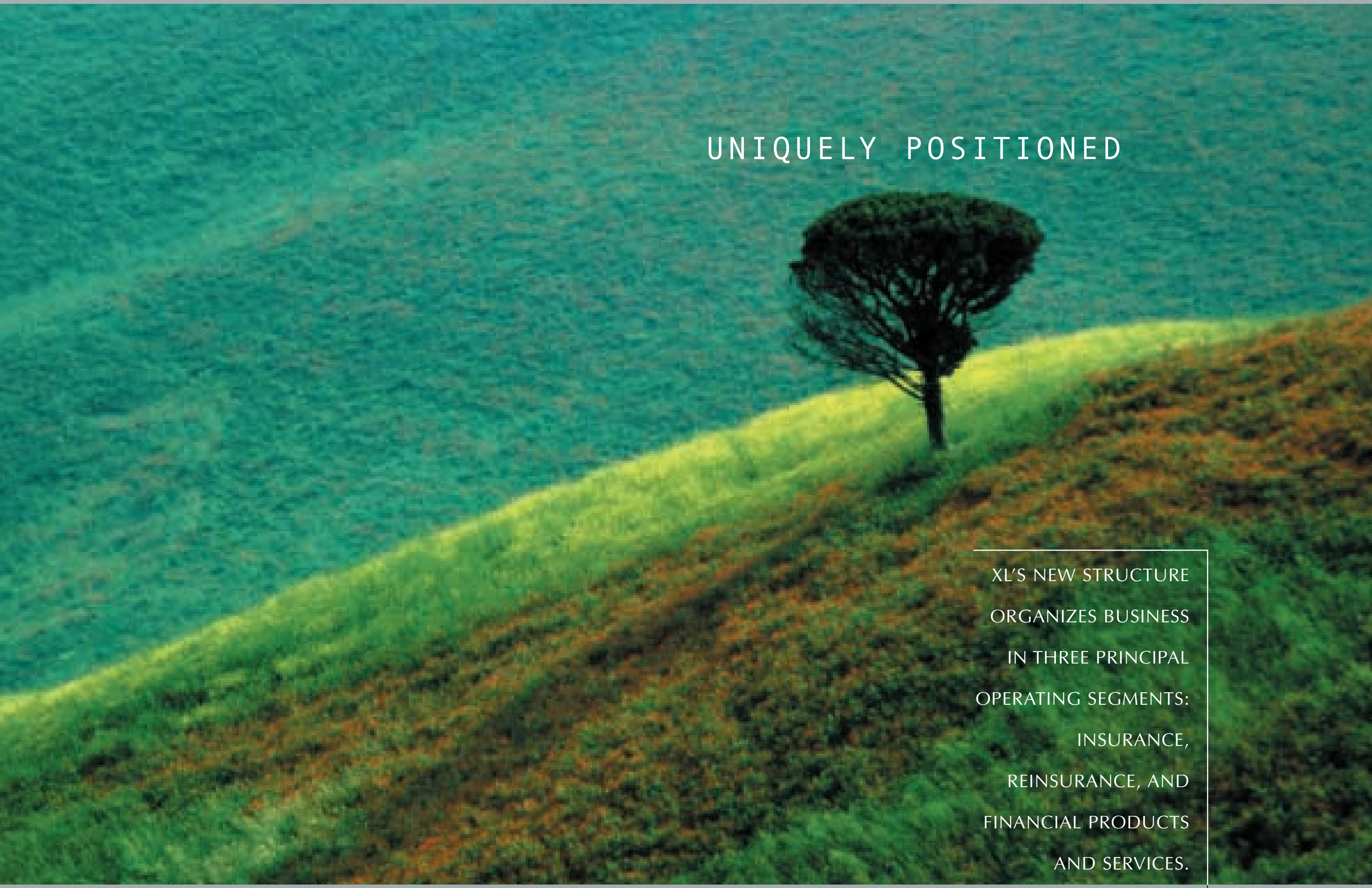
Along the way, we re-evaluated our businesses, re-underwriting entire books of business and closing down lines that we didn't feel could meet XL's profitability targets. This last activity was necessary in light of the market conditions we were seeing and the need to be focused on profitable opportunities.

Q. Looking forward, what is your goal for the Insurance Operations?

BROWN: Our goal is to build a highly profitable, efficient insurance operation that continues to capitalize on our underwriting strengths in specialty lines. We need to continue the integration activities to develop new product offerings and to leverage even further the opportunities we have to market additional XL products to existing customers. We will continue to start or invest in new operations that we think have a strategic fit and that meet our financial and underwriting criteria.

We are especially excited about the opportunities that the combined XL and Winterthur International risk management businesses provide for the Company as well as the potential we foresee arising from a new, Internet-based, small commercial operation we plan to launch later this year.

UNIQUELY POSITIONED



XL'S NEW STRUCTURE ORGANIZES BUSINESS IN THREE PRINCIPAL OPERATING SEGMENTS: INSURANCE, REINSURANCE, AND FINANCIAL PRODUCTS AND SERVICES. BY ALIGNING BUSINESS OPERATIONS BASED ON PRODUCT LINES, WE HAVE ESTABLISHED A SINGLE STRATEGIC DIRECTION AND ARE BETTER POSITIONED TO LEVERAGE OUR GROUP-WIDE CAPABILITIES.

Flexible

Some trees are able to adapt to even the most unexpected of environments.

LLOYD'S SYNDICATES

Lloyd's is also an integral part of the Company's Insurance Operations, but is reported separately as the nature of these operations and the market in which the syndicates underwrite is significantly different from the Company's other insurance subsidiaries.

Q. Can you describe XL's Lloyd's operations?

BROWN: We have two managing agencies at Lloyd's, Brockbank and Denham, which we have recently combined into a single organization, XL Brockbank. XL Brockbank receives fees and commissions for underwriting services it provides to the syndicates it manages. Currently, the Company operates a total of four active syndicates (581, 861, 990 and 1209) and two motor syndicates in run-off (253 and 2253). Of these three are dedicated corporate syndicates (990, 1209 and 2253).

Q. What markets do you serve?

BROWN: Our Lloyd's operations serve a globally diverse group of clients seeking specialty insurance and reinsurance coverages which have traditionally been provided by the underwriting syndicates based in London. Our two major product lines are marine and political risk.

Q. Have you changed the focus of your Lloyd's business?

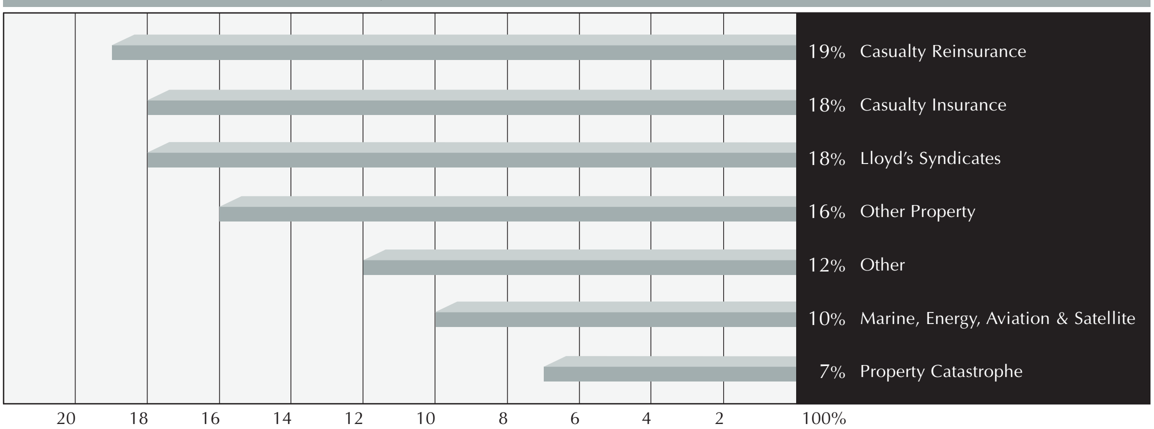
BROWN: Yes. A year ago we exited the motor insurance market which we considered non-core to our specialist commercial market focus. We also discontinued several lines of business late in 2000 as part of a company-wide realignment.

In addition to the restructuring, the most significant change to the group last year came with the retirement of Mark Brockbank. As founder of The Brockbank Group plc, Mark built an organization that is a leader in the Lloyd's market and left shoes that were difficult to fill. We were extremely fortunate that Nick Metcalf has assumed Mark's position and are very pleased that Nick will be able to lead our new Lloyd's operations.

Q. What is the capacity of your Lloyd's syndicates and how much of it does XL own?

BROWN: In 2000, the Company's total capacity of our Lloyd's syndicates was $787 million, of which XL Capital owned approximately 53 percent. As a result of trading activity last year, we were able to buy $90 million of the remaining third party Names' capacity. Consequently, XL

Business Mix (Net Premiums Earned, 2000)



Capital owns 63 percent of the 2001 capacity of $787 million.

Q. What is the outlook for your Lloyd's business?

BROWN: Although our operations have historically outperformed the broader Lloyd's market, our business has also suffered from the highly competitive market conditions experienced in the insurance and reinsurance markets over the last several years. These markets have also turned, as have most of the other areas where XL participates. As a market leader in many lines, I expect XL Brockbank to benefit from the current underwriting turn and contribute positively to XL's future financial performance.

REINSURANCE

Q. What benefits were derived from unifying the leadership of all XL Capital's Reinsurance Operations?

HENRY C.V. KEELING, Chief Executive, Reinsurance Operations: Unifying the leadership of the group's reinsurance operations has brought greater strategic coordination among our individual operating units and allows us to deliver a single message throughout the Reinsurance segment. We believe that this helps us forge a shared vision for our reinsurance operations and creates a better experience for clients and producers, to leverage internal synergies and generate growth. It has also enabled us to establish common disciplines and standards for underwriting, financial reporting and information technology together with the opportunity to cross-sell many more of our products to the clients of each of our specialist and regional units.

Q. What is the scope of XL Capital's Reinsurance Operations?

KEELING: In 2000, the Reinsurance Operations of the Company comprised the four major reinsurance units of the Company: XL Mid Ocean Re, NAC Re, Latin American Re and Le Mans Ré. The organizations are separate legal entities and together provide XL Capital with a true multi-national capability to serve its reinsurance clients.

Including Le Mans Ré, XL's Reinsurance Operations employ approximately 500 people in 24 offices located in 13 countries.

Q. What is the significance of the re-branding of XL's Reinsurance Operations?

KEELING: The renaming of our two largest reinsurance companies is aimed at making it easier for XL's reinsurance customers to do business with us wherever they are in the world. It was timely to change the names of XL Mid Ocean Re and NAC Re to reflect their role within the overall XL brand. Both companies will use the brand 'XL Re'. Latin American Re will similarly adopt the "XL Re" brand and an "XL Re" name during the course of 2001.

Q. What are your markets?

KEELING: Our reinsurance units have global capabilities, offering coverage on both a proportional and excess of loss basis. While we remain focused on those areas where we feel we can most effectively deploy our capacity and resources, we are involved in most lines of property and casualty reinsurance and, increasingly, life reinsurance.

XL Re Ltd operates from Bermuda, with key branch offices in London and Singapore, offering property, casualty, marine and aerospace coverage. We also have a specialist life and health reinsurance unit in London that works on pro-

Diversity

BUILDING ON XL'S INHERENT STRENGTHS, THE NEWLY-ESTABLISHED FINANCIAL PRODUCTS AND SERVICES BUSINESS SEGMENT CREATES DIVERSIFIED, NON-CORRELATED, STREAMS OF INCREASED EARNINGS. THIS SEGMENT WILL FACILITATE FURTHER GROWTH THROUGH THE DEVELOPMENT OF NEW PRODUCTS AND ENTRY INTO NEW MARKETS, AND BY ENABLING US TO LEVERAGE CORE CAPABILITIES.

STRENGTH

The roots of the mangrove tree help stabilize and build up shorelines.

viding financial solutions for customers, both on its own and in conjunction with other XL Capital units.

XL Reinsurance America Inc. – which is the new name being adopted for the former NAC Re – is based in the U.S. where it has traditionally provided specialty casualty reinsurance, property treaty and both property and casualty facultative lines primarily for U.S. customers.

The Company also owns 49% of Le Mans Ré in France and, through this vehicle, offers a broad range of reinsurance to the European market. Effective December 2000, we became the 100% owners of Latin American Re which, as its name implies, focuses on the Central and South American reinsurance markets.

Q. Can you describe the market conditions in your key reinsurance markets?

KEELING: We enjoyed a more normal catastrophe loss year in 2000 after being severely impacted in 1999 by several large natural events. During the second half of 2000, we began to see changes in most of the markets where we operate after several years of pricing declines. Currently almost all lines are receiving rate increases, with the range of price increases being driven by actual loss experience and changes in cedants' exposure rather than withdrawal of capacity.

Q. What were your key accomplishments in 2000?

KEELING: Our major achievement this past year was the successful restructuring of our Reinsurance Operations and the creation of "XL Re" as a common brand. In addition, we re-underwrote a significant portion of our casualty book, improving the profile and profitability of the Company's long-tailed exposure while, at the same time, withdrawing from a number of unprofitable lines. We believe that these actions should enhance our future prospects, not only for better returns but also to provide a broader, more effective and comprehensive service to our clients and producers.

FINANCIAL PRODUCTS & SERVICES

Q. What is your strategy for Financial Products and Services?

ROBERT R. LUSARDI, Chief Executive, Financial Products and Services: We have positioned this segment of our business to capitalize on the convergence activities taking place between the financial services and insurance industries. Our goal is to create a broad-based stream of earnings for the Company uncorrelated with property-casualty results. In addition, through our hiring of qualified professionals we expect to develop the intellectual capital and skills necessary to lead in the convergence of the insurance and financial services markets.

Q. What are the key components of your business?

LUSARDI: There are essentially four pieces to the Financial Products and Services unit: financial guaranty; capital markets/hedging; strategic investments and asset accumulation; and long duration liabilities including structured products, and wholesale life insurance transactions.

Q. Explain what you are doing in financial guaranty. How does this relate to other areas at XL?

LUSARDI: In financial guaranty, we have two companies providing insurance and reinsurance to this market. Our two companies, XL Capital Assurance, which is a monoline insurer based in New York, and XL Financial Assurance, a reinsurer located in Bermuda, recently attained AAA ratings from Standard & Poor's and Fitch allowing us to offer the highest quality credit enhancement products.

Our focus to date has been on enhancing credits for the asset backed structured finance and the structured single risk areas. Examples of the former include pools of assets such as loans, credit card receivables, and auto loans. XL has targeted essential infrastructure projects such as toll roads, airports, water facilities and also selected future flow transactions. In addition, we have maintained our strategic reinsurance relationship with FSA since its acquisition by Dexia, whereby each partner continues to be a minority shareholder in each others' Bermuda-based financial guaranty company.

In the financial guaranty business, XL is bearing risks for extended durations, currently averaging 5 years with certain exposures in excess of 20 years. Underwriting these risks requires specialized credit, structuring, and surveillance skills necessary to minimize losses.

XL is also using these specialized skills in the continuing development of XL Financial Solutions, a joint venture between XL's three operating businesses, whereby we structure integrated insurance and capital markets solutions to meet corporate client needs. Many of the solutions tailored may not involve risk transfer in the traditional sense. The Company often records these as deposit liabilities and our investment management skills become particularly important.

Since it is critical to attempt to "match fund" these long duration liabilities, XL has focused on building our capabilities in the asset management area where we have aligned ourselves with a number of very successful investment managers. We believe this enables XL to access intellectual capital through minority ownership stakes in specialized investment disciplines for the benefit of both XL and our increasingly sophisticated client base.

Q. What is your strategy for the capital markets and how does "insurance" fit?

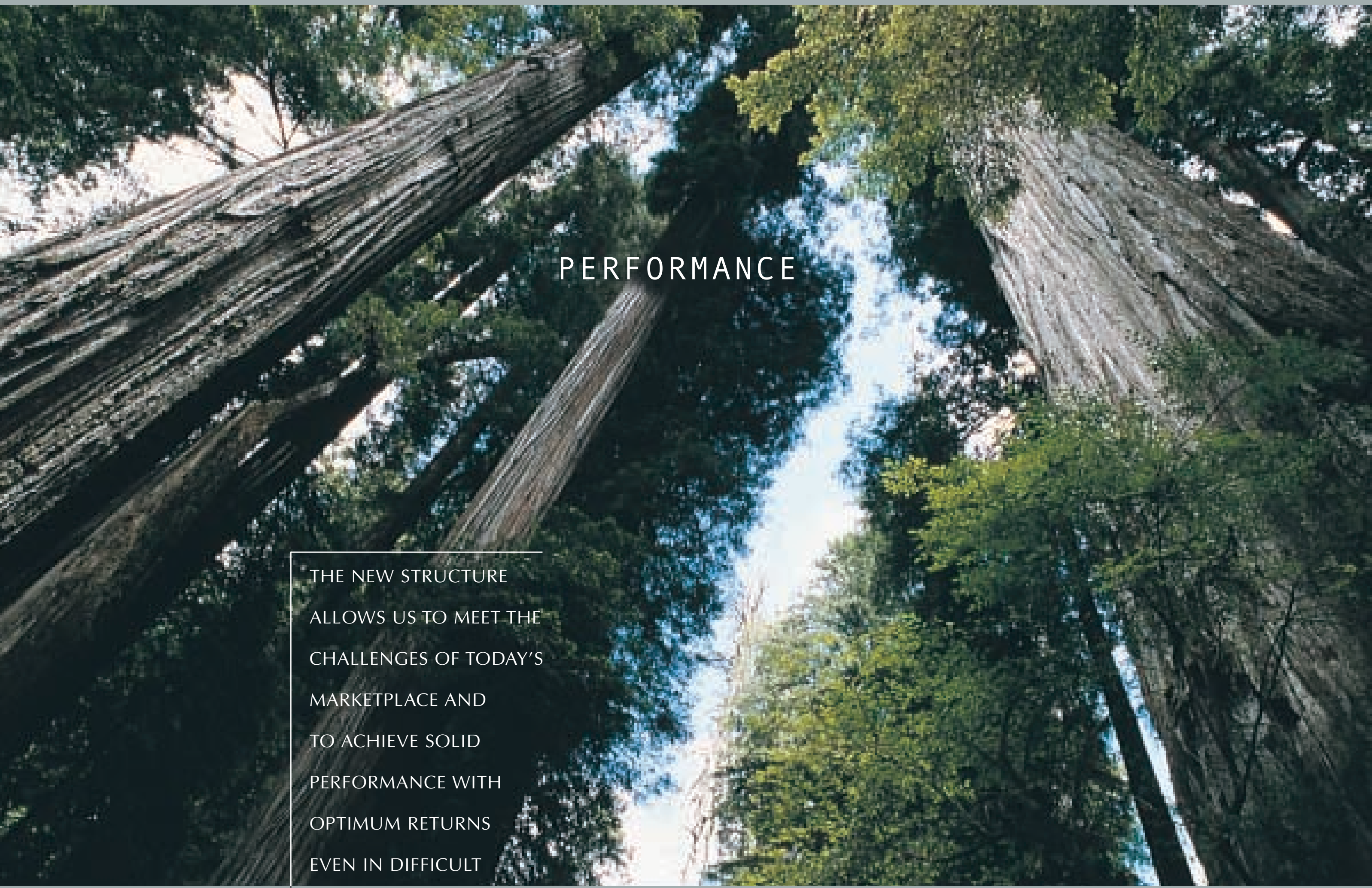
LUSARDI: At this stage, XL is trying to develop products that combine insurance and capital markets risks rather than pure financial products. Examples include financial guaranty, which essentially insures bond issues, Reeve Court, which provides life insurance to high net worth individuals and other life products with significant investment features, and our most recent initiative, Element Re, which was formed to take products traditionally in the capital markets and offer them in insurance form, while continuing to hedge the risks through the capital markets. Element Re's two initial products are weather-related insurance and pulp and paper price protection.

Q. Expand on your initiatives in asset accumulation.

LUSARDI: One of our goals as a Company is to increase the ratio of invested assets to capital, thereby increasing XL's investment income per equity dollar. Long duration liabilities, such as financial guaranty, sophisticated risk solutions through XL Financial Solutions, and selected life insurance transactions are particularly attractive in this regard, since we "accumulate" and hold the associated long duration assets while compounding our return.

During 2000, we increased our long duration assets to over $1.25 billion and originated in excess of $200 million in financial guaranty adjusted gross premium. In 2001, we will also focus on our life insurance and reinsurance initiatives.

A common thread in our financial activities is to match our capabilities in managing these long duration liabilities with the skills needed to deliver long-term investment returns.



PERFORMANCE

THE NEW STRUCTURE ALLOWS US TO MEET THE CHALLENGES OF TODAY'S MARKETPLACE AND TO ACHIEVE SOLID PERFORMANCE WITH OPTIMUM RETURNS EVEN IN DIFFICULT MARKET CONDITIONS. BY CAREFULLY CONTROLLING THE GROWTH OF OUR REINSURANCE SEGMENT WE HAVE PUT IN PLACE THE STRATEGIC ELEMENTS NECESSARY TO TAKE ADVANTAGE OF AN IMPROVING BUSINESS CLIMATE.

Controlled growth

Bonsai is an ancient art. Each tree is the product of carefully controlled growth.

XL's total return investment strategy is increasingly being provided by our investment affiliates, whereby XL not only earns investment returns but also shares in a portion of their management and incentive fees, which XL earns as "Equity in Earnings of Affiliates". We believe this will be quite important to XL in the future and we are creating a separate unit to centralize our skills in this area, led by Chris Greetham.

Q. Can you provide examples of XL's "Affiliates"?

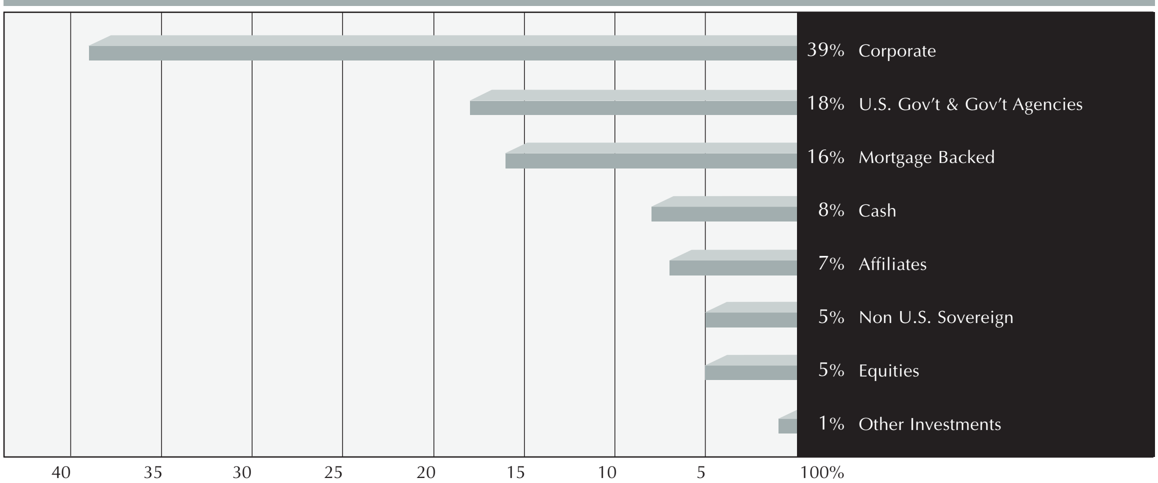
LUSARDI: XL's "affiliates" can be broken down into two basic categories, insurance affiliates and investment affiliates:

Insurance/Reinsurance	Investment
Annuity & Life Re	Agora
FSA International	Highfields
Le Mans Re	MKP
	Pareto Partners
	Prime Advisors
	Venturion

Q. What were the key accomplishments of the Financial Products and Services unit this year?

LUSARDI: All of the Financial Products and Services units at XL were started from scratch and were profitable by the end of their first year, which is a particular achievement in financial businesses. Each unit has a Chief Operating Officer responsible for their day to day activities. Particular credit should go to David Stevens who has led our very successful efforts in the financial guaranty business. Finally, as mentioned above, we established XL Capital Assurance as a New York-domiciled AAA financial guaranty insurer, the first new AAA insurer in many years. In addition, our Bermuda-based financial guaranty reinsurer, XL Financial Assurance, also received AAA ratings.

Investment Asset Mix (at December 31, 2000)



FINANCIALS

Selected Financial Data

The selected consolidated financial data below is based upon the Company's fiscal year end of December 31. The selected consolidated financial data should be read in conjunction with the consolidated financial statements and the notes thereto presented under Item 8.

	2000	1999	1998	1997	1996
	(U.S. dollars in thousands, except per share amounts and ratios)				
Income Statement Data:					
Net premiums earned	$ 2,035,240	$ 1,750,006	$1,324,291	$1,114,758	$1,038,643
Net investment income	542,500	525,318	417,290	345,115	304,823
Net realized gains on investments	50,571	94,356	211,204	410,658	174,593
Equity in net income of affiliates	74,355	40,907	50,292	64,959	59,084
Fee income and other	14,793	100,400	22,325	—	—
Losses and loss expenses	1,432,559	1,304,304	841,517	738,849	739,058
Acquisition costs, operating expenses and exchange gains and losses	743,067	689,005	436,598	318,107	277,801
Interest expense	32,147	37,378	33,444	29,622	22,322
Amortization of intangible assets	58,597	49,141	26,881	7,403	368
Income before minority interest and income tax expense	451,089	431,159	686,962	841,509	537,594
Net income	506,352	470,509	656,330	809,029	516,471
Per Share Data:					
Net income per share – basic (3)	$ 4.07	$ 3.69	$ 5.86	$ 7.95	$ 4.81
Net income per share – diluted (3)	$ 4.03	$ 3.62	$ 5.68	$ 7.74	$ 4.73
Weighted average shares Outstanding – basic (3)	124,503	127,601	112,034	101,708	107,339
Weighted average shares Outstanding – diluted (3)	125,697	130,304	116,206	105,005	109,908
Cash dividends per share (4)	$ 1.80	$ 1.76	$ 1.64	$ 1.36	$ 0.95
Balance Sheet Data:					
Total investments available for sale	$ 9,501,548	$ 9,122,591	$9,057,892	$6,562,609	$5,647,589
Cash and cash equivalents	930,469	557,749	480,874	383,594	321,140
Investments in affiliates	792,723	479,911	154,668	524,866	414,891
Total assets	16,941,952	15,090,912	13,581,140	9,070,031	7,823,375
Unpaid losses and loss expenses	5,672,062	5,369,402	4,896,643	3,972,376	3,623,334
Notes payable and debt	450,032	410,726	613,873	453,866	323,858
Shareholders' equity	5,573,668	5,577,078	5,612,603	3,195,749	2,637,533
Book value per share	$ 44.58	$ 43.64	$ 43.59	$ 31.55	$ 25.31
Fully diluted book value per share	$ 44.78	$ 43.13	$ 43.20	$ 31.42	$ 25.24
Operating Ratios:					
Loss and loss expense ratio (2)	70.4%	74.5%	63.5%	66.3%	71.2%
Underwriting expense ratio (5)	36.4%	34.3%	30.3%	27.9%	26.2%
Combined ratio (6)	106.8%	108.8%	93.8%	94.2%	97.4%

(1) All prior period information includes the results of NAC as though it had always been a part of the Company.
(2) The loss and loss expense ratio is the calculated by dividing the losses and loss expenses incurred by the net premiums earned.
(3) Net income per share is based on the weighted average number of ordinary shares and ordinary share equivalents outstanding for each period as required by Statement of Financial Accounting Standard No. 128.
(4) Cash dividends per share have not been adjusted for the pooling effect of NAC.

(5) The underwriting expense ratio is the sum of acquisition expenses and operating expenses divided by net premiums earned. Operating expenses relating to the corporate segment and foreign exchange gains and losses have not been included for purposes of calculating the underwriting expense ratio. See Note 3 to the consolidated financial statements for further information.
(6) The combined ratio is the sum of the loss and loss expense ratio and the underwriting expense ratio. A combined ratio of under 100% represents an underwriting profit and over 100% represents an underwriting loss.

Management's Discussion and Analysis of Results of Operations and Financial Condition

The following is a discussion of the Company's results of operations and financial condition. Prior period information presented is the combination of the results formerly presented by XL Capital and NAC, as required for a business combination accounted for by the pooling of interests method, which assumes NAC had always been a part of the Company. See Note 6 to the audited Consolidated Financial Statements for further details.

This ''Management's Discussion and Analysis of Results of Operations and Financial Condition'' contains forward-looking statements which involve inherent risks and uncertainties, including, but not limited to, business, financial and integration risks associated with the Winterthur International acquisition and the risk that the acquisition will not be consummated. Statements that are not historical facts, including statements about the Company's beliefs and expectations, are forward-looking statements. These statements are based upon current plans, estimates and expectations. Actual results may differ materially from those projected in such forward-looking statements, and therefore undue reliance should not be placed on them. See ''–Cautionary Note Regarding Forward-Looking Statements'' for a list of additional factors that could cause actual results to differ materially from those contained in any forward-looking statement.

This discussion and analysis should be read in conjunction with the audited Consolidated Financial Statements and notes thereto presented under Item 8.

Overview

The insurance and reinsurance industry has remained competitive through 2000. The Company has experienced price increases on some of the short-tail business, such as the property and property catastrophe lines as the retrocession markets have become more capacity constrained. While the long tail business, such as the excess casualty lines, have not experienced the equivalent level of price increases, market pressure for rate reduction is no longer as prevalent as in 1999. During 2000, the Company continued to evaluate its product lines for profitability and exited certain lines where pricing remains at unsatisfactory levels.

Results of Operations

The following table presents an after-tax analysis of the Company's net income for the years ended December 31, 2000, 1999 and 1998 (U.S. dollars in thousands, except per share amounts):

	2000	1999	1998
Net income excluding net realized gains on investments	$442,932	$370,809	$457,402
Net realized gains on investments	63,420	99,700	198,928
Net income	$506,352	$470,509	$656,330
Earnings per share – basic	$4.07	$3.69	$5.86
Earnings per share – diluted	$4.03	$3.62	$5.68

Net income increased in 2000 compared to 1999 due to an increase in net investment income, equity in net income of affiliates and exchange gains and losses. This increase was partially offset by an increase in the underwriting loss. In 2000, the Company incurred after-tax charges of $124.6 million, or $0.98 per share, which included certain reserve adjustments together with employee severance charges and other costs associated with the realignment of the Company's operations and the discontinuation of certain business lines. These charges affected the underwriting results across all of the Company's segments, excluding the financial products and services segment. In 1999, the Company incurred losses of $125.0 million after-tax, or $0.97 per share, as a result of two major European windstorms in December 1999. In addition, 1999 includes an increase to reserves of $95.0 million associated with the merger with NAC. These two factors are the primary reason for the decrease in net income excluding realized gains on investments in 1999 as compared to 1998.

Basic and diluted earnings per share increased in 2000 as compared to 1999 due to both an increase in net income and a reduction in the weighted average number of shares outstanding. The decrease in the weighted average number of shares outstanding in 2000 is a result of the Company repurchasing 5.1 million shares during the year. The decrease in the basic and diluted earnings per share in 1999 over 1998 is due to a reduction in net income.

Segments

The Company is organized into three underwriting segments – insurance, reinsurance, and financial products and services – and a corporate segment, which includes the investment operations of the Company. Lloyd's syndicates are included in the insurance segment but are shown separately as the nature of their operations and the market in which the syndicates underwrite is significantly different to the Company's other insurance subsidiaries. See Item 1 and Item 8, Note 3 to the Consolidated Financial Statements for further details.

Insurance Operations – Excluding Lloyd's Syndicates

The following table summarizes the underwriting profit for this segment (U.S. dollars in thousands):

	2000	% change 00 vs 99	1999	% change 99 vs 98	1998
Net premiums earned	$726,506	56.9%	$463,069	12.9%	$410,030
Fee income and other	7,692	1.4%	7,584	(8.0%)	8,244
Losses and loss expenses	502,898	62.7%	309,079	15.4%	267,823
Acquisition costs	117,251	79.5%	65,318	37.0%	47,688
Operating expenses	94,129	32.4%	71,094	43.0%	49,702
Exchange gains	(2,344)	NM	(165)	NM	–
Underwriting profit	$ 22,264	(12.1%)	$ 25,327	(52.3%)	$ 53,061

NM=Not Meaningful

Growth in net premiums earned in 2000 over 1999 is mainly due to new business, primarily environmental liability, written by ECS. ECS contributed approximately $260.0 million in gross premiums written and $110.0 million in net premiums earned in 2000. No premiums were written or earned by ECS in 1999 as ECS only commenced writing business on behalf of the Company with effect from January 1, 2000. Prior to this date, ECS had agency agreements in place with other companies. In addition, XL Aerospace wrote aviation and satellite business totaling $160.0 million in gross premiums written and $60.0 million in net premiums earned. In 1999, this agency wrote this business on behalf of the Lloyd's syndicates, of which the Company's share was approximately $20.0 million in gross premium written and $11.5 million in net premium earned. 2000 also includes approximately $60.0 million in gross premiums written and $25.0 million in net premiums earned of new professional liability business written. Generally, in 2000, premium rates have continued to be negatively affected by increased competition. Some price increases were experienced in 2000 in property lines, which have also contributed to the increase in net premiums earned. However, pricing has remained relatively unchanged on the liability lines of business. Contracts were not renewed where premium rates were not deemed by the Company to be sufficient to cover the risks underwritten.

The increase in net premiums earned in 1999 over 1998 is primarily the result of an increase in the gross premiums written in the primary property, aviation and satellite, marine and other lines of business. Net premiums earned in 1999 also reflect the purchase of Intercargo in May 1999, for which approximately $33.0 million was earned from the date of purchase. Partially offsetting this increase is a decrease in the general liability lines, where there was a reduction in the amount of gross premiums written due to increased competition that caused premium rates to decline.

There was a small increase in the net premiums earned in 1999 over 1998 in the other liability business, which comprises mostly professional lines, despite a decrease in the amount of gross premiums written in 1999 compared to 1998. The increase in net premiums earned is primarily as a result of several tailored programs written in 1998, which are earned over a period greater than one year.

Fee income and other relates to fees relating to the provision of risk management and other services. As the managing agencies write more business on behalf of the Company, fee income from agency fees is expected to decline in future years.

The increases in net losses and loss expenses, acquisition costs and operating expenses are also primarily attributable to the new business generated by ECS and XL Aerospace. These are included in the discussions below as part of the analysis of the Company's underwriting ratios.

The decrease in the underwriting profit in each year in this segment is due to higher loss and loss expense ratios as shown below. The following table presents the ratios for this segment for each of the three years ended December 31:

	2000	1999	1998
Loss and loss expense ratio	69.2%	66.7%	65.4%
Underwriting expense ratio	29.1%	29.5%	23.8%
Combined ratio	98.3%	96.2%	89.2%

The loss and loss expense ratio includes the effects of an intercompany stop loss arrangement in place in 2000 and 1999 with a subsidiary in the reinsurance segment. Losses incurred relating to this arrangement were $33.5 million and $100.0 million in 2000 and 1999, respectively. There was no such arrangement in place in 1998. The purpose of this arrangement is to efficiently manage statutory surplus levels across the Company. The higher losses in 1999 were the result of catastrophic losses that occurred in 1999. Had this arrangement not been in place, the loss and loss expense ratio would have been 64.6% and 45.2% in 2000 and 1999, respectively. The increase in the loss ratio in 2000 over 1999 is due to several factors. In 2000, the Company applied higher loss ratios to certain of its casualty lines written in 2000. These loss ratios have been actuarially estimated and reflect the continued negative impact that competitive market conditions have had on rates for these lines of business written in 2000. There was a reduction of loss reserves in 1999 established on the Company's liability lines due to updated actuarially determined reserve estimates that reflect the favorable development of these lines relating to prior years. Loss reserve adjustments were made in 2000 as discussed previously. Partially offsetting the increases in 2000 are additional reductions in loss reserves relating to liability lines written in prior years.

Excluding the effects of the stop loss arrangement, the loss ratio decreased in 1999 compared to 1998 due to the reduction of liability loss reserves relating to 1998 and prior years. Due to the lack of industry data available, the Company estimates loss reserves based upon its own experience. When the Company commenced writing this type of business in 1986, limited data was available and the Company has made its best estimates for loss reserves for each underwriting year since that time. Over time, the amount of data has increased, providing a larger statistical base for estimating reserves. Redundancies in prior year reserves have occurred where loss experience has developed more favorably than expected. This trend is not necessarily expected to continue.

The net decrease in the underwriting expense ratio in 2000 compared to 1999 is mainly due to the significant increase in net premiums earned year over year and, unlike acquisition costs, operational expenses do not change as a direct cost of net premiums earned. Partially offsetting this decrease is the inclusion of expense charges of $13.9 million relating to employee severance and other costs in 2000 associated with the realignment of operations and the discontinuation of certain business lines. Excluding these costs, the underwriting expense ratio in 2000 would have been 27.2%. The increase in the expense ratio in 1999 over 1998 is due to two factors: changes in the product mix towards U.S. primary business in 1999 which tends to have higher acquisition costs, and the additional operating expenses incurred by the Company in establishing its start up operations in the U.S. and new lines of business.

Insurance Operations – Lloyd's Syndicates

The following table summarizes the underwriting results for the Lloyd's syndicates (U.S. dollars in thousands):

	2000	% change 00 vs 99	1999	% change 99 vs 98	1998
Net premiums earned	$357,824	0.6%	$355,769	131.2%	$153,852
Fee income and other	(6,626)	NM	65,892	NM	14,081
Losses and loss expenses	260,372	(12.5%)	297,595	152.0%	118,111
Acquisition costs	119,870	34.4%	89,195	191.4%	30,614
Operating expenses	28,727	(2.0%)	29,305	90.3%	15,399
Exchange gains	(5,986)	NM	(1,180)	NM	(524)
Underwriting (loss) profit	$ (51,785)	NM	$ 6,746	55.7%	$ 4,333

The small increase in net premiums earned in 2000 over 1999 reflect the growth in business written by XL Brockbank and Denham due principally to an increase in syndicate capacity provided by the Company from approximately 43% to 50% at XL Brockbank and from approximately 43% to 75% at Denham. The Company has increased capacity at Denham to 100% for 2001. Partially offsetting this increase is the reduction in net premiums earned relating to the motor business that was sold effective December 31, 1999. The Company retains the residual liability on this business. In the years ended December 31, 2000 and 1999, net premiums earned on the motor business were $82.8 million and $135.9 million respectively. Net premiums earned relating to the motor business will decline substantially in subsequent years. In addition, net premiums earned were reduced in 2000 relating to additional reinsurance costs recorded by XL Brockbank relating to an outwards stop loss reinsurance policy. Under this policy, additional premiums become payable as losses develop for certain lines of business. Reinsurance costs of $23.3 million, $13.4 million and $7.6 million were incurred for 2000, 1999 and 1998, respectively. Of the cost incurred for 2000, approximately $19.1 million relates to losses on certain business lines that the Company will be exiting as part of the reorganization. Coverage provided by this stop loss reinsurance policy has been significantly reduced for 2001 and while this may reduce reinsurance costs, it exposes XL Brockbank to potentially higher net losses.

The increase in net premiums earned in 1999 compared to 1998 is a result of the acquisition of Brockbank in August 1998. In addition, results for Denham were not significant in 1998.

In 1999, fee income and other primarily relates to the sale by XL Brockbank of its two motor insurance businesses, Admiral and Zenith, resulting in a gain of $40.2 million. In addition, 1999 also included $42.1 million of fees generated from the motor business prior to the sale. No such income was earned in 2000. XL Brockbank's managing agencies may also earn profit commissions and fees from syndicates they manage in order to offset their operating expenses. 1999 included $2.9 million in profit commissions. Due to the loss deterioration in the Lloyd's market, no commissions were earned in 2000, resulting in expenses in excess of fee income in 2000.

Exchange gains in 2000 and 1999 arise from the translation of foreign currency assets and liabilities, primarily from exchange rate movements between U.K sterling and the U.S. dollar in the year.

The following table presents the underwriting ratios:

	2000	1999	1998
Loss and loss expense ratio	72.8%	83.6%	76.8%
Underwriting expense ratio	41.5%	33.3%	29.9%
Combined ratio	114.3%	116.9%	106.7%

The decrease in the loss ratio and increase in the expense ratio in 2000 over 1999 primarily reflects the effect of the sale of the motor business. In 1999, the motor business had a loss ratio of approximately 101.1% and an expense ratio of approximately 21.8%. Other business written by XL Brockbank and Denham typically has lower loss ratios and higher commissions than the motor business. The increase in the expense ratio in 2000 was also due to two other factors (i) the reduction in net premiums earned due to the additional reinsurance costs for the stop loss policy. Excluding the effects of this reinsurance cost, the expense ratio would have been 39.0%, 32.1% and 28.5% for 2000, 1999 and 1998, respectively, and (ii) 2000 includes a charge of $7.5 million for employee severance and other costs associated with the realignment of the Company's operations.

The increase in the loss ratio in 1999 over 1998 is due to reserve increases related to adverse development on the U.K. motor business prior to the sale for which the Company still retains residual liabilities.

Reinsurance Operations

The following table summarizes the underwriting results for this segment (U.S. dollars in thousands):

	2000	% change 00 vs 99	1999	% change 99 vs 98	1998
Net premiums earned	$927,195	1.9%	$ 909,915	19.7%	$760,409
Fee income and other	(2,197)	NM	–		–
Losses and loss expenses	663,173	(4.2%)	692,269	52.0%	455,583
Acquisition costs	247,352	10.2%	224,359	31.2%	171,039
Operating expenses	102,132	0.1%	101,978	17.7%	86,670
Exchange (gains) losses	3,868	NM	1,286	NM	(1,129)
Underwriting (loss) profit	$ (91,527)	16.8%	$(109,977)	NM	$ 48,246

The increase in net premiums earned is mainly a result of an increase in net premiums written across most lines of business. The Company has experienced some premium rate increases in the other property, marine, aviation and satellite lines of business in 2000 over 1999. However, pricing also remained generally unchanged in the international property (excluding property catastrophe) and liability lines of business written by the Company. Partially offsetting this increase in net premiums earned is an increase in reinsurance costs incurred in 2000 over 1999, primarily relating to stop loss reinsurance policies. Under these policies, additional premiums become due once losses exceed certain levels. Additional reinsurance costs of $80.6 million, $20.5 million and $5.5 million were incurred in 2000, 1999 and 1998, respectively, relating to these policies, where reinsurance recoveries have been recorded of $151.8 million, $65.0 million and $25.0 million, respectively, for each of the years.

The increase in net premiums earned in 1999 over 1998 is due to two factors: (i) the acquisition of Mid Ocean in August 1998 which results in only five months of net premiums earned included in 1998 compared to twelve months in 1999, and (ii) increases in gross premiums written and earned in the casualty reinsurance business in 1999 resulting from new business opportunities.

Fee income and other in 2000 relates primarily to non-underwriting costs relating to an outward reinsurance contract that did not exist in 1999 or prior.

Operating expenses increased in 1999 over 1998 due to the acquisition of Mid Ocean.

The following table presents the underwriting ratios for this segment:

	2000	1999	1998
Loss and loss expense ratio	71.5%	76.1%	60.0%
Underwriting expense ratio	37.7%	35.9%	33.9%
Combined ratio	109.2%	112.0%	93.9%

Net losses and loss expenses incurred in the segment reflect a recovery of $33.5 million and $100.0 million respectively, under an intercompany stop loss arrangement. The loss and loss expense ratio in 2000 and 1999 would have been 75.1% and 87.1% respectively, had this arrangement not been in place. Included in net losses incurred in 2000 are loss reserve adjustments as discussed previously. Excluding the effects of the intercompany stop loss agreement, the loss ratio was higher in 1999 compared to both 2000 and 1998 primarily due to a higher amount of catastrophe losses and a reserve adjustment of $95.0 million relating to the merger with NAC. Loss events in 2000, which included an oil refinery loss in Kuwait, several satellite losses and the Singapore Airlines loss, totaled approximately $95.0 million. Catastrophe losses in 1999 included European windstorms, hailstorms in Sydney, tornadoes in Oklahoma and satellite losses totaling approximately $185.0 million. In addition, there was an increase in the loss ratio in 2000 and 1999 in the casualty reinsurance business in accordance with actuarial estimates, caused to a large extent by the deterioration in premium rates. Actuarial assumptions are used to establish initial expected loss ratios employed in the actuarial methodologies from which the reserve for losses and loss expenses is derived. Such loss ratios are periodically adjusted to reflect comparisons with actual claims development, inflation and other considerations.

Property catastrophe business has loss experience that is generally categorized as low frequency but high severity in nature. This may result in volatility in the Company's financial results for any fiscal year or quarter. Property catastrophe losses generally are notified and paid within a short period of time from the covered event.

The increase in the underwriting expense ratio in 2000 compared to 1999 is primarily due to lower net earned premiums in 2000 relating to the additional stop loss reinsurance costs incurred. Excluding the effect of these costs, the underwriting expense ratio would have been 34.7%, 35.1% and 33.6% for 2000, 1999 and 1998, respectively. Underwriting expenses increased in 1999 over 1998 primarily due to an increase in profit commissions payable to cedents of proportional business written by XL Re. Profitability on some contracts written in earlier underwriting years has increased relative to original estimates, with the resulting increases in profit commissions payable.

The Company's casualty business includes a minimal element of asbestos and environmental claims on business written prior to 1986. The Company's reserving process includes a supplemental evaluation of claims liabilities from exposure to asbestos and environmental claims, including related loss adjustment expenses. However, the Company's loss and loss expense reserves for such exposures, net of reinsurance, as of December 31, 2000, 1999, and 1998 is less than 1% of its total reserves. A reconciliation of the Company's gross and net liabilities for such exposures for the three years ending December 31, 2000 is set forth in Note 7 of the Notes to Consolidated Financial Statements.

Financial Products and Services

The following table summarizes the underwriting profit for this segment (U.S. dollars in thousands):

	2000	% change 00 vs 99	1999
Net premiums earned	$ 23,715	11.6%	$ 21,253
Fee income and other	15,924	(40.9%)	26,924
Losses and loss expenses	6,116	14.1%	5,361
Acquisition costs	1,323	(37.2%)	2,108
Operating expenses	29,969	79.8%	16,670
Exchange (gains) losses	–	–	–
Underwriting profit	$ 2,231	(90.7%)	$ 24,038

Financial guaranty premiums are earned over the life of the exposure, which is generally longer than that in the Company's other operating segments. Certain premiums, such as those received on an installment basis are not earned until the premium is reported. The increase in net premiums earned mainly reflects new business written in 2000.

The Company may provide financial guaranties in credit default swap form rather than in insurance form. Premiums received in respect of credit default swaps, net of estimated losses, are included as fee income and earned over the life of the policies. Fee income in 2000 relates primarily to credit default swaps. From time to time, the Company will assist in structuring other financial transactions that may result in fee income. These transactions tend to be irregular in nature.

In late 2000, the Company established operations to provide insurance form coverages that previously were available primarily in capital markets. No premiums were written relating to this business in 2000. The Company intends to hedge these risks as they are assumed.

The following table presents the underwriting ratios for the financial products and services segment:

	2000	1999
Loss and loss expense ratio	25.8%	25.2%
Underwriting expense ratio	131.9%	88.4%
Combined ratio	157.7%	113.6%

The financial guaranty operations write business with an expected loss ratio of approximately 25%. Operating expenses for this segment include expenses associated with the Company's activities in writing financial solutions and in generating deposit liabilities. Revenues associated with these transactions are reflected in investment income, net realized gains on investments and equity earnings in affiliates. Thus, the expense ratio and combined ratio tend to be higher than traditional insurance results. Not all premiums written have related acquisition costs. The calculation of the expense ratio excludes fee income derived from credit default swap transactions. If this income were included, the expense ratio and the combined ratio would have been 81.8% and 107.6% respectively in 2000 and 70.4% and 95.6% respectively in 1999. The high expense ratio continues to reflect the start up nature of this segment.

Investment Activities

The following table illustrates the change in net investment income and net realized gains and losses for each of the three years ended December 31, 2000 (U.S dollars in thousands):

	2000	% change 00 vs 99	1999	% change 99 vs 98	1998
Net investment income	$542,500	3.3%	$525,318	25.9%	$417,290
Net realized investment gains	$ 50,571	NM	$ 94,356	NM	$211,204
Annualized effective yield	5.99%	–	5.85%	–	5.38%

External investment professionals manage the Company's portfolio under the direction of the Company's management.

As at December 31, 2000 and 1999, total investments and cash, net of the payable for investments purchased, were $9.1 billion, respectively. While there was no significant change between the years, 2000 included the reinvestment of investment income and realized gains, and the receipt of assets relating to the loss portfolio transfers discussed further in ''–Financial Condition and Liquidity''. These receipts were offset by the transfer of assets to limited partnerships and affiliate investments, claim payments and the repurchase of the Company's shares. As the Company's long-tail casualty business matures over the next three to five years, it is possible that claims payments may increase due to the additional exposure to events that occurred in prior years but have not yet been paid. Funds available for investment may therefore be reduced as compared to prior years due to such increased claims payments. The Company's fixed income investments (including short-term investments and cash equivalents) at December 31, 2000 represented approximately 86.4% of investments available for sale and were managed by several independent investment managers with different strategies. Of the fixed income securities, approximately 88.9% were investment grade, with 61.1% rated Aa or AA or better by a nationally recognized rating agency.

The net payable for investments purchased relates to timing differences as investments are accounted for on a trade date basis. This increased to $1.4 billion at December 31, 2000 from $0.6 billion at December 31, 1999, primarily due to higher investment in certain mortgage-backed securities where the settlement period is generally longer than most fixed income investments.

The increase in investment income in the years presented is primarily due to an increase in the annualized effective yield on the portfolio as the proportion of fixed maturities held increased compared to the prior year. The Company's investment base includes assets relating to deposit liabilities assumed in 2000 and late 1999. Investment income earned on these assets is reduced by the investment expense created by the accretion of these deposit liabilities. Excluding the assets relating to deposit liabilities, the investment base has declined in 2000 compared to 1999 due to claims payments, repurchase of shares and reallocation of assets to other strategic investmnets. However, investment yields have been higher in 2000 compared to 1999, which together with additional income derived from the asset accumulation business, has resulted in higher net investment income.

Net realized gains in 2000 include a $54.1 million gain on the sale of the Company's investment in FSA Holdings, Inc. However, offsetting this gain, the Company incurred realized capital losses of approximately $66.2 million in certain other investments where the Company determined there to be an other than temporary decline in value of such investments.

Net realized investment gains in 1999 and 1998 reflect the strong performance of the equity market. In 1998, equity gains of $150.0 million were realized as some of the Company's equity managers realized gains where they believed that valuations had reached their targets. However, 1999 equity gains were offset by declining fixed income markets that had been strong throughout most of 1998. Due to declining interest rates combined with widening spreads in the corporate and mortgage markets, the fixed income sector allowed the Company opportunities to increase the yield on its investment in 1999.

Other Revenues and Expenses

The following table sets forth other revenues and expenses of the Company for each of the three years ended December 31, 2000 (U.S. dollars in thousands):

	2000	% change 00 vs 99	1999	% change 99 vs 98	1998
Equity in net income of affiliates	$ 74,355	81.8%	$ 40,907	(18.7)%	$50,292
Foreign exchange gains	55,159	NM	–	–	–
Amortization of intangible assets	58,597	19.2%	49,141	82.8%	26,881
Corporate operating expenses	61,935	(30.4)%	89,037	NM	37,139
Interest expense	32,147	(14.0)%	37,378	11.8%	33,444
Minority interest	1,093	NM	220	NM	749
Income tax	(56,356)	42.4%	(39,570)	NM	29,883

The increase in equity earnings of affiliates in 2000 compared to 1999 is primarily attributable to increased returns on the Company's holdings in investment management companies and the funds managed by those companies, in addition to new affiliate investments made in 2000. 1999 included a loss of $3.6 million relating to Arch Capital (formerly Risk Capital), which was sold in 2000. This loss, together with the inclusion of only seven months of equity earnings from the Company's equity position in Mid Ocean in 1998, contributed to the decrease in equity in net income of affiliates in 1999 compared to 1998.

Foreign exchange gains in 2000 related to the revaluation of a deposit liability denominated in U.K. Sterling. The exchange rate movement on the assets matching this deposit liability is included in accumulated other comprehensive income as those assets are designated as available for sale, and in net realized gains on sale of investments. Effective January 1, 2001, the Company has reorganized its corporate and operational structure for U.K. Sterling asset accumulation business such that future exchange translation adjustments of this nature will be matched against corresponding investment portfolio movements with minimal effect on earnings.

The increase in the amortization of intangible assets in 2000 compared to 1999 primarily related to a full year's charge for ECS and XL Specialty, acquired in the second quarter of 1999. The increase in 1999 over 1998 related to the acquisition of Mid Ocean in 1998, where a full year's goodwill charge was included in 1999.

Corporate operating expenses in 2000 included $5.7 million relating to charges for employee severance and other costs relating to the realignment of Company's operations. 1999 included $45.3 million of charges related to the merger with NAC and 1998 included $17.5 million of charges associated with the merger with Mid Ocean were included in corporate operating expenses. Excluding these charges, the net increase in corporate operating expenses in each of the years presented is due to the increase in the corporate infrastructure necessary to support the growing worldwide operations of the Company.

Decreases in interest expense in 2000 compared to 1999 reflect a reduction in debt carried by the Company through 2000 compared to 1999. The Company extinguished convertible debt assumed in connection with the NAC merger in 1999. In addition, the Company pooled capital with its existing operations as a result of acquisitions in the U.S. in 1999, which facilitated repayment of debt in the third quarter of 1999. This decrease was partially offset by interest expense related to interim borrowings used to finance the repurchase of shares in the year ended December 31, 2000. Increases in interest expense in 1999 compared to 1998 is due to the increase in the average long-term debt outstanding in 1999, which was mainly used to finance the acquisitions of ECS and Intercargo, and the repurchase of shares in both 1999 and 1998.

The change in the income taxes of the Company principally reflects the decline in the profitability of the U.S. operations for each year. Deterioration of the casualty book in 2000 and 1999 resulted in pre-tax net losses for U.S. operations, generating an income tax benefit for both years. See Note 17 to the Consolidated Financial Statements.

Financial Condition and Liquidity

As a holding company, the Company's assets consist primarily of its investments in subsidiaries and the Company's future cash flows depend on the availability of dividends or other statutorily permissible payments from its subsidiaries. The ability to pay such dividends is limited by the applicable laws and regulations of Bermuda, the United States, Ireland and the United Kingdom, including the Society of Lloyd's that are described more fully in Note 18 to Consolidated Financial Statements. No assurance can be given that the Company or its subsidiaries will be permitted to pay dividends in the future. The Company's shareholders' equity at December 31, 2000 was $5.6 billion, of which $3.2 billion was retained earnings.

Certain business written by the Company has loss experience characterized as low frequency and high severity exposures. This may result in volatility in both the Company's results and operational cash flows. However, the Company continues to generate positive cash flow from operating activities.

In 2000, 1999 and 1998, the total amount of net losses paid by the Company was $1.7 billion, $1.1 billion, $0.7 billion, respectively. The increase in 2000 compared to 1999 is due to an increase in the amount of net premiums written by the Company, together with losses paid for the settlement of previously established reserves, particularly catastrophe losses. Paid losses in 2000 also include $74.0 million relating to a commutation payment. The increase in paid losses in 1999 over 1998 is primarily due to the acquisition of Mid Ocean in August 1998. The higher amount of paid claims in 2000 compared to 1999 has contributed to the lower operational cash flow in 2000 as compared to 1999.

The Company establishes reserves to provide for estimated claims, the general expenses of administering the claims adjustment process and for losses incurred but not reported. These reserves are calculated by using actuarial and other reserving techniques to project the estimated ultimate net liability for losses and loss expenses. The Company's reserving practices and the establishment of any particular reserve reflect management's judgment concerning sound financial practice and does not represent any admission of liability with respect to any claims made against the Company's subsidiaries. No assurance can be given that actual claims made and payments related thereto will not be in excess of the amounts reserved.

Inflation can have an effect on the Company in that inflationary factors can increase damage awards and potentially result in larger claims. The Company's underwriting philosophy is to adjust premiums in response to inflation, although this may not always be possible due to competitive pressure. Inflationary factors are considered in determining the premium level on any multi-year policies at the time contracts are written.

In 2000, the Company made the following investments:

(1) The Company exchanged its investment in Arch Capital (formerly known as Risk Capital Holdings), an affiliate, and $3.6 million in cash for Arch Capital's ownership in Latin American Re and 1.4 million shares and 100,000 warrants of Annuity & Life Re. The Company also acquired the remaining shares of Latin American Re owned by that company's management in December 2000.

(2) The Company acquired ECS Re, a subsidiary of ECS Inc, for $21.0 million in cash.

(3) The Company invested a further $177.2 million in affiliates, the majority of which related to investment fund affiliates, and a further $55.9 million in limited partnerships and other investments.

The Company assumed loss portfolio transfers during 2000 and 1999 that are accounted for on a deposit basis. These reserves are included in deposit liabilities and policy benefit reserves with the corresponding assets held in investments available for sale.

In 1999, the Company completed the purchase of Intercargo and ECS for a total of $222.8 million in cash. Both of these transactions are accounted for under the purchase method of accounting, and resulted in goodwill of $159.6 million. These transactions were financed in part through bank borrowings and internal funds.

During 1999, the Company redistributed assets from investments available for sale and cash for the following investments:

(1) The Company made minority investments in Highfields Capital Management LP and MKP Capital Management LP and into the funds they manage totaling $281.2 million.

(2) The Company invested $97.0 million in a joint venture with Les Mutuelles du Mans Assurances Group to form a new French reinsurance company, Le Mans Ré.

(3) The Company invested a further $91.0 million in limited partnerships and other investments.

The Company has had several stock repurchase programs as part of its capital management strategy. In June 1999, the Board of Directors rescinded the Company's share repurchase program in place at that time. On January 9, 2000, the Board of Directors authorized a new program for the repurchase of up to $500.0 million. The new share repurchase program was announced in conjunction with a dividend increase of $0.04 per share per annum. Under the current program, in 2000, the Company purchased 5.1 million shares at a cost of $247.7 million or an average of $48.82 per share.

As at December 31, 2000, the Company had bank, letter of credit and loan facilities available from a variety of sources, including commercial banks, totaling $2.6 billion comprising a 364-day facility, 5-year facilities, notes payable and letter of credit facilities. Debt and notes outstanding at December 31, 2000 were $450.0 million and letters of credit outstanding were $1.1 billion. Letters of credit issued and outstanding, 14% of which were collateralized by the Company's investment portfolio, primarily support U.S. non-admitted business and the Company's Lloyd's capital requirements. Approximately 40% of the letters of credit outstanding were issued in connection with intercompany reinsurance agreements.

During 2000 and 1999, borrowings under these facilities were $250.3 million and $328.7 million, respectively, and repayments under the facilities were $211.0 million and $339.7 million, respectively. The borrowings in 2000 were used as interim funding of share buybacks and were repaid using funds from the equity portfolio. The borrowings in 1999 facilitated the repurchase of shares and the purchase of Intercargo and ECS. In June 1999, the Company converted $100 million 5.25% Convertible Subordinate Debentures due 2002 through the issue of 1.8 million shares out of treasury. The total pre-tax interest expense on notes and debt outstanding during the year ended December 31, 2000 and 1999 was $32.1 million and $37.4 million, respectively. Associated with the Company's bank and loan commitments are various loan covenants with which the Company was in compliance throughout the period. See Note 10 to the Consolidated Financial Statements for further details.

Recent Accounting Pronouncements

See Note 2 to the Consolidated Financial Statements for a discussion on recent accounting pronouncements.

Year 2000 Issues

There was no significant impact of Year 2000 issues on the Company's technology systems. The Company did not experience any significant disruption due to the impact of Year 2000 issues on its service providers.

The Company continues to be subject to risks associated with Year 2000 issues based upon the underwriting exposures that it assumed. All insurance and reinsurance subsidiaries of the Company examined the potential exposure to Year 2000-related risks associated with the coverages that they provided. In some instances, Year 2000-related risks were expressly excluded from or included in certain coverages, and in other instances, coverage in respect of such risks is neither expressly excluded nor included. To the extent that Year 2000-related risks materialize, participants in the property and casualty insurance and reinsurance industry, including the Company, could pay or incur significant claims, losses or defense costs which could have a material adverse effect on the Company's results of operations and financial condition. In view of the apparent lack of significant Year 2000-related losses, the Company does not expect to have substantial exposure to Year 2000-related coverage claims. See generally ''–Cautionary Note Regarding Forward-Looking Statements''.

Quantitative and Qualitative Disclosure of Market Risk

The Company is exposed to potential loss from various market risks, including changes in interest rates and foreign currency exchange rates. The Company manages its market risks based on guidelines established by management. The Company enters into derivatives and other financial instruments for trading purposes, primarily for risk management purposes.

This risk management discussion and the estimated amounts generated from the sensitivity analyses are forward-looking statements of market risk assuming certain adverse market conditions occur. Actual results in the future may differ significantly from these anticipated results due to actual developments in the global financial markets. The results of analysis used by the Company to assess and mitigate risk should not be considered projections of future events of losses. See generally ''—Cautionary Note Regarding Forward-Looking Statements''.

The Company's investment portfolio consists of fixed income and equity securities, denominated in both U.S. and foreign currencies. Accordingly, earnings will be affected by changes in interest rates, equity prices and foreign currency exchange rates.

An immediate 100 basis point adverse shift in the treasury yield curve would result in a decrease in total return of 6.1% or $480.0 million on the Company's fixed income portfolio as of December 31, 2000.

In evaluating the impact of price changes of the equity portfolio, a 10% change in equity prices would affect total return by approximately $55.7 million at December 31, 2000.

The Company has short-term debt and long-term debt outstanding. Interest rates on short-term debt are LIBOR based. Accordingly, any changes in interest rates will affect interest expense.

Foreign Currency Risk Management

The Company uses foreign exchange contracts to manage its exposure to the effects of fluctuating foreign currencies on the value of its foreign currency fixed maturities and equity investments. These contracts are not designated as specific hedges for financial reporting purposes and therefore, realized and unrealized gains and losses on them are recorded in income in the period in which they occur. These contracts generally have maturities of three months or less. In addition, where the Company's investment managers believe potential gains exist in a particular currency, a forward contract may not be entered into. At December 31, 2000, forward foreign exchange contracts with notional principal amounts totaling $111.9 million were outstanding. The fair value of these contracts as at December 31, 2000 was $109.6 million with unrealized losses of $2.3 million. Gains of $28.1 million were realized during the year. Based on this value, a 10% appreciation or depreciation of the U.S. dollar as compared to the level of other currencies under contract at December 31, 2000 would have resulted in approximately $0.4 million and $7.4 million in unrealized losses, respectively.

In addition, the Company also enters into foreign exchange contracts to buy and sell foreign currencies in the course of trading its foreign currency investments. These contracts are not designated as specific hedges, and generally have maturities of two weeks or less. As such, any realized or unrealized gains or losses are recorded in income in the period in which they occur. At December 31, 2000, the Company had $54.9 million of such contracts outstanding, and had recognized $1.5 million in realized and unrealized losses for the year. Based on this value, a 10% appreciation or depreciation of the U.S. dollar as compared to the level of other currencies under contract at December 31, 2000 would have resulted in approximately $6.1 million in unrealized gains and $5.1 million in unrealized losses, respectively.

The Company attempts to hedge directly the foreign currency exposure of a portion of its foreign currency fixed maturity investments using forward foreign exchange contracts that generally have maturities of three months or less, and which are rolled over to provide continuing coverage for as long as the investments are held. Where an investment is sold, the related foreign exchange sale contract is effectively closed by entering into an offsetting purchase contract. At December 31, 2000, the Company had, as hedges, foreign exchange contracts for the sale of $121.0 million and the purchase of $25.7 million of foreign currencies at fixed rates, primarily Euros. The notional value of fixed maturities denominated in foreign currencies that were hedged and held by the Company as at December 31, 2000 was $100.6 million. Based on this value, a 10% appreciation or depreciation of the U.S. dollar as compared to the level of other currencies under contract at December 31, 2000 would have resulted in approximately $12.1 million and $1.1 million in unrealized losses, respectively.

In connection with these foreign exchange contracts directly hedging foreign currency fixed maturity investments, unrealized foreign exchange gains or losses are deferred and included in accumulated other comprehensive income. As at December 31, 2000, unrealized losses amounted to $10.2 million. Realized gains of $14.6 million were recognized in earnings during 2000.

During the year ended December 31, 2000, the Company used foreign exchange contracts to manage its exposure to the effects of fluctuating foreign currencies on the amount of its known claims payable in foreign currencies. These contracts were not designated as specific hedges for financial reporting purposes and therefore, realized and unrealized gains and losses on these contracts were recorded in income in the period in which they occurred. As at December 31, 2000, no contracts were outstanding. A loss of $6.8 million was realized in the year in connection with these contracts.

In 2000, the Company used foreign exchange forward contracts to reduce its exposure to premiums receivable denominated in foreign currencies. The forward contract is closely matched with the receivable maturity date. Both the foreign currency receivable and the offsetting forward contract are marked to market on each balance sheet date, with any gains and losses recognized in the income statement. As at December 31, 2000, the Company had forward contracts outstanding for the sale of $10.0 million of foreign currencies at fixed rates, primarily U.K. Sterling. Losses of $0.1 million were realized during 2000.

The Company attempts to manage the exchange volatility arising on certain administration costs denominated in foreign currencies. Throughout the year, forward contracts are entered into to acquire the foreign currency at an agreed rate in the future. Any gains or losses on the forward contracts are deferred and included as a component of shareholders' equity. As the administration expenses are incurred, the gains and losses are recognized in the income statement. At December 31, 2000, the Company had forward contracts outstanding for the purchase of $12.8 million of Euros and U.K. Sterling at fixed rates. Gains deferred in accumulated other comprehensive income as at December 31, 2000 were insignificant. No gains or losses were realized during the year.

Financial Market Exposure

The Company invests in a synthetic equity portfolio of S&P Index futures with an exposure approximately equal in amount to the market value of underlying assets held in this fund. As at December 31, 2000, the portfolio held $43.7 million in exposure to S&P 500 Index futures and underlying assets of $43.2 million. Based on this value, a 10% increase or decrease in the price of these futures would have resulted in exposure of $48.1 million and $39.3 million, respectively. The value of the futures is updated daily with the change recorded in income as a realized gain or loss. For the year ended December 31, 2000, net realized losses from index futures totaled $0.2 million as a result of the 10.1% decrease in the S&P Index during the twelve-month period.

Derivative investments are also utilized to add value to the portfolio where market inefficiencies are believed to exist and also to adjust the duration of a portfolio of fixed income securities to match the duration of related deposit liabilities. At December 31, 2000, bond and stock index futures outstanding were $40.1 million with underlying investments having a market value of $2.5 billion. A 10% appreciation or depreciation of these derivative instruments at this time would have resulted in unrealized gains and losses of $4.0 million, respectively.

Current Outlook

Most of the property and casualty markets in which the Company operates have seen some improvements in pricing and policy terms and conditions for renewals of contracts the Company has underwritten thus far for 2001. However, the Company believes there will need to be a continuation of these improvements for some time in order for the industry to fully recover from the prolonged competitive downturn that has negatively impacted most companies' results over the past several years.

Cautionary Note Regarding Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 (''PSLRA'') provides a ''safe harbor'' for forward-looking statements. This Form 10-K, the Company's Annual Report to Stockholders, any proxy statement, any Form 10-Q or Form 8-K of the Company or any other written or oral statements made by or on behalf of the Company may include forward-looking statements which reflect the Company's current views with respect to future events and financial performance. Such statements include forward-looking statements both with respect to the Company and the insurance and reinsurance sectors in general (both as to underwriting and investment matters). Statements which include the words ''expect'', ''intend'', ''plan'', ''believe'', ''project'', ''anticipate'', ''will'', and similar statements of a future or forward-looking nature identify forward-looking statements for purposes of the PSLRA or otherwise.

All forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause actual results to differ materially from those indicated in such statements. The Company believes that these factors include, but are not limited to, the following: (i) ineffectiveness or obsolescence of the Company's business strategy due to changes in current or future market conditions; (ii) increased competition on the basis of pricing, capacity, coverage terms or other factors; (iii) greater frequency or severity of claims and loss activity, including as a result of natural or man-made catastrophic events, than the Company's underwriting, reserving or investment practices anticipate based on historical experience or industry data; (iv) developments in the world's financial and capital markets which adversely affect the performance of the Company's investments; (v) changes in regulation or tax laws applicable to the Company, its subsidiaries, brokers or customers; (vi) acceptance of the Company's products and services, including new products and services; (vii) changes in the availability, cost or quality of reinsurance; (viii) changes in the distribution or placement of risks due to increased consolidation of insurance and reinsurance brokers; (ix) the impact of the Year 2000-related issues on the Company's underwriting exposures; (x) loss of key personnel; (xi) the effects of mergers, acquisitions and divestitures, including, without limitation, the Winterthur International acquisition; (xii) changes in rating agency policies or practices; (xiii) changes in accounting policies or practices; and (xiv) changes in general economic conditions, including inflation, foreign currency exchange rates and other factors. The foregoing review of important factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements that are included herein or elsewhere. The Company undertakes no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future developments or otherwise.

Item 8. Financial Statements and Supplementary Data

Index to Consolidated Financial Statements and Related Notes

XL CAPITAL LTD

CONSOLIDATED BALANCE SHEETS
AS AT DECEMBER 31, 2000 AND 1999

(U.S. dollars in thousands, except share amounts)

	2000	1999
ASSETS		
Investments:		
Fixed maturities at fair value (amortized cost: 2000, $8,714,196; 1999, $7,835,919)	$ 8,605,081	$ 7,581,151
Equity securities, at fair value (cost: 2000, $515,440; 1999, $863,020)	557,460	1,136,180
Short-term investments, at fair value (amortized cost: 2000, $347,147; 1999, $405,375)	339,007	405,260
Total investments available for sale	9,501,548	9,122,591
Cash and cash equivalents	930,469	557,749
Investments in affiliates	792,723	479,911
Other investments	177,651	165,613
Accrued investment income	143,235	111,590
Deferred acquisition costs	309,268	275,716
Prepaid reinsurance premiums	391,789	217,314
Premiums receivable	1,119,723	1,126,397
Reinsurance balances receivable	196,002	149,880
Unpaid losses and loss expenses recoverable	1,339,767	831,864
Intangible assets (accumulated amortization: 2000, $177,260; 1999, $118,663)	1,591,108	1,626,946
Deferred tax asset, net	152,168	97,928
Other assets	296,501	327,413
Total assets	$16,941,952	$15,090,912
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities:		
Unpaid losses and loss expenses	$ 5,672,062	$ 5,369,402
Deposit liabilities and policy benefit reserves	1,209,926	837,893
Unearned premiums	1,741,393	1,497,376
Notes payable and debt	450,032	410,726
Reinsurance balances payable	441,900	387,916
Net payable for investments purchased	1,372,476	622,260
Other liabilities	439,433	345,738
Minority interest	41,062	42,523
Total liabilities	$11,368,284	$ 9,513,834
Commitments and Contingencies		
Shareholders' Equity:		
Authorized, 999,990,000 ordinary shares, par value $0.01 Issued and outstanding:		
Class A ordinary shares (2000, 125,020,676; 1999, 124,691,541)	$ 1,250	$ 1,247
Class B ordinary shares (2000, Nil; 1999, 3,115,873)	–	31
Contributed surplus	2,497,416	2,520,136
Accumulated other comprehensive (loss) income	(104,712)	19,311
Deferred compensation	(17,727)	(28,797)
Retained earnings	3,197,441	3,065,150
Total shareholders' equity	$ 5,573,668	$ 5,577,078
Total liabilities and shareholders' equity	$16,941,952	$15,090,912

See accompanying notes to Consolidated Financial Statements

XL CAPITAL LTD

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31, 2000, 1999 AND 1998

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

	2000	1999	1998
Revenues:			
Net premiums earned	$2,035,240	$1,750,006	$1,324,291
Net investment income	542,500	525,318	417,290
Net realized gains on sales of investments	50,571	94,356	211,204
Equity in net income of affiliates	74,355	40,907	50,292
Fee income and other	14,793	100,400	22,325
Total revenues	2,717,459	2,510,987	2,025,402
Expenses:			
Losses and loss expenses	1,432,559	1,304,304	841,517
Acquisition costs	485,796	380,980	249,341
Operating expenses	316,892	308,083	188,910
Exchange gains	(59,621)	(58)	(1,653)
Interest expense	32,147	37,378	33,444
Amortization of intangible assets	58,597	49,141	26,881
Total expenses	2,266,370	2,079,828	1,338,440
Income before minority interest and income tax expense	451,089	431,159	686,962
Minority interest in net income of subsidiary	1,093	220	749
Income tax (benefit) expense	(56,356)	(39,570)	29,883
Net income	$ 506,352	$ 470,509	$ 656,330
Change in net unrealized appreciation of investments	(118,321)	(211,842)	(15,414)
Foreign currency translation adjustments	(5,702)	(4,032)	(872)
Comprehensive Income	$ 382,329	$ 254,635	$ 640,044
Weighted average ordinary shares and ordinary share equivalents outstanding – basic	124,503	127,601	112,034
Weighted average ordinary shares and ordinary share equivalents outstanding – diluted	125,697	130,304	116,206
Earnings per ordinary share and ordinary share equivalent – basic	$ 4.07	$ 3.69	$ 5.86
Earnings per ordinary share and ordinary share equivalent – diluted	$ 4.03	$ 3.62	$ 5.68

See accompanying notes to Consolidated Financial Statements

XL CAPITAL LTD

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2000, 1999 AND 1998

(U.S. dollars in thousands)

	2000	1999	1998
Ordinary Shares:			
Balance-beginning of year	$ 1,278	$ 1,287	$ 1,013
Issue of shares	–	1	15
Issue of shares – Mid Ocean acquisition	–	–	291
Exercise of stock options	23	5	3
Repurchase of treasury shares	(51)	(15)	(35)
Balance-end of year	1,250	1,278	1,287
Contributed Surplus:			
Balance-beginning of year	2,520,136	2,508,062	506,452
Issue of shares	2,652	15,951	101,502
Issue of shares Mid Ocean acquisition	–	–	2,093,426
Exercise of stock options	74,538	11,711	9,147
Repurchase of treasury shares	(99,910)	(15,588)	(202,465)
Balance-end of year	2,497,416	2,520,136	2,508,062
Accumulated other comprehensive (loss) income:			
Balance-beginning of year	19,311	235,185	251,471
Net change in unrealized gains on investment portfolio, net of tax	(112,031)	(213,482)	(10,352)
Net change in unrealized gains on investment portfolio of affiliate	(6,290)	1,640	(5,062)
Currency translation adjustments	(5,702)	(4,032)	(872)
Balance-end of year	(104,712)	19,311	235,185
Deferred Compensation:			
Balance-beginning of year	(28,797)	(22,954)	(18,263)
Forfeit (issue) of restricted shares	1,555	(13,603)	(10,506)
Amortization	9,515	7,760	5,815
Balance-end of year	(17,727)	(28,797)	(22,954)
Retained Earnings:			
Balance-beginning of year	3,065,150	2,891,023	2,455,076
Net income	506,352	470,509	656,330
Cash dividends paid	(225,572)	(212,659)	(156,482)
Repurchase of treasury shares	(148,489)	(83,723)	(63,901)
Balance-end of year	3,197,441	3,065,150	2,891,023
Total shareholders' equity	$5,573,668	$5,577,078	$5,612,603

See accompanying notes to Consolidated Financial Statements

XL CAPITAL LTD

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2000, 1999 AND 1998

(U.S. dollars in thousands)

	2000	1999	1998
Cash flows provided by operating activities:			
Net income	$ 506,352	$ 470,509	$ 656,330
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Net realized gains on sales of investments	(50,571)	(94,356)	(211,204)
Amortization of discounts on fixed maturities	(47,099)	(14,429)	(14,718)
Equity in net income of affiliates	(74,355)	(40,907)	(50,292)
Amortization of deferred compensation	8,861	7,657	5,815
Amortization of intangible assets	58,597	49,141	26,881
Unpaid losses and loss expenses	259,728	411,396	323,857
Unearned premiums	244,017	131,767	52,161
Premiums receivable	6,674	(166,027)	4,245
Unpaid losses and loss expenses recoverable	(506,242)	(212,928)	(221,177)
Prepaid reinsurance premiums	(174,475)	(1,848)	(45,961)
Reinsurance balances receivable	(46,122)	(25,109)	(31,103)
Other	77,086	(25,632)	39,783
Total adjustments	(243,901)	18,725	(121,713)
Net cash provided by operating activities	262,451	489,234	534,617
Cash flows provided by (used in) investing activities:			
Proceeds from sale of fixed maturities and short-term investments	22,287,287	15,664,591	15,765,103
Proceeds from redemption of fixed maturities and short-term investments	460,733	134,565	516,418
Proceeds from sale of equity securities	1,480,853	1,017,177	918,501
Purchases of fixed maturities and short-term investments	(22,798,463)	(16,075,719)	(16,460,877)
Purchases of equity securities	(1,071,351)	(803,728)	(1,020,032)
Deferred (gains) losses on forward contracts	9,388	(509)	(12,163)
Investments in affiliates, net of dividends received	(180,818)	(342,142)	24,193
Acquisition of subsidiaries, net of cash acquired	(3,094)	(173,206)	41,483
Other investments	(55,917)	(120,717)	4,411
Deposit liabilities and policy benefit reserves	372,033	837,893	–
Other assets	(40,564)	(35,133)	13,430
Net cash provided by (used in) investing activities	460,087	103,072	(209,533)
Cash flows provided by (used in) financing activities:			
Issue of shares	–	69	514
Proceeds from exercise of stock options	74,561	14,014	15,092
Repurchase of treasury shares	(248,450)	(99,344)	(266,401)
Dividends paid	(225,572)	(212,659)	(156,481)
Proceeds from loans	250,300	328,700	655,000
Repayment of notes	–	(100,000)	–
Repayment of loans	(211,000)	(339,735)	(495,000)
Repayment of debentures	–	(101,737)	–
Minority interest	10,892	(4,900)	19,988
Net cash used in financing activities	(349,269)	(515,592)	(227,288)
Effects of exchange rate changes on foreign currency cash	(549)	161	(516)
Increase in cash and cash equivalents	372,720	76,875	97,280
Cash and cash equivalents – beginning of year	$ 557,749	$ 480,874	$ 383,594
Cash and cash equivalents – end of year	$ 930,469	$ 557,749	$ 480,874
Net taxes received (paid)	$ 13,347	$ (30,246)	$ (31,200)
Interest paid	$ (30,505)	$ (28,268)	$ (32,800)

See accompanying notes to Consolidated Financial Statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Years Ended December 31 2000, 1999 and 1998
(U.S. dollars in thousands, except per share amounts)

1. History

XL Capital Ltd (sometimes referred to as the ''Company'') is a holding company organized under the laws of the Cayman Islands. XL was incorporated on March 16, 1998, as the successor to EXEL Limited, a Cayman Islands corporation organized in 1986, in connection with EXEL's merger with Mid Ocean Limited, a Cayman Islands corporation. The merger was accounted for as a purchase under U.S. generally accepted accounting principles (''GAAP'') and as such, results of operations of Mid Ocean are included from August 1, 1998, the effective date of the merger. In the merger, all of the shares of EXEL and Mid Ocean were exchanged for shares in the Company according to two schemes of arrangement under Cayman Islands law. The Company operated under the name ''EXEL Limited'' from completion of the merger until February 1, 1999 when its current name was approved by the requisite vote of the Company's shareholders. References herein to XL Capital or the Company also shall include EXEL unless the context otherwise requires. The Company is a leading provider of insurance and reinsurance, including coverages relating to certain financial risks, to industrial, commercial and professional service firms, insurance companies and other enterprises on a worldwide basis.

In 1999, XL Capital merged with NAC Re Corp, a Delaware corporation. The merger has been accounted for as a ''pooling of interests'' under U.S. GAAP. Under pooling of interests accounting, it is assumed that XL Capital and NAC have been merged from the date of incorporation of the Company, and accordingly, all prior period information contained in these financial statements includes the results of NAC. NAC was organized in 1985 and, through its subsidiaries, writes property and casualty insurance and reinsurance in the U.S., Canada and Europe. Subsequent to the merger agreement, XL Capital amended its financial year from November 30 to December 31 as a conforming pooling adjustment and to facilitate year end reporting for its subsidiaries.

XL Insurance, a company organized under the laws of Bermuda, was formed in 1986 in response to a shortage of high excess liability coverage for Fortune 500 companies in the U.S. In 1990, XL Insurance formed XL Europe, an insurance company organized under the laws of Ireland to serve European clients and, in 1998, formed two companies now known as XL Insurance Company of New York and XL Capital Assurance.

XL Re, formerly XL Mid Ocean Re, is organized under the laws of Bermuda. On August 7, 1998, XL Mid Ocean Re was formed through the merger of XL Global Reinsurance and Mid Ocean Re. Mid Ocean Re and Global Capital Re were organized in 1992 and 1993, respectively, initially to write property catastrophe reinsurance following a reduction in market capacity due to the effects of severe hurricanes that struck the southeastern United States in the late 1980's and early 1990's.

The Company further expanded into the U.S. in 1999 by completing the acquisition of both Intercargo Corporation and ECS, Inc. Intercargo, renamed XL Specialty, underwrites specialty insurance products for companies engaged in international trade, including U.S. Customs bonds and marine cargo insurance. ECS is an underwriting manager, which specializes in environmental insurance coverages and risk management services.

XL Brockbank, formerly Brockbank, was acquired through the merger with Mid Ocean. XL Brockbank is organized under the laws of the United Kingdom and is a leading Lloyd's managing agency that provides underwriting and similar services to five Lloyd's syndicates. Two of these syndicates are dedicated corporate syndicates whose capital is provided solely by the Company. The two corporate syndicates, which commenced operations on January 1, 1996, underwrite property, marine and energy, aviation, satellite, professional indemnity and other specialty lines of insurance and reinsurance to a global client base. As a managing agency, XL Brockbank may receive fees and commissions in respect of underwriting services it provides to the non-related syndicates. In the fourth quarter of 1999, XL Brockbank sold its two motor insurance businesses, Admiral and Zenith.

1. History (Continued)

Denham Syndicate Management Limited was acquired in 1998 and it also provides underwriting and similar services to one corporate syndicate, whose capital is partially provided by the Company. This syndicate writes a specialized book of international business, concentrating on long-tail casualty and non-marine physical damage.

The Company has pursued a strategy of entering into ventures with other organizations that possess expertise in lines of business that the Company wishes to write. These ventures are considered to be of strategic importance. The Company's principal ventures are in the areas of financial guaranty insurance, life insurance for high net worth individuals, political risk insurance and currency and related risk management. In July 1999, the Company entered into a venture with Les Mutuelles du Mans Assurances Group to form a new French reinsurance company, Le Mans Ré. The Company owns a 49% shareholding in the new company, which underwrites a worldwide portfolio comprising most classes of property and casualty reinsurance business together with a selective portfolio of life reinsurance business.

In 1999, the Company made strategic minority investments in two investment management firms. The Company acquired minority investments in Highfields Capital Management L.P., a global equity investment firm, and MKP Capital Management, a New York-based fixed income investment manager specializing in mortgage-backed securities.

In 1998, the Company entered into a venture with FSA Holdings Ltd to write financial guaranty insurance and reinsurance. Under the terms of the venture, each of the Company and FSA formed a Bermuda insurance company in which it is the majority shareholder and made a minority investment in the company formed by its co-venturer.

The Company formed Reeve Court Insurance, a Bermuda company organized as a venture with such company's management for the purpose of providing life insurance to high net worth individuals in 1998.

In 1997, the Company acquired a 75% holding in Latin American Re, a Bermuda reinsurance company. The remaining minority interest was purchased in 2000.

The Company formed Sovereign Risk Insurance as a joint venture in 1997. Sovereign is a Bermuda-based managing general agency that writes political risk insurance on a subscription basis on behalf of its shareholders.

In 1996, the Company acquired approximately 30% of Pareto Partners, a firm that specializes in foreign currency management and related services.

2. Significant Accounting Policies

(a) Basis of Preparation

These consolidated financial statements include the accounts of the Company and all of its subsidiaries and have been prepared in accordance with U.S. generally accepted accounting principles (''GAAP''). They include the merger with NAC, which occurred in June 1999, and which has been accounted for as a ''pooling of interests'' under U.S. GAAP. They are based upon the Company's fiscal year end of December 31. Results of operations, statements of position and cash flows include NAC as though it had always been a part of the Company. All significant intercompany accounts and transactions have been eliminated. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amount 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 those estimates.

(b) Premiums and Acquisition Costs

Premiums written are recorded in accordance with the terms of the underlying policies. Reinsurance premiums assumed are estimated based upon information received from ceding companies and any subsequent differences arising on such estimates are recorded in the period they are determined. Financial guaranty installment premiums are recorded as premiums written when reported. Premiums are earned on a monthly pro-rata basis over the period the coverage is provided. Financial guaranty insurance premiums are earned over the life of the exposure. Unearned premiums represent the portion of premiums written which is applicable to the unexpired terms of policies in force. Premiums written and unearned premiums are presented after deductions for reinsurance ceded to other insurance companies.

Acquisition costs, which vary with and are related to the acquisition of policies, primarily commissions paid to brokers, are deferred and amortized over the period the premiums are earned. Future earned premiums, the anticipated losses and other costs, together with investment income related to those premiums are also considered in determining the level of acquisition costs to be deferred.

(c) Reinsurance

In the normal course of business, the Company seeks to reduce the loss that may arise from events that could cause unfavorable underwriting results by reinsuring certain levels of risk in various areas of exposure with other insurance enterprises or reinsurers. Reinsurance premiums ceded are expensed and the commissions recorded thereon are earned on a monthly pro-rata basis over the period the reinsurance coverage is provided. Prepaid reinsurance premiums represent the portion of premiums ceded that is applicable to the unexpired term of policies in force. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policy. Provision is made for estimated unrecoverable reinsurance.

(d) Fee Income and Other

Fee income and other includes fees earned for services, together with premiums, net of loss reserve estimates, on credit default swaps. The Company recognizes fee income over the estimated performance or risk period of the related services provided. Any adjustments to those estimated periods any cumulative adjustments resulting therefrom are reflected in income in the year in which the adjustment is made.

2. Significant Accounting Policies (Continued)

(e) Investments

Investments are considered available for sale and are carried at fair value. The fair value of investments is based upon quoted market values where available or by reference to broker or underwriter bid indications. The net unrealized appreciation or depreciation on investments, net of tax, is included in accumulated other comprehensive income. Any unrealized depreciation in value considered by management to be other than temporary is charged to income in the period that it is determined.

Short-term investments comprise investments with a maturity equal to or greater than 90 days but less than one year. Equity securities include investments in open end mutual funds. All investment transactions are recorded on a trade date basis. Realized gains and losses on sales of equities and fixed income investments are determined on the basis of average cost and amortized cost, respectively. Investment income is recognized when earned and includes interest and dividend income together with the amortization of premium and discount on fixed maturities and short-term investments.

Financial futures and forward currency contracts are carried at fair value, with the corresponding realized or unrealized gain or loss included in income, except in the instance of forward foreign currency contracts that are used to hedge currency risks on specific investments. Gains and losses from these contracts are deferred and included in accumulated other comprehensive income until the corresponding investment asset is sold.

(f) Cash Equivalents

Cash equivalents include fixed interest deposits placed with a maturity of under 90 days when purchased.

(g) Foreign Currency Translation

Assets and liabilities of foreign operations whose functional currency is other than the U.S. dollar are translated at year end exchange rates. Revenue and expenses of such foreign operations are translated at average exchange rates during the year. The effect of the translation adjustments for foreign operations, net of applicable deferred income taxes, is included in accumulated other comprehensive income.

Other monetary assets and liabilities denominated in foreign currencies are translated at the exchange rate in effect at the balance sheet date with the resulting foreign exchange gains and losses recognized in income, unless the foreign currency exposure is directly hedged as discussed above. Revenue and expense transactions are translated at the average exchange rates prevailing during the year.

(h) Investments in Affiliates

Investments in which the Company has significant influence over the operations are classified as affiliates and are carried under the equity method of accounting. Under this method, the Company records its proportionate share of income or loss from such investments in its results of operations.

(i) Other Investments

The Company accounts for its other investments, including investments in limited partnerships, on a cost basis as it has no significant influence over these entities. Investments are written down to their realizable value where management considers there is an other than temporary decline in value. Income is recorded when received.

2. Significant Accounting Policies (Continued)

(j) Amortization of Intangible Assets

Intangible assets represent goodwill recorded in connection with the Company's business combinations and are amortized on a straight-line basis over the expected life of the related operations acquired, not exceeding 40 years. The Company evaluates the recoverability of its intangible assets whenever changes in circumstances warrant. If it is determined that an impairment exists, the excess of the unamortized balance over the fair value of the intangible asset will be charged to earnings at that time.

(k) Losses and Loss Expenses

Unpaid losses and loss expenses includes reserves for unpaid reported losses and loss expenses and for losses incurred but not reported. The reserve for unpaid reported losses and loss expenses is established by management based on amounts reported from insureds or ceding companies and consultation with independent legal counsel, and represents the estimated ultimate cost of events or conditions that have been reported to or specifically identified by the Company.

The Company recognizes as a component of loss reserves, the loss experience accounts of policyholders for policies written on a multi-year basis where experience accounts are a percentage of premiums net of related losses paid. Interest expense on the experience accounts is charged to investment income. In the event the insured cancels the policy, the return of the experience account is treated as a return premium if there has been no loss notification.

The reserve for losses incurred but not reported has been estimated by management in consultation with independent actuaries and is based on loss development patterns determined by reference to the Company's underwriting practices, the policy form and the experience of the relevant industries.

Certain workers' compensation reserves are considered fixed and determinable and are subject to tabular reserving. Such tabular reserves are discounted using an interest rate of 7%.

Management believes that the reserves for unpaid losses and loss expenses are sufficient to pay losses that fall within coverages assumed by the Company. However, there can be no assurance that losses will not exceed the Company's total reserves. The methodology of estimating loss reserves is periodically reviewed to ensure that the assumptions made continue to be appropriate and any adjustments resulting therefrom are reflected in income of the year in which the adjustments are made.

(l) Deposit Liabilities and Policy Benefit Reserves

Short duration contracts entered into by the Company which are not deemed to transfer significant underwriting and/or timing risk are accounted for as deposits, whereby liabilities are initially recorded at the same amount as assets received. An initial accretion rate is established based on actuarial estimates whereby the deposit liability is increased to the estimated amount payable over the term of the contract. This accretion charge is presented in the period as either interest income where the contract does not transfer underwriting risk, or net losses and loss expenses incurred where the contract does not transfer significant timing risk. Policy benefit reserves relate to long duration contracts written by the Company which do not transfer significant mortality or morbidity risks, and are also accounted for as deposits.

The Company will periodically re-assess the amount of deposit liabilities and policy benefit reserves. Any changes to the estimated ultimate liability will be reflected as an adjustment to earnings to reflect the cumulative effect to date of the period the contract has been in force and by an adjustment to the future accretion rate of the liability over the remaining estimated contract term.

2. Significant Accounting Policies (Continued)

(m) Income Taxes

The Company utilizes the asset and liability method of accounting for income taxes. Under this method, deferred income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. A valuation allowance is established for any portion of a deferred tax asset that management believes will not be realized.

(n) Stock Plans

The Company accounts for stock compensation plans in accordance with Accounting Principles Board (''APB'') Opinion No. 25, ''Accounting for Stock Issued to Employees''. Accordingly, compensation expense for stock option grants and stock appreciation rights is recognized to the extent that the fair value of the stock exceeds the exercise price of the option at the measurement date.

(o) Per Share Data

Basic earnings per share is based on weighted average common shares outstanding and excludes any dilutive effects of options and convertible securities. Diluted earnings per share assumes the conversion of dilutive convertible securities and the exercise of all dilutive stock options.

(p) Fair Value of Financial Instruments

Fair value of certain assets and liabilities are based on published market values, if available, or estimates of fair value of similar issues. Fair values are reported in Notes 4 and 10.

(q) Recent Accounting Pronouncements

The Financial Accounting Standards Board issued Statement No. 133, ''Accounting for Derivative Instruments and Hedging Activities,'' (FAS 133) in June 1998. FAS 133 establishes accounting and reporting standards for derivative instruments embedded in other contracts (collectively referred to as derivatives), and for hedging activity. It requires an entity to recognize all derivatives as either assets or liabilities in the balance sheet and measure those instruments at fair value. The Company will adopt FAS 133, as amended, as of January 1, 2001. Credit default swaps issued by the Company meet the definition of a derivative under FAS 133. From January 1, 2001 the Company will record these products at fair value, with the fair value adjustment being recorded in earnings in each period. The level of such adjustments will be dependent upon a number of factors including changes in interest rates, credit spreads and other market factors.

The Company has established a committee and completed an implementation plan to identify all derivatives, evaluate risk management hedging strategies and determine appropriate valuation methodologies in order to assess the impact that adoption of this statement will have on its financial position and results of operation. Based on the Company's current accounting treatment for derivatives and as a result of its review, the Company has estimated that FAS 133, as amended, will not have a significant impact on the results of operations, financial condition or liquidity in future periods.

3. Segment Information

The Company is organized into three underwriting segments – insurance, reinsurance, and financial products and services – in addition to a corporate segment that includes the investment operations of the Company. Lloyd's syndicates are part of the insurance segment but are described separately as the nature of the business written and

3. Segment Information (Continued)

the market in which the Lloyd's syndicates underwrite are significantly different to the Company's other insurance subsidiaries. Certain business written by the Company has loss experience characterized as low frequency and high severity. This may result in volatility in both the Company's results and operational cash flows.

Insurance Operations – excluding Lloyd's Syndicates

Insurance business written includes general liability, other liability including directors and officers, professional and employment practices liability, environmental liability, property, program business, marine, aviation, satellite and other product lines including U.S. Customs bonds, surety, political risk and specialty lines.

Insurance Operations – Lloyd's Syndicates

The Lloyd's syndicates write property, marine and energy, aviation and satellite, professional indemnity, liability coverage and other specialty lines, primarily of insurance but also reinsurance.

Reinsurance Operations

Reinsurance business written includes treaty and facultative reinsurance to primary insurers of casualty risks, principally: general liability; professional liability; automobile and workers' compensation; commercial and personal property risks; specialty risks including fidelity and surety and ocean marine; property catastrophe; property excess of loss; property pro-rata; marine and energy; aviation and satellite; and various other reinsurance to insurers on a worldwide basis. The Company endeavors to manage its exposures to catastrophic events by limiting the amount of its exposure in each geographic zone worldwide and requires that its property catastrophe contracts provide for aggregate limits and varying attachment points.

Financial Products and Services

Financial products and services business written includes insurance and reinsurance solutions for complex financial risks. These include financial guaranty insurance and reinsurance, credit enhancement swaps and other collateralized transactions. While each of these is unique and is tailored for the specific needs of the insured, they are typically multi-year policies. Due to the nature of these types of policies, premium volume as well as profit margin can vary significantly from period to period. The Company has approached this market on a ''net-line'' basis, but may cede a portion of some risks to third parties from time to time. In 1999, the Company began assuming large loss portfolios as part of its new asset accumulation strategy.

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

3. Segment Information (Continued)

The Company evaluates performance of each segment based on underwriting profit or loss. Other items of revenue and expenditure of the Company are not evaluated at the segment level. In addition, management does not allocate assets by segment. The following is an analysis of the underwriting profit or loss by segment together with a reconciliation of underwriting profit or loss to net income:

Year ended December 31, 2000	Insurance	Lloyd's Syndicates	Reinsurance	Financial Services	Total
Net premiums earned	$726,506	$357,824	$927,195	$ 23,715	$2,035,240
Fee income and other	7,692	(6,626)	(2,197)	15,924	14,793
Net losses and loss expenses (2).	502,898	260,372	663,173	6,116	1,432,559
Acquisition costs	117,251	119,870	247,352	1,323	485,796
Operating expenses (3)	94,129	28,727	102,132	29,969	254,957
Exchange (gains) and losses	(2,344)	(5,986)	3,868	–	(4,462)
Underwriting profit (loss)	$ 22,264	$ (51,785)	$ (91,527)	$ 2,231	$ (118,817)
Net investment income					542,500
Net realized gains on investments					50,571
Equity in net earnings of affiliates					74,355
Interest expense					32,147
Amortization of intangible assets					58,597
Corporate operating expenses (3)					61,935
Other exchange gain					55,159
Minority interest					1,093
Income tax benefit					56,356
Net income					$ 506,352
Loss and loss expense ratio	69.2%	72.8%	71.5%	25.8%	70.4%
Underwriting expense ratio	29.1%	41.5%	37.7%	131.9%	36.4%
Combined ratio	98.3%	114.3%	109.2%	157.7%	106.8%

(1) Ratios are based on net premiums earned, excluding fee income and other. The underwriting expense ratio excludes exchange gains and losses.

(2) Net losses and loss expenses for the insurance segment include, and the reinsurance segment exclude, $33.5 million relating to an intercompany stop loss arrangement. Total results are not affected. The loss and loss expense ratio would have been 64.6% and 75.1% and the underwriting results would have been a profit of $55.8 million and a loss of $125.0 million in the insurance and reinsurance segments, respectively, had this stop loss arrangement not been in place.

(3) Operating expenses exclude corporate operating expenses, shown separately.

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

3. Segment Information (Continued)

Year ended December 31, 1999	Insurance	Lloyd's Syndicates	Reinsurance	Financial Services	Total
Net premiums earned	$463,069	$355,769	$ 909,915	$ 21,253	$1,750,006
Fee income and other	7,584	65,892	–	26,924	100,400
Net losses and loss expenses (2)	309,079	297,595	692,269	5,361	1,304,304
Acquisition costs	65,318	89,195	224,359	2,108	380,980
Operating expenses (3)	71,094	29,305	101,978	16,670	219,047
Exchange (gains) and losses	(165)	(1,180)	1,286	–	(59)
Underwriting profit (loss)	$ 25,327	$ 6,746	$(109,977)	$ 24,038	$ (53,866)
Net investment income					525,318
Net realized gains on investments					94,356
Equity in net earnings of affiliates					40,907
Interest expense					37,378
Amortization of intangible assets					49,141
Corporate operating expenses (4)					89,037
Minority interest					220
Income tax benefit					(39,570)
Net income					$ 470,509
Loss and loss expense ratio	66.7%	83.6%	76.1%	25.2%	74.5%
Underwriting expense ratio	29.5%	33.3%	35.9%	88.4%	34.3%
Combined ratio	96.2%	116.9%	112.0%	113.6%	108.8%

(1) Ratios are based on net premiums earned, excluding fee income and other. The underwriting expense ratio excludes exchange gains and losses.

(2) Net losses and loss expenses for the insurance segment include, and the reinsurance segment exclude, $100.0 million relating to an intercompany stop loss arrangement. Total results are not affected. The loss and loss expense ratio would have been 45.2% and 87.1% and the underwriting results would have been a profit of $125.3 million and a loss of $210.0 million in the insurance and reinsurance segments, respectively, had this stop loss arrangement not been in place.

(3) Operating expenses exclude corporate operating expenses, shown separately.

(4) Corporate operating expenses include one-time charges of $45.3 million related to the merger with NAC.

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

3. Segment Information (Continued)

Year ended December 31, 1998	Insurance	Lloyd's Syndicates	Reinsurance	Financial Services	Total
Net premiums earned	$410,030	$153,852	$760,409	$ –	$1,324,291
Fee income and other	8,244	14,081	–	–	22,325
Net losses and loss expenses	267,823	118,111	455,583	–	841,517
Acquisition costs	47,688	30,614	171,039	–	249,341
Operating expenses (2)	49,702	15,399	86,670	–	151,771
Exchange gains	–	(524)	(1,129)	–	(1,653)
Underwriting profit (loss)	$ 53,061	$ 4,333	$ 48,246	$ –	$ 105,640
Net investment income					417,290
Net realized gains on investments					211,204
Equity in net earnings of affiliates					50,292
Interest expense					33,444
Amortization of intangible assets					26,881
Corporate operating expenses (3)					37,139
Minority interest					749
Income tax expense					29,883
Net income					$ 656,330
Loss and loss expense ratio	65.4%	76.8%	60.0%	N/A	63.5%
Underwriting expense ratio	23.8%	29.9%	33.9%	N/A	30.3%
Combined ratio	89.2%	106.7%	93.9%	N/A	93.8%

(1) Ratios are based on net premiums earned, excluding fee income and other. The underwriting expense ratio excludes exchange gains and losses

(2) Operating expenses exclude corporate operating expenses, shown separately.

(3) Corporate operating expenses include one-time charges of $17.5 million related to the merger with Mid Ocean.

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

3. Segment Information (Continued)

Supplemental Segment and Geographic Information

The following table is an analysis of the Company's gross premiums written, net premiums written and net premiums earned by line of business:

	Year ended December 31		
Gross premium written:	**2000**	**1999**	**1998**
Casualty insurance	$ 634,189	$ 297,899	$ 411,405
Casualty reinsurance	493,362	481,392	311,057
Property catastrophe	159,771	147,372	80,420
Other property	568,441	424,666	315,013
Marine, energy, aviation and satellite	365,850	212,452	108,701
Lloyd's syndicates (1)	486,640	591,520	162,773
Other (2)	420,778	287,619	254,170
Total	$3,129,031	$2,442,920	$1,643,539
Net premium written:	**2000**	**1999**	**1998**
Casualty insurance	$ 396,935	$ 232,614	$ 301,362
Casualty reinsurance	326,127	419,000	268,460
Property catastrophe	132,288	128,863	71,380
Other property	404,749	311,312	231,690
Marine, energy, aviation and satellite	230,356	152,783	82,484
Lloyd's syndicates (1)	311,814	423,880	145,691
Other (2)	313,971	233,431	223,197
Total	$2,116,240	$1,901,883	$1,324,264
Net premium earned:	**2000**	**1999**	**1998**
Casualty insurance	$ 358,653	$ 272,677	$ 287,438
Casualty reinsurance	390,452	331,778	282,245
Property catastrophe	132,818	133,420	122,583
Other property	334,347	324,571	233,405
Marine, energy, aviation and satellite	212,273	163,112	92,147
Lloyd's syndicates (1)	357,824	355,769	153,852
Other (2)	248,873	168,679	152,621
Total	$2,035,240	$1,750,006	$1,324,291

(1) Lloyd's syndicates write a variety of coverages encompassing most of the above lines of business.

(2) Other premiums written and earned include political risk, surety, bonding and warranty.

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

3. Segment Information (Continued)

The following table shows an analysis of the Company's net premiums written by geographical location of subsidiary:

Net premiums written:	2000	1999	1998
Bermuda	$ 609,609	$ 561,750	$ 534,092
United States	934,110	684,468	497,364
Europe and other	572,521	655,665	292,808
Total	$2,116,240	$1,901,883	$1,324,264

Major Customers

During 2000, 1999 and 1998, approximately 22%, 21% and 34%, respectively, of the Company's consolidated gross written premiums were generated from or placed by Marsh & McLennan Companies. During 2000, 1999 and 1998, approximately 16%, 13% and 19%, respectively, of the Company's consolidated gross written premiums were generated from or placed by AON Corporation and its subsidiaries. No other broker accounted for more than 10% of gross premiums written in each of the three years ended December 31, 2000.

4. Investments

Net investment income is derived from the following sources:

	Year ended December 31		
	2000	1999	1998
Fixed maturities, short-term investments and cash equivalents	$551,317	$538,169	$423,612
Equity securities	10,661	11,835	19,596
Total investment income	561,978	550,004	443,208
Investment expenses	19,478	24,686	25,918
Net investment income	$542,500	$525,318	$417,290

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

4. Investments (Continued)

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

	Year ended December 31		
	2000	**1999**	**1998**
Net realized gains (losses):			
Fixed maturities and short-term investments:			
Gross realized gains	$780,430	$ 116,226	$445,086
Gross realized losses	(815,419)	(214,196)	(398,046)
Net realized gains (losses)	(34,989)	(97,970)	47,040
Equity securities:			
Gross realized gains	303,503	254,779	613,186
Gross realized losses	(149,842)	(62,453)	(463,159)
Net realized gains	153,661	192,326	150,027
Write down of other investments	(66,200)	–	–
Net realized (loss)gain on sale of investment in affiliate	(1,901)	–	14,137
Net realized gains on investments	50,571	94,356	211,204
Change in unrealized appreciation:			
Fixed maturities and short-term investments	137,628	(333,868)	(37,741)
Equity securities	(231,140)	101,652	41,819
Deferred (losses) gains on forward contracts	(9,388)	762	(13,708)
Investment portfolio of affiliates	(6,290)	(11,438)	(5,062)
Change in deferred income tax liability	(9,131)	31,050	(722)
Net change in unrealized appreciation on investments	(118,321)	(211,842)	(15,414)
Total net realized gains (losses) and change in unrealized appreciation on investments	$ (67,750)	$(117,486)	$195,790

There were no significant non-income producing investments as at December 31, 2000, 1999 and 1998.

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

4. Investments (Continued)

The cost (amortized cost for fixed maturities and short-term investments), market value and related unrealized gains (losses) of investments are as follows:

December 31, 2000	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Market Value
Fixed maturities:				
U.S. Government and Government agency	$1,361,972	$ 51,524	$ (1,373)	$1,412,123
Corporate	4,419,283	65,962	(255,122)	4,230,123
Mortgage-backed securities	1,818,697	18,649	(6,951)	1,830,395
U.S. States and political subdivisions of the States	516,949	18,936	(2,100)	533,785
Non-U.S. Sovereign Government	597,295	16,318	(14,958)	598,655
Total fixed maturities	$8,714,196	$171,389	$ (280,504)	$8,605,081
Short-term investments:				
U.S. Government and Government agency	$ 162,641	202	$ (27)	$ 162,816
Corporate	179,709	1,451	(9,539)	171,621
Non-U.S. Sovereign Government	4,797	52	(279)	4,570
Total short-term investments	$ 347,147	$ 1,705	$ (9,845)	$ 339,007
Total equity securities	$ 515,440	$ 84,650	$ (42,630)	$ 557,460

December 31, 1999	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Market Value
Fixed maturities:				
U.S. Government and Government agency	$ 560,628	$ 1,011	$ (12,532)	$ 549,107
Corporate	4,610,613	31,407	(234,730)	4,407,290
Mortgage-backed securities	1,118,104	682	(23,602)	1,095,184
U.S. States and political subdivisions of the States	779,328	7,850	(17,402)	769,776
Non-U.S. Sovereign Government	767,246	10,809	(18,261)	759,794
Total fixed maturities	$7,835,919	$ 51,759	$ (306,527)	$7,581,151
Short-term investments:				
U.S. Government and Government agency	$ 82,475	$ –	$ (63)	$ 82,412
Corporate	315,834	229	(270)	315,793
Non-U.S. Sovereign Government	7,066	–	(11)	7,055
Total short-term investments	$ 405,375	$ 229	$ (344)	$ 405,260
Total equity securities	$ 863,020	$377,302	$ (104,142)	$1,136,180

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

4. Investments (Continued)

The contractual maturities of fixed maturity securities are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	December 31, 2000		December 31, 1999	
	Amortized Cost	Market Value	Amortized Cost	Market Value
Due after 1 through 5 years	$1,829,636	$1,791,752	$2,091,280	$2,025,736
Due after 5 through 10 years	1.906,291	1,873,982	1,816,040	1,773,639
Due after 10 years	3,159,572	3,105,941	2,810,495	2,686,592
Mortgage-backed securities	1,818,697	1,833,406	1,118,104	1,095,184
	$8,714,196	$8,605,081	$7,835,919	$7,581,151

At December 31, 2000 and 1999, approximately $113.1 million and $89.4 million, respectively, of securities were on deposit with various U.S. state or government insurance departments in order to comply with relevant insurance regulations.

The Company has two facilities available for the issue of letters of credit collateralized against the Company's investment portfolio with a value of $483.0 million at December 31, 2000 and $791.4 million at December 31, 1999. At December 31, 2000 and 1999, approximately $160.0 million and $591.0 million, respectively, of letters of credit were issued and outstanding under these facilities.

Included in cash and invested assets at December 31, 2000 and 1999 are approximately $18.0 million and $16.6 million, respectively, of assets held in an escrow account in accordance with U.S. insurance regulations.

5. Investments in Affiliates

The Company's investment in affiliates and equity in net income from such affiliates are summarized below:

	December 31, 2000		December 31, 1999		December 31, 1998	
	Carrying Value	Equity in Net Income for the Year	Carrying Value	Equity in Net Income for the Year	Carrying Value	Equity in Net Income for the Year
Investment management companies and related investment funds	$571,022	$70,032	$291,723	$43,865	$ 10,609	$ (1,400)
Insurance affiliates	221,700	4,323	188,188	2,958	144,059	51,692
	$792,722	$74,355	$479,911	$40,907	$154,668	$50,292

The Company has minority investments ranging from 20% to 30% in several investment fund managers. The significant investments include Highfields Capital Management LP, a global equity investment firm, and MKP Capital Management, a fixed income investment manager specializing in mortgage-backed securities. The Company has invested in certain closed end funds, including funds managed by these investment fund managers, all of which are included in investment management companies and related investment funds, above.

5. Investments in Affiliates (Continued)

The Company's significant insurance affiliate investments at December 31, 2000 include Le Mans Ré, Annuity & Life Re (''ALRe'') and FSA International, with ownership in those entities at 49%, 11% and 20%, respectively. Insurance affiliates included Risk Capital Holdings at December 31, 1999 and 1998, and Mid Ocean at December 31, 1998.

The Company owned approximately 28% of the issued shares of Arch Capital (formerly Risk Capital Holdings) at December 31, 1999. In 2000, the Company exchanged its shares in Arch Capital and $3.6 million in cash for Arch Capital's ownership in Latin American Re and 1.4 million shares and 100,000 warrants in ALRe, in which the Company had an existing investment. ALRe is a Bermuda-based company and is a leading provider of annuity and life reinsurance to insurance companies in North America. Although the Company has beneficial ownersh ip of only 11% of ALRe's outstanding common shares, XL is deemed to have significant influence as the Company has representatives on ALRe's board of directors. Based upon the quoted market value of ALRe's common shares, the total market value of the Company's investment was $91.1 million compared to a carrying value of $60.8 million at December 31, 2000.

In 1999, the Company signed a joint venture agreement with Les Mutuelles du Mans Assurances Group to form a new French reinsurance company, Le Mans Ré. The Company owns a 49% shareholding in the new company, which underwrites a worldwide portfolio comprising most classes of property and casualty reinsurance business together with a selective portfolio of life reinsurance business. The Company contributed $31.2 million in additional capital during 2000.

The Company owned approximately 25% of Mid Ocean until July 31, 1998. Subsequent to this date, Mid Ocean was acquired by the Company and has been consolidated.

In certain investments, the carrying value is different from the underlying share of the investee's net assets. The difference represents goodwill on acquisition that is being amortized.

6. Business Combinations and Change in Fiscal Year End

(a) NAC Re Corp

On June 18, 1999, the Company merged with NAC in an all-stock transaction. Shareholders of NAC received 0.915 Company shares for each NAC share in a tax-free exchange. Approximately 16.9 million of the Company's ordinary shares were issued in this transaction. The merger transaction has been accounted for as a pooling of interests under U.S. GAAP.

Following the merger, the Company changed its fiscal year end from November 30 to December 31 as a conforming pooling adjustment. No adjustments were necessary to conform NAC's accounting policies, although certain reclassifications were made to the NAC financial statements to conform to the Company's presentation.

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

6. Business Combinations and Change in Fiscal Year End (Continued)

The following table presents a reconciliation of the total revenues, net income, and earnings per share of the Company as previously reported as adjusted for the change in fiscal year end, combined with the results of NAC:

December 1998	Consolidated Total Revenues	Consolidated Net income
XL Capital – year end November 30, 1998 as previously reported	$1,217,648	$587,663
Less one month December 31, 1997	93,835	57,168
Add one month December 31, 1998	202,210	29,785
XL Capital – year end December 31, 1998 as adjusted before combination with NAC	1,326,023	560,280
NAC – year end December 31, 1998	699,379	96,050
Combined results – year end December 31, 1998	$2,025,402	$656,330

	Basic Earnings per Share	Diluted Earnings per Share
XL Capital – year end November 30, 1998 as previously reported	$6.32	$6.20
XL Capital – year end December 31, 1998 as adjusted before combination with NAC	$5.88	$5.77
NAC – year end December 31, 1998 (1)	$5.74	$5.22
Weighted average combined earnings per share as adjusted	$5.86	$5.68

(1) After giving effect to the exchange of 0.915 Company shares for each NAC Share.

(b) ECS, Inc and Intercargo Corporation

In 1999, the Company acquired ECS, an underwriting manager which specializes in environmental insurance coverages and risk management services. ECS commenced underwriting policies on behalf of the Company's insurance and reinsurance subsidiaries effective January 1, 2000.

In 1999, the Company acquired Intercargo, which underwrites specialty insurance products for companies engaged in international trade, including U.S. Customs bonds and marine cargo insurance.

The Intercargo and ECS acquisitions have been accounted for under the purchase method of accounting. The combined purchase price was $222.8 million and the resulting goodwill of $159.6 million is being amortized over 20 years. Net cash acquired as a result of the acquisition was $49.6 million.

(c) Mid Ocean Limited

In August 1998, the Company merged with Mid Ocean. Shareholders of Mid Ocean received 1.0215 Ordinary Shares for each Mid Ocean share subject to a cash election option which was taken up of $96 million. The merger with Mid Ocean was accounted for as a purchase under U.S. GAAP and results of operations of Mid Ocean are included from August 1, 1998. The total purchase price was $2.2 billion; the fair value of Mid Ocean's net assets not already owned by the Company was $0.9 billion with the balance of $1.3 billion representing goodwill which is

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

6. Business Combinations and Change in Fiscal Year End (Continued)

being amortized over 40 years. On August 1, 1998, the consolidated balance sheet of Mid Ocean included the following items at fair value:

Investments available for sale	$1,668,224
Premiums receivable	445,540
Other assets	442,831
Total assets	2,556,595
Unpaid loss and loss expense reserves	595,261
Unearned premium	458,994
Total liabilities	1,195,835
Shareholders' equity	1,360,760

Cash and cash equivalents totaling $137 million is included in other assets. Net cash acquired as a result of this merger was $41 million.

See Note 22 for further details.

7. Losses and Loss Expenses

Unpaid losses and loss expenses are comprised of:

	Year ended December 31		
	2000	1999	1998
Reserve for reported losses and loss expenses	$2,788,378	$2,175,688	$2,062,046
Reserve for losses incurred but not reported	2,883,684	3,193,714	2,834,597
Unpaid losses and loss expenses	$5,672,062	$5,369,402	$4,896,643
Net losses and loss expenses incurred comprise:			
Loss and loss expense payments	$1,910,624	$1,392,024	$ 849,777
Change in unpaid losses and loss expenses	625,043	303,140	285,775
Reinsurance recoveries	(1,103,108)	(390,860)	(294,035)
Net losses and loss expenses incurred	$1,432,559	$1,304,304	$ 841,517

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

7. Losses and Loss Expenses (Continued)

The following table represents an analysis of paid and unpaid losses and loss expenses and a reconciliation of the beginning and ending unpaid losses and loss expenses for the years indicated:

	2000	1999	1998
Unpaid losses and loss expenses at beginning of year	$5,369,402	$4,896,643	$3,972,376
Unpaid losses and loss expenses recoverable	(831,864)	(593,960)	(363,716)
Net unpaid losses and loss expenses at beginning of year	4,537,538	4,302,683	3,608,660
Increase (decrease) in net losses and loss expenses incurred in respect of losses occurring in:			
Current year	1,827,443	1,591,414	1,097,161
Prior years	(394,884)	(287,110)	(255,644)
Total net incurred losses and loss expenses	1,432,559	1,304,304	841,517
Interest incurred on experience reserves and exchange rate effects	(27,064)	(5,950)	2,516
Net loss reserves acquired	52,932	30,003	580,879
Less net losses and loss expenses paid in respect of losses occurring in:			
Current year	411,685	281,806	272,456
Prior years	1,251,985	811,696	458,433
Total net paid losses	1,663,670	1,093,502	730,889
Net unpaid losses and loss expenses at end of year	4,332,295	4,537,538	4,302,683
Unpaid losses and loss expenses recoverable	1,339,767	831,864	593,960
Unpaid losses and loss expenses at end of year	$5,672,062	$5,369,402	$4,896,643

Business written by the Company has loss experience characterized as low frequency but high severity in nature. This may result in volatility in the Company's financial results. Actuarial assumptions used to establish the liability for losses and loss expenses are periodically adjusted to reflect comparisons to actual loss and loss expense development, inflation and other considerations.

Several aspects of the Company's casualty insurance operations complicate the actuarial reserving techniques for loss reserves as compared to other insurance operations. Among these aspects are the differences in the policy forms from more traditional forms, the lack of complete historical loss data for losses of the same type intended to be covered by the policies and the expectation that losses in excess of the attachment level of the Company's policies generally will be characterized by low frequency and high severity, limiting the utility of claims experience of other insureds for similar claims. While management believes it has made a reasonable estimate of ultimate losses, the ultimate claims experience may not be as reliably predicted as may be the case with other insurance operations, and there can be no assurance that losses and loss expenses will not exceed the total reserves.

Net losses incurred in 2000 increased over 1999, principally due to current year development. Current year development reflects both the growth in business assumed and an increase in loss ratios applied. The increase in the loss ratio is due to the effect of competition which has depressed premium rates, particularly on certain casualty lines. Current year losses also reflect the early development of certain losses on the Company's large account business within its insurance operations. Historically, the Company does not experience the reporting of such losses at an early

7. Losses and Loss Expenses (Continued)

stage and the Company's reserving methodology for these lines of business extrapolates these losses into the projections of future development. If future development is eventually determined to be less than the estimated ultimate losses recorded, loss reserves will be reduced at that time. This occurred for the 1993 through 1996 underwriting years, resulting in a reduction in prior year losses.

Net losses incurred for 2000 also reflects reserve adjustments to several unprofitable lines of business that the Company has now exited, including trucking, inland energy and certain classes of aviation. A net reserve charge of $114.0 million has been recorded for these lines.

There has been a high level of paid losses in 2000 due to the settlement of previously established reserves, particularly catastrophe losses as noted below.

The Company's outward reinsurance programs in 2000 have mitigated part of the overall loss development, as shown by the increase in the unpaid losses and loss expenses recoverable, both in the insurance and reinsurance segments. In relation to business lines exited from the Lloyd's operations, additional reinsurance costs of $19.1 million were incurred in respect of expected loss recoveries recorded of $38.0 million. In the reinsurance segment, $80.6 million of additional reinsurance costs were recorded with $151.8 million of expected loss recoveries. The purchase of additional reinsurance in 2000 relates primarily to the casualty lines where the Company has taken advantage of favorable pricing and terms.

Partially offsetting this increase in net incurred losses in 2000 compared to 1999 was a reduction in the number and magnitude of catastrophe losses that occurred. Catastrophe losses in 2000, which included an oil refinery loss in Kuwait, several satellite losses, and the Singapore Airlines loss, totaled approximately $95.0 million. By comparison, 1999 generated approximately $185.0 million of catastrophe losses to the Company, including the European storms in December, hailstorms in Sydney, tornadoes in Oklahoma and satellite losses.

Net losses incurred in 1999 increased significantly over 1998 for a number of reasons. The Company acquired Mid Ocean and Brockbank in August 1998 and therefore only recognized the effect of their operations for five months in 1998. Incurred losses for these entities were approximately $475.0 million in 1999 compared to $260.0 million in 1998. Partially offsetting this, in 1998, the Company incurred approximately $60.0 million in catastrophe losses relating to Hurricane Georges and the SwissAir loss. These losses were incurred in the reinsurance operations.

In 1999, the Lloyd's operations experienced loss deterioration on the U.K. motor business principally from the 1998 and 1999 underwriting years of approximately $20.0 million. The motor business was sold in December 1999 and the Company retains residual liability on this business.

1999 incurred losses also include an increase to reinsurance loss reserves of $95.0 million for NAC Re due to an alignment of reserving methodologies at the time of the merger with the Company in June 1999.

The decrease in prior year incurred losses in all three years is driven primarily by the Company's insurance liability excess of loss reserves. The basis for establishing IBNR for these lines is relatively judgmental due to the lack of industry data available. Consequently, the Company estimates loss reserves through actuarial models based upon its own experience. When the Company commenced writing this type of business in 1986, limited data was available and the Company has made its best estimate of loss reserves for each underwriting year since that time. Over time, the amount of data has increased, providing a larger statistical base for estimating reserves. Redundancies in prior year loss reserves have occurred where loss experience has developed more favorably than expected. This trend is not necessarily expected to continue.

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

7. Losses and Loss Expenses (Continued)

The increase in paid losses in 1999 reflects the acquisition of Mid Ocean and Brockbank in 1998.

The Company's net incurred losses and loss expenses includes a charge of $2.8 million, $10.6 million and $1.2 million in 2000, 1999 and 1998, respectively, for estimates of actual and potential non-recoveries from reinsurers. Such charges for non-recoveries relate mainly to reinsurance ceded for casualty business written prior to 1986. As at December 31, 2000 and 1999, the reserve for potential non-recoveries from reinsurers was $25.6 million and $25.8 million, respectively.

Except for certain workers' compensation liabilities, the Company does not discount its unpaid losses and loss expenses. The Company utilizes tabular reserving for workers' compensation unpaid losses that are considered fixed and determinable and discounts such losses using an interest rate of 7%. The tabular reserving methodology results in applying uniform and consistent criteria for establishing expected future indemnity and medical payments (including an explicit factor for inflation) and the use of mortality tables to determine expected payment periods. Tabular unpaid losses and loss expenses, net of reinsurance, at December 31, 2000 and 1999 were $168.8 million and $85.7 million, respectively. The related discounted unpaid losses and loss expenses were $63.4 million and $28.1 million as of December 31, 2000 and 1999.

The nature of the Company's high excess of loss liability and catastrophe business can result in loss payments that are both irregular and significant. Similarly, adjustments to reserves for individual years can be irregular and significant. Such adjustments are part of the normal course of business for the Company. Conditions and trends that have affected development of liability in the past may not necessarily occur in the future. Accordingly, it is inappropriate to extrapolate future redundancies based upon historical experience.

Asbestos and Environmental Related Claims

The Company's reserving process includes a continuing evaluation of the potential impact on unpaid liabilities from exposure to asbestos and environmental claims, including related loss adjustment expenses. Liabilities are established to cover both known and incurred but not reported claims.

A reconciliation of the opening and closing unpaid losses and loss expenses related to asbestos and environmental exposure claims related to business written prior to 1986 for the years indicated is as follows:

	Year ended December 31		
	2000	**1999**	**1998**
Net unpaid losses and loss expenses at beginning of year	$36,206	$34,850	$32,767
Net incurred losses and loss expenses	1,053	4,416	5,541
Less net paid losses and loss expenses	2,512	3,060	3,458
Net (decrease) increase in unpaid losses and loss expenses	(1,459)	1,356	2,083
Net unpaid losses and loss expenses at end of year	34,747	36,206	34,850
Unpaid losses and loss expenses recoverable at end of year	48,133	49,022	43,211
Gross unpaid losses and loss expenses at end of year	$82,880	$85,228	$78,061

Incurred but not reported (''IBNR'') losses, net of reinsurance, included in the above table was $14.0 million in 2000, $16.1 million in 1999 and $17.0 million in 1998. Unpaid losses recoverable are net of potential uncollectable amounts.

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

7. Losses and Loss Expenses (Continued)

As of December 31, 2000 and 1999, the Company had approximately 374 and 370 open claim files, respectively, for potential asbestos exposures and 613 and 689 open claim files, respectively, for potential environmental exposures on business written prior to 1986. Approximately 45% and 46% of the open claim files for 2000 and 1999, respectively, are due to precautionary claim notices. Precautionary claim notices are submitted by the ceding companies in order to preserve their right to receive coverage under the reinsurance contract. Such notices do not contain an incurred loss amount to the Company.

The Company believes it has made reasonable provision for its asbestos and environmental exposures and is unaware of any specific issues that would significantly affect its estimate for losses and loss expenses.

The estimation of loss and loss expense liabilities for asbestos and environmental exposures is subject to much greater uncertainty than is normally associated with the establishment of liabilities for certain other exposures due to several factors, including: i) uncertain legal interpretation and application of insurance and reinsurance coverage and liability; ii) the lack of reliability of available historical claims data as an indicator of future claims development; iii) an uncertain political climate which may impact, among other areas, the nature and amount of costs for remediating waste sites; and iv) the potential of insurers and reinsurers to reach agreements in order to avoid further significant legal costs. Due to the potential significance of these uncertainties, the Company believes that no meaningful range of loss and loss expense liabilities beyond recorded reserves can be established. As these uncertainties are resolved, additional reserve provisions, which could be material in amount, may be necessary.

8. Reinsurance

The Company utilizes reinsurance and retrocession agreements principally to increase aggregate capacity and to reduce the risk of loss on business assumed. The Company's reinsurance and retrocession agreements provide for recovery of a portion of losses and loss expenses from reinsurers and reinsurance recoverables are recorded as assets. The Company is liable if the reinsurers are unable to satisfy their obligations under the agreements.

The effect of reinsurance and retrocessional activity on premiums written and earned is shown below:

	Premiums written Year ended December 31			Premiums earned Year ended December 31		
	2000	1999	1998	2000	1999	1998
Direct	$ 1,688,923	$1,088,028	$ 779,551	$1,456,064	$ 994,339	$ 672,871
Assumed	1,440,108	1,354,892	863,988	1,455,694	1,259,632	926,730
Ceded	(1,012,791)	(541,037)	(319,275)	(876,518)	(503,965)	(275,310)
Net	$ 2,116,240	$1,901,883	$1,324,264	$2,035,240	$1,750,006	$1,324,291

The Company recorded reinsurance recoveries on losses and loss expenses incurred of $1.1 billion, $390.9 million and $294.0 million for the years ended December 31, 2000, 1999 and 1998, respectively. The Company is the beneficiary of letters of credit, trust accounts and funds withheld in the aggregate amount of $371.0 million at December 31, 2000, collateralizing reinsurance recoverables with respect to certain retrocessionnaires.

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

9. Deposit Liabilities and Policy Benefit Reserves

The Company has entered into certain contracts that transfer insufficient risk to be accounted for as reinsurance under SFAS No. 113. These contracts have been recorded as deposit liabilities and are matched by an equivalent amount of investments. At December 31, 2000 and 1999, total deposit liabilities were $628.4 million and $310.4 million, respectively.

In December 1999, the Company entered into a contract reinsuring a portfolio of life and annuity business that has been accounted for as an investment contract under SFAS No. 97, with a corresponding liability for estimated future policy benefits in the amount of $635.6 million. The Company transferred liabilities of $108.1 million in 2000 to a third party for an equivalent consideration.

10. Notes Payable and Debt and Financing Arrangements

As at December 31, 2000, the Company had bank, letter of credit and loan facilities available from a variety of sources, including commercial banks, totaling $2.6 billion (1999: $2.16 billion) of which $450.0 million (1999: $410.7 million) was outstanding. In addition, $1.1 billion (1999: $891.6 million) of letters of credit were outstanding, 14% of which were collateralized by the Company's investment portfolio, supporting U.S. non-admitted business and the Company's Lloyd's capital requirements. Approximately 40% of the non-collateralized letters of credit were issued in connection with intercompany quota share agreements between subsidiaries.

The financing structure at December 31, 2000 was as follows:

Facility	Commitment	In Use/Outstanding
Debt:		
364 day Revolver	$ 500,000	$ –
2 facilities of 5 year Revolvers – total	350,000	350,000
7.15% Senior Notes due 2005	100,000	100,000
	$ 950,000	$ 450,000
Letters of Credit:		
5 facilities – total	$1,679,000	$1,109,000

The financing structure at December 31, 1999 was as follows:

Facility	Commitment	In Use/Outstanding
Debt:		
Company term note	$ 11,000	$ 11,000
2 facilities of 364 day Revolvers – total	650,000	–
2 facilities of 5 year Revolvers – total	350,000	299,700
7.15% Senior Notes due 2005	100,000	100,000
	$1,111,000	$ 410,700
Letters of Credit:		
7 facilities – total	$1,246,500	$ 891,600

10. Notes Payable and Debt and Financing Arrangements (Continued)

The Company entered a $500.0 million 364-day revolving credit facility effective June 5, 2000 to replace previous facilities of $650.0 million that expired during the year. A syndicate of banks provides this facility and borrowings are unsecured. The Company borrowed and repaid $200.0 million under the expired facility during the first quarter of 2000. There were no borrowings under the facilities during the remainder of the year ended December 31, 2000. The weighted average interest rate on the funds borrowed was approximately 6.3% during 2000 and approximately 5.41% during 1999.

Two syndicates of banks provide the two five-year facilities and borrowings are unsecured. The amounts of $350.0 million and $299.7 million outstanding at December 31, 2000 and 1999, respectively, relate primarily to the remaining outstanding balance from the $300.0 million borrowed to finance the cash option election available to shareholders in connection with the Mid Ocean acquisition in August 1998, and the $109.7 million borrowed to finance the acquisition of ECS and Intercargo during 1999. The weighted average interest rate on funds borrowed during 2000 was approximately 6.6% and 5.43% during 1999.

In 1995, the Company issued $100.0 million of 7.15% Senior Notes due November 15, 2005 through a public offering at a price of $99.9 million.

The Company repaid an $11.0 million term note on September 29, 2000.

The Company has five letter of credit facilities available at December 31, 2000, two from two syndicates of banks, one from a U.K. bank and two from U.S. banks. These facilities include a new $1.0 billion unsecured syndicated letter of credit facility that replaced several syndicated and bilateral facilities provided by U.K. banks, in addition to a new $304.0 million unsecured syndicated facility that replaced several existing facilities supporting the Company's Lloyd's capital requirements. The letter of credit facilities are used to collateralize certain reinsureds' premium and unpaid loss reserves with the Company and to support Lloyd's capital requirements of the Company's corporate syndicates. Of the letters of credit outstanding at December 31, 2000, $160.0 million (1999: $591.0 million) were collateralized against the Company's investment portfolio and $949.0 million (1999: $300.6 million) were unsecured. The Company plans to continue the process of transferring letters of credit into one of the new syndicated facilities.

$100.0 million of 5.25% Convertible Subordinated Debentures due December 15, 2002 were issued in December 1992 through a private offering. The Debentures were called in June 1999 and converted to approximately 1.8 million of the Company's shares.

$100.0 million of 8% Senior Notes due June 15, 1999 were issued in June 1992 through a public offering. These Notes were repaid in June 1999 through additional borrowings and internal funds.

Total pre-tax interest expense on the borrowings described above was $32.1 million, $37.4 million and $33.4 million for the years ended December 31, 2000, 1999 and 1998, respectively. Associated with the Company's bank and loan commitments are various loan covenants with which the Company was in compliance throughout the three-year period.

11. Commitments and Contingencies

(a) Financial Instruments with Off-Balance Sheet Risk

The Company invests in derivative instruments, such as foreign currency forward contracts and futures for purposes other than trading. These derivative instruments are used for foreign currency exposure management and to obtain exposure to specific financial markets.

(i) Foreign Currency Exposure Management

The Company uses foreign exchange contracts to manage its exposure to the effects of fluctuating foreign currencies on the value of its foreign currency fixed maturities and equity investments. These contracts are not designated as specific hedges for financial reporting purposes and therefore, realized and unrealized gains and losses recognized on them are recorded in income in the period in which they occur. These contracts generally have maturities of three months or less. In addition, where the Company's investment managers are of the opinion that potential gains exist in a particular currency, then a forward contract will not be entered into. At December 31, 2000 and 1999, forward foreign exchange contracts with notional principal amounts totaling $111.9 million and $339.3 million, respectively, were outstanding. The fair value of these contracts as at December 31, 2000 was $109.6 million (1999: $341.1 million) with unrealized losses of $2.3 million (1999: $1.8 million). Gains of $28.1 million and losses of $2.7 million were realized during 2000 and 1999, respectively.

In addition, the Company also enters into foreign exchange contracts to buy and sell foreign currencies in the course of trading its foreign currency investments. These contracts are not designated as specific hedges for financial reporting purposes, and generally have maturities of two weeks or less. As such, any realized or unrealized gains or losses are recorded in income in the period in which they occur. At December 31, 2000, the Company had $54.9 million of such contracts outstanding, and had recognized $1.5 million in realized and unrealized losses for the year. At December 31, 1999, the value of such contracts outstanding was not significant.

The Company attempts to hedge directly the foreign currency exposure of a portion of its foreign currency fixed maturity investments using forward foreign exchange contracts that generally have maturities of three months or less, and which are rolled over to provide continuing coverage for as long as the investments are held. Where an investment is sold, the related foreign exchange sale contract is closed by entering into an offsetting purchase contract. At December 31, 2000, the Company had, as hedges, foreign exchange contracts for the sale of $121.0 million (1999: $94.0 million) and the purchase of $25.7 million (1999: $7.4 million) of foreign currencies at fixed rates, primarily Euros. The notional value of fixed maturities denominated in foreign currencies that were hedged and held by the Company as at December 31, 2000 and 1999 was $100.6 million and $85.2 million, respectively.

In connection with these foreign exchange contracts directly hedging foreign currency fixed maturity investments, unrealized foreign exchange gains or losses are deferred and included in accumulated other comprehensive (loss) income. As at December 31, 2000, unrealized losses amounted to $10.2 million. As at December 31, 1999, unrealized losses amounted to $2.0 million and were offset by corresponding increases in the U.S. dollar value of the investments. As at December 31, 2000, realized gains of $14.6 million were recognized in the income statement. As at December 31, 1999, realized losses amounted to $0.7 million.

During the year ended December 31, 2000, the Company used foreign exchange contracts to manage its exposure to the effects of fluctuating foreign currencies on the amount of its known claims payable in foreign currencies. These contracts were not designated as specific hedges for financial reporting purposes and therefore, realized and unrealized gains and losses on these contracts were recorded in income in the period in which they occurred. As at December 31, 2000 no contracts were outstanding. A loss of $6.8 million was realized in the year in connection with these contracts.

11. Commitments and Contingencies (Continued)

In 2000, the Company used foreign exchange forward contracts to reduce its exposure to premiums receivable denominated in foreign currencies. The forward contract is closely matched with the receivable maturity date. Both the foreign currency receivable and the offsetting forward contract are marked to market on each balance sheet date, with any gains and losses recognized in earnings. At December 31, 2000, the Company had forward contracts outstanding for the sale of $10.0 million of foreign currencies at fixed rates, primarily U.K. Sterling. Losses of $0.2 million were realized during 2000.

The Company attempts to manage the exchange volatility arising from certain administration costs denominated in foreign currencies. Throughout the year, forward contracts are entered into to acquire the foreign currency at an agreed rate in the future. Any gains or losses on the forward contracts are deferred and included as a component of shareholders' equity. As the administration expenses are incurred, the gains and losses are recognized in the income statement. At December 31, 2000, the Company had forward contracts outstanding for the purchase of $12.8 million of Euros and U.K. Sterling at fixed rates. Gains and losses deferred in accumulated other comprehensive income and realized throughout the year were insignificant.

The Company is exposed to credit risk in the event of non-performance by the other parties to the forward contracts, however the Company does not anticipate non-performance. The difference between the notional principal amounts and the associated market value is the Company's maximum credit exposure.

(ii) Financial Market Exposure

The Company also invests in a synthetic equity portfolio of S&P Index futures with an exposure approximately equal in amount to the market value of underlying assets held in this fund. As at December 31, 2000, the portfolio held $43.7 million (1999: $121.9 million) in exposure to S&P 500 Index futures and underlying assets of $43.2 million (1999: $122.0 million). The value of the futures is updated daily with the change recorded in income as a realized gain or loss. For the years ended December 31, 2000 and 1999, results from index futures totaled net realized losses of $0.2 million and net realized gains of $11.3 million, respectively.

Derivative investments are also utilized to add value to the portfolio where market inefficiencies are believed to exist and also to adjust the duration of a portfolio of fixed income securities to match related deposit liabilities. At December 31, 2000, bond and stock index futures outstanding were $40.1 million (1999: $241.1 million), with underlying investments having a market value of $2.5 billion (1999: $2.5 billion).

(b) Concentrations of Credit Risk

The Company's investment portfolio is managed by external managers in accordance with guidelines that have been tailored to meet specific investment strategies, including standards of diversification which limit the allowable holdings of any single issue. The Company did not have an aggregate investment in a single entity, other than the U.S. government, in excess of 10% of shareholders' equity at December 31, 2000 and 1999.

(c) Other Investments

The Company has committed to invest in several limited partnerships as part of its overall corporate strategy. The primary purpose of these partnerships is to invest capital provided by the partners in various insurance and reinsurance ventures. The Company had invested $103.0 and $65.4 million as at December 31, 2000 and 1999, respectively, with commitments to invest a further $149.7 million over the next ten years. The Company received income from its investments of $4.0 million and $9.4 million and for the years ended December 31 2000 and 1999, respectively. The Company continually reviews the performance of the partnerships to ensure there is no other than

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

11. Commitments and Contingencies (Continued)

temporary decline in the values of its investments. The Company is a limited partner and, as such, does not actively participate in the management of the partnerships.

(d) Properties

The Company rents space for its principal executive offices under leases that expire up to 2013. Total rent expense for the years ended December 31, 2000, 1999, and 1998 was approximately $18.3 million, $13 million, and $9 million, respectively. Future minimum rental commitments under existing leases are expected to be as follows:

Year ending December 31: 2001	$ 16,204
2002	15,611
2003	14,196
2004	11,505
2005	9,938
Later years	54,855
Total minimum future rentals	$122,309

In 1997, the Company acquired commercial real estate in Bermuda for the purpose of securing long-term office space for its worldwide headquarters. The total cost of this development, including the land, is expected to be approximately $110.0, of which $101.0 million had been spent as at December 31, 2000. It is estimated that the development will be completed in April 2001.

(e) Tax Matters

The Company is a Cayman Islands corporation and, except as described below, neither it nor its non-U.S. subsidiaries have paid United States corporate income taxes (other than withholding taxes on dividend income) on the basis that they are not engaged in a trade or business or otherwise subject to taxation in the United States; however, because definitive identification of activities which constitute being engaged in trade or business in the United States is not provided by the Internal Revenue Code of 1986, regulations or court decisions, there can be no assurance that the Internal Revenue Service will not contend that the Company or its non-U.S. subsidiaries are engaged in trade or business or otherwise subject to taxation in the United States. If the Company or its non-U.S. subsidiaries were considered to be engaged in trade or business in the United States (and, if the Company or such subsidiaries were to qualify for the benefits under the income tax treaty between the United States and Bermuda or Ireland, such businesses were attributable to a ''permanent establishment'' in the United States), the Company or such subsidiaries could be subject to U.S. tax at regular tax rates on its taxable income that is effectively connected with its U.S. trade or business plus an additional 30% ''branch profits'' tax on such income remaining after the regular tax, in which case there could be a significant adverse effect on the Company's results of operations and financial condition.

(f) Financial Guaranties

The Company insures and reinsures financial guaranties issued to support public and private borrowing arrangements. Financial guaranties are conditional commitments that guaranty the performance of a customer to a third party. The Company's potential liability in the event of non-performance by the issuer of the insured obligation is represented by its proportionate share of the aggregate outstanding principal and interest payable (''insurance in

11. Commitments and Contingencies (Continued)

force'') on such insured obligation. At December 31, 2000, the Company's aggregate insurance in force was $16.6 billion. The Company manages its exposure to credit risk through a structured underwriting process which includes detailed credit analysis, review of and adherence to underwriting guidelines, surveillance policies and procedures and the use of reinsurance.

12. Share Capital

(a) Authorized and Issued

The authorized share capital is 999,990,000 ordinary shares of a par value of $0.01 each. Holders of Class A shares are entitled to one vote for each share. In June 2000, the Company's Class B ordinary shares were converted into Class A ordinary shares on a one-for-one basis.

The following table is a summary of shares issued and outstanding (in thousands):

	Year ended December 31		
	2000	1999	1998
Balance – beginning of year	127,807	128,745	101,282
Exercise of options	2,247	443	425
Issue of restricted shares	21	107	289
Repurchase of shares	(5,074)	(1,488)	(3,443)
Issue of Class A shares	19	–	27,076
Issue of Class B shares	–	–	3,116
Balance – end of year	125,020	127,807	128,745

The issue of shares in 1998 was in exchange for Mid Ocean shares and FSA shares.

(b) Share Repurchases

The Company has had several stock repurchase plans in the past as part of its capital management program. In June 1999, the Board of Directors rescinded the Company's share repurchase plans. On January 9, 2000, the Board of Directors authorized the repurchase of shares up to $500 million. During 2000, the Company repurchased 5.1 million shares at a total cost of $247.7 million, or an average cost of $48.82 per share.

(c) Stock Plans

The Company's executive stock plan, the ''1991 Performance Incentive Program'', provides for grants of non-qualified or incentive stock options, restricted stock awards and stock appreciation rights (''SARs''). The plan is administered by the Company and the Compensation Committee of the Board of Directors. Stock options may be granted with or without SARs. Grant prices are established at the fair market value of the Company's common stock at the date of grant. Options and SARs have a life of 10 years and vest annually over three years from date of grant.

Restricted stock awards issued under the 1991 Performance Incentive Program plan vest over a five year period from the date of grant. These shares contained certain restrictions, for said period, relating to, among other things, forfeiture in the event of termination of employment and transferability. As the shares are issued, deferred compensation equivalent to the difference between the issue price and the estimated fair market value on the date of the grant is charged to shareholders' equity and subsequently amortized over the five-year restriction period. Restricted stock

12. Share Capital (Continued)

issued under the plan totaled 77,472 shares, 113,100 shares and 147,836 shares in 2000, 1999 and 1998, respectively. Restricted stock awards granted by NAC prior to the merger amounted to 3,627 shares and 23,700 shares in 1999 and 1998. Vesting for such shares generally occurs over a six year period.

The Company also has stock plans in place for its non-employee directors. The ''Stock and Option Plan'' issues non-qualified options to the directors–4,000 shares at the commencement of their directorship and 5,000 shares each year thereafter. All options vest immediately on the grant date. Effective April 11, 1997, all options granted to non-employee directors are granted under the 1991 Performance Incentive Program. Directors may also may make an irrevocable election preceding the beginning of each fiscal year to defer cash compensation that would otherwise be payable as his or her annual retainer in increments of $5,000. The deferred payments are credited in the form of shares calculated by dividing 110% of the deferred payment by the market value of the Company's stock at the beginning of the fiscal year. Each anniversary thereafter, 20% of these shares are distributed. Shares issued under the plan totaled 7,846, nil and 2,737 in 2000, 1999 and 1998, respectively.

A second stock plan, intended to replace the directors' ''Retirement Plan for Non-Employee Directors,'' provides for the issue of share units equal to the amount that would have been credited to the Retirement Plan, divided by the market price of the Company's stock on January 1 of each year. These units receive dividends in the form of additional units equal to the cash value divided by the market price on the payment date. Stock units totaling 13,237, 1,217 and 5,531 were issued for in 2000, 1999 and 1998, respectively.

As a result of the merger with Mid Ocean during August 1998, 791,573 Mid Ocean options were converted to options of XL Capital.

Following the merger with NAC, new option plans were created in the Company to adopt the NAC plans. Options generally have a five or six year vesting schedule, with the majority expiring 10 years from the date of grant; the remainder having no expiration. A stock plan is also maintained for non-employee directors. Options expire 10 years from the date of grant and are fully exercisable six months after their grant date.

In 1999, the Company adopted the 1999 Performance Incentive Plan under which 1,250,000 options were available and issued to employees who were not directors or executive officers of the Company.

(d) FAS 123 Pro Forma Disclosure

The Company has adopted the disclosure-only provisions of Statement of Financial Accounting Standard No. 123, ''Accounting for Stock-Based Compensation.'' Had the Company adopted the accounting provisions of SFAS No. 123, compensation costs would have been determined based on the fair value of the stock option awards

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

12. Share Capital (Continued)

granted in 2000, 1999 and 1998, and net income and earnings per share would have been reduced to the pro-forma amounts indicated below:

	Year Ended December 31,		
	2000	1999	1998
Net income – as reported	$506,352	$470,509	$656,330
Net income – pro-forma	$481,560	$437,592	$635,239
Basic earnings per share – as reported	$ 4.07	$ 3.69	$ 5.86
Basic earnings per share – pro-forma	$ 3.87	$ 3.43	$ 5.67
Diluted earnings per share – as reported	$ 4.03	$ 3.62	$ 5.68
Diluted earnings per share – pro-forma	$ 3.83	$ 3.36	$ 5.47

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	2000	1999	1998
Dividend yield	3.58%	3.43%	1.81%
Risk free interest rate	5.04%	5.90%	4.76%
Expected volatility	25.77%	24.66%	24.72%
Expected lives	7.5 years	7.5 years	9.2 years

Total stock based compensation expensed was $9.5 million, $7.7 million and $5.8 million, in 2000, 1999 and 1998, respectively.

(e) Options

Following is a summary of stock options and related activity:

	2000		1999		1998	
	Number of Shares	Average Exercise Price	Number of Shares	Average Exercise Price	Number of Shares	Average Exercise Price
Outstanding – beginning of year	10,282,723	$46.50	7,685,414	$50.61	5,744,063	$35.28
Granted	579,852	$49.95	3,207,492	$57.06	1,749,885	$68.27
Granted – Mid Ocean conversion	–	–	–	–	791,573	$72.44
Exercised	(2,515,774)	$31.48	(421,163)	$27.57	(425,251)	$30.06
Cancelled	(183,784)	$61.80	(189,020)	$55.25	(174,856)	$40.12
Outstanding – end of year	8,163,017	$51.09	10,282,723	$46.50	7,685,414	$46.79
Options exercisable	5,034,693		5,287,657		4,288,434	
Options available for grant	9,904,918	*	1,028,853	*	2,455,190	*

* Available for grant includes shares that may be granted as either stock options or restricted stock.

12. Share Capital (Continued)

The following table summarizes information about the Company's stock options (including stock appreciation rights) for options outstanding as of December 31, 2000:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number of Options (000s)	Average Exercise Price	Average Remaining Contractual Life (Years)	Number of Options (000s)	Average Exercise Price
$10.44 – $32.93	600	$25.42	4.1	600	$25.42
$33.88 – $50.00	4,671	$46.03	7.2	2,615	$43.62
$50.31 – $64.69	1,753	$58.08	7.6	1,070	$59.39
$66.50 – $87.38	1,139	$74.58	7.8	750	$74.71
$10.44 – $87.38	8,163	$51.09	7.1	5,035	$49.43

(f) Voting

The Company's Articles of Association restrict the voting power of any person to less than approximately 10% of total voting power.

(g) Share Rights Plan

Rights to purchase Class A ordinary shares (''the Rights'') were distributed as a dividend at the rate of one Right for each Class A ordinary share held of record as of the close of business on October 31, 1998. Each Right entitles holders of Class A ordinary shares to buy one ordinary share at an exercise price of $350. The Rights would be exercisable, and would detach from the Class A ordinary shares, only if a person or group were to acquire 20% or more of XL's outstanding Class A ordinary shares, or were to announce a tender or exchange offer that, if consummated, would result in a person or group beneficially owning 20% or more of Class A ordinary shares. Upon a person or group without prior approval of the Board acquiring 20% or more of Class A ordinary shares, each Right would entitle the holder (other than such an acquiring person or group) to purchase Class A ordinary shares (or, in certain circumstances, Class A ordinary shares of the acquiring person) with a value of twice the Rights exercise price upon payment of the Rights exercise price. The Company will be entitled to redeem the Rights at $0.01 per Right at any time until the close of business on the tenth day after the Rights become exercisable. The Rights will expire at the close of business on September 30, 2008, and do not initially have a fair value. The Company has initially reserved 119,073,878 Class A ordinary shares being authorized and unissued for issue upon exercise of Rights.

13. Retirement Plans

The Company maintains both defined contribution and defined benefit retirement plans, which vary for each subsidiary. Plan assets are invested principally in equity securities and fixed maturities.

The Company has a qualified defined contribution plan which is managed externally and whereby employees and the Company contribute a certain percentage of the employee's gross salary into the plan each month. The Company's contribution generally vests over 5 years.

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

13. Retirement Plans (Continued)

At NAC, a qualified non-contributory defined benefit pension plan exists to cover substantially all its U.S. employees. This plan also includes a non-qualified supplemental defined benefit plan designed to compensate individuals to the extent their benefits under the Company's qualified plan are curtailed due to Internal Revenue Code limitations. Benefits are based on years of service and compensation, as defined in the plan, during the highest consecutive three years of the employee's last ten years of employment. Under these plans, the Company's policy is to make annual contributions to the plan that are deductible for federal income tax purposes and that meet the minimum funding standards required by law. The contribution level is determined by utilizing the entry age cost method and different actuarial assumptions than those used for pension expense purposes. The projected benefit obligation, accumulated benefit obligation and fair value of the assets for this plan with accumulated benefit obligations in excess of the plan assets were $21.3 million, $12.6 million and $12.3 million, respectively, as of December 31, 2000 and $16.6 million, $10.0 million and $11.0 million, respectively as of December 31, 1999. The discount rates used in determining the actuarial present value of benefit obligations were 7.25% and 7.75% for 2000 and 1999, respectively. The rate of increase for future compensation levels was 6.0% for 2000 and 6.5% for 1999. The assumed rate of return on plan assets was 9.0% for both 2000 and 1999.

NAC also maintains a qualified contributory defined contribution plan for substantially all its U.S. employees.

The Company's expenses for its retirement plans are not considered to be significant.

14. Accumulated Other Comprehensive Income

The related tax effects allocated to each component of the change in accumulated other comprehensive income were as follows:

	Before Tax amount	Tax Expense (Benefit)	Net of Tax amount
Year ended December 31, 2000			
Unrealized gains (losses) on investments:			
Unrealized losses arising during year	$ (76,881)	$(21,980)	$ (54,901)
Less reclassification for gains (losses) realized in income	50,571	(12,849)	63,420
Net unrealized losses	(127,452)	(9,131)	(118,321)
Foreign currency translation adjustments	(5,600)	102	(5,702)
Change in accumulated other comprehensive income	$(133,052)	$ (9,029)	$(124,023)
Year ended December 31, 1999			
Unrealized gains (losses) on investments:			
Unrealized losses arising during year	$(148,536)	$(36,394)	$(112,142)
Less reclassification for gains (losses) realized in income	94,356	(5,344)	99,700
Net unrealized losses	(242,892)	(31,050)	(211,842)
Foreign currency translation adjustments	(6,308)	(2,276)	(4,032)
Change in accumulated other comprehensive income	$(249,200)	$(33,326)	$(215,874)

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

14. Accumulated Other Comprehensive Income (Continued)

	Before Tax amount	Tax Expense (Benefit)	Net of Tax amount
Year ended December 31, 1998			
Unrealized gains (losses) on investments:			
Unrealized gains arising during year	$ 196,512	$ 12,998	$ 183,514
Less reclassification for gains realized in income	211,204	12,276	198,928
Net unrealized gains (losses)	(14,692)	722	(15,414)
Foreign currency translation adjustments	(1,342)	(470)	(872)
Change in accumulated other comprehensive income	$ (16,034)	$ 252	$ (16,286)

15. Contributed Surplus

Under the laws of the Cayman Islands, the use of the Company's contributed surplus is restricted to the issue of fully paid shares (i.e. stock dividend or stock split) and the payment of any premium on the redemption of ordinary shares.

16. Dividends

The following dividend information relates to the Company without inclusion of the pooling effect with NAC:

In 2000, four regular quarterly dividends were paid at $0.45 per share to shareholders of record of February 15, May 25, August 15 and November 15.

In 1999, four regular quarterly dividends were paid at $0.44 per share to shareholders of record at February 5, April 23, July 12 and September 24.

In 1998, four regular quarterly dividends were paid, three of $0.40 per share to shareholders of record at February 6, April 16 and July 15, and one of $0.44 per share to shareholders of record at September 28.

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

17. Taxation

Under current Cayman Islands law, the Company is not subject to any taxes in the Cayman Islands on either income or capital gains. The Company has received an undertaking that, in the event of any such taxes being imposed, the Company will be exempted from Cayman Islands income or capital gains taxes until June 2018.

The Company's U.S. subsidiaries are subject to federal, state and local corporate income taxes and other taxes applicable to U.S. corporations. The provision for federal income taxes has been determined on the basis of the income of each of the Company's U.S. subsidiaries as if a tax return has been prepared on an individual company basis. Should the U.S. subsidiaries pay a dividend to the Company, withholding taxes will apply.

Bermuda presently imposes no income, withholding or capital gains taxes and the Bermuda subsidiaries are exempted until March 2016 from any such future taxes pursuant to the Bermuda Exempted Undertakings Tax Protection Act 1966, and Amended Act 1987.

XL Europe has been approved to carry on business in the International Services Centre in Dublin. Under Section 39 of the Finance Act 1990, XL Europe is entitled to benefit from a 10% tax rate on profits (including investment income) until 2005.

XL Brockbank, NAC Re International and XL Re's London branch office are subject to United Kingdom corporation taxes. Other branches of the Company are subject to relevant local taxes.

The income tax provision in the consolidated statement of income gives effect to the permanent differences between financial and taxable income as applied for each relevant subsidiary. Due to the fact that the Company and certain subsidiaries are not subject to direct U.S. income taxes and that certain U.S. subsidiaries have tax-exempt income, the Company's effective income tax rate for its U.S. operation is less than the statutory U.S. Federal tax rate.

The tax charge (benefit) in each of the three years ended December 31, 2000 is comprised of amounts from the various taxable jurisdictions in which the Company operates. For all countries other than the U.S., there generally is no significant difference between the effective tax rate and the statutory rate in that jurisdiction. For U.S. operating income (loss), the effective rate differs from the statutory rate of 35% primarily due to tax-exempt investment income in all years, merger related costs in 1999 and a change in management's valuation allowance.

Significant components of the provision for income taxes attributable to operations were as follows:

	Year ended December 31		
	2000	**1999**	**1998**
Current (benefit) expense:			
U.S	$ (3,175)	$(27,098)	$10,490
Non U.S	8,612	9,664	14,680
Total current (benefit) expense	5,437	(17,434)	25,170
Deferred (benefit) expense:			
U.S	(53,338)	(17,534)	4,729
Non U.S	(8,455)	(4,602)	(16)
Total deferred (benefit) expense	(61,793)	(22,136)	4,713
Total tax (benefit) expense	$(56,356)	$(39,570)	$29,883

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

17. Taxation (Continued)

The U.S. subsidiaries current U.S. taxable income for the years ended December 31, 2000 and 1999 is based on regular taxable income. The current U.S. tax expense for the year ended December 31, 1998 is based on alternative minimum taxable income.

Net taxes received in the year ended December 31, 2000 were approximately $13.3 million. In the years ended December 31, 1999 and 1998, net taxes paid were approximately $30.2 million and $31.2 million, respectively. The Company's net current tax asset included in ''other assets'' in the accompanying financial statements was $14.3 million at December 31, 2000.

Significant components of the Company's deferred tax assets and liabilities, which principally relate to U.S. subsidiaries as of December 31, 2000 and 1999 were as follows:

	Year ended December 31	
	2000	**1999**
Deferred tax asset:		
Net unpaid loss reserve discount	$ 83,230	$81,672
Net unearned premiums	13,929	10,264
Unrealized depreciation on investments	–	11,995
Compensation liabilities	9,271	8,960
Other	55,429	12,516
Deferred tax asset, gross of valuation allowance	161,859	125,407
Valuation allowance	–	(11,995)
Deferred tax asset, net of valuation allowance	161,859	113,412
Deferred tax liability:		
Deferred policy acquisition costs	$ –	$ 6,850
Unrealized appreciation on investments	7,553	–
Currency translation adjustments	566	566
Other	1,572	8,068
Deferred tax liability	9,691	15,484
Net deferred tax asset	$152,168	$97,928

At December 31, 2000, the Company's management concluded that all deferred tax assets are more likely than not to be realized and consequently, no valuation allowance has been provided. At December 31, 1999, the Company's management established a valuation allowance for certain deferred tax assets.

Shareholders' equity at December 31, 2000 and 1999 reflects tax benefits of $3.3 million and $1.5 million, respectively, related to compensation expense deductions for stock options exercised for one of the Company's U.S. subsidiaries.

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

18. Statutory Financial Data

The Company's ability to pay dividends is subject to certain regulatory restrictions on the payment of dividends by its subsidiaries. The payment of such dividends is restricted by applicable laws of Bermuda, Ireland, the U.S. and U.K., including Lloyd's. The Company relies primarily on cash dividends from XL Insurance and XL Re.

Bermuda

Under The Insurance Act, 1978, (as amended by the Insurance Act Amendment 1995) amendments thereto and related regulations of Bermuda, the Company's Bermuda subsidiaries, the most significant of which are XL Insurance and XL Re, are required to prepare statutory financial statements and to file in Bermuda a statutory financial return. The Act also requires these companies to maintain certain measures of solvency and liquidity during the year.

XL Insurance's and XL Re's statutory capital and surplus, statutory net income and the minimum statutory capital and surplus required by the Act were as follows:

	Year ended December 31					
	XL Insurance			XL Re		
	2000	1999	1998	2000	1999	1998
Statutory net income	$ 744,139	$ 16,715	$ 361,663	$ 3,611	$ 155,534	$ 108,290
Statutory capital and surplus	$2,061,422	$1,314,995	$1,297,461	$2,149,806	$2,062,421	$1,966,200
Minimum statutory capital and surplus required by the Act	$ 295,879	$ 427,939	$ 300,755	$ 370,317	$ 196,254	$ 100,000

The primary difference between statutory net income and statutory capital and surplus for the Company's subsidiaries, as shown above, and net income and shareholders' equity presented in accordance with GAAP are deferred acquisition costs.

Under the Act, XL Insurance and XL Re are classified as a Class 4 insurer and reinsurer, respectively. Therefore, they are restricted to the payment of dividends in any one financial year of 25% of the prior year's statutory capital and surplus, unless their directors attest that such dividends will not cause the company to fail to meet its relevant statutory requirements. XL Insurance and XL Re have not been prevented from paying dividends by this restriction.

United States

The Company's U.S. insurance and reinsurance subsidiaries, the most significant of which is NAC Re, are subject to regulatory oversight under the insurance statutes and regulations of the jurisdictions in which they conduct business.

Consolidated statutory net income and surplus of NAC Re, as reported to the insurance regulatory authorities, differs in certain respects from the amounts as prepared in accordance with GAAP. The main differences between statutory net income and GAAP income relate to deferred acquisition costs, deferred income taxes and amortization of intangible assets. The main differences between statutory surplus and shareholders' equity, in addition to deferred acquisition costs and deferred income tax net assets, are intangible assets, unrealized appreciation on investments, and any unauthorized/authorized reinsurance charges.

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

18. Statutory Financial Data (Continued)

The following table shows statutory net income and GAAP net income (loss) and consolidated statutory surplus and consolidated shareholders' equity of NAC Re.

	Year ended December 31		
	2000	**1999**	**1998**
Net income:			
Statutory net income	$(110,574)	$ 8,948	$101,862
GAAP net income (loss)	$ (56,686)	$ (1,060)	$ 98,586
Shareholders' Equity:			
Consolidated statutory surplus	$ 575,575	$440,102	$737,114
GAAP consolidated shareholder's equity	$ 823,099	$700,725	$750,725

NAC Re is subject to the New York insurance law, which imposes certain restrictions on the payment of cash dividends and tax reimbursements. Generally, NAC Re may pay cash dividends only out of statutory earned surplus. However, the maximum amount of dividends that may be paid in any twelve month period without the prior approval of the New York Insurance Department is the lesser of net investment income or 10% of statutory surplus as such terms are defined in the New York insurance law. Statutory earned deficit at December 31, 2000 and 1999 was $12.2 million and $27.7 million, respectively. Consequently, NAC Re cannot make a dividend distribution at this time.

XL Brockbank, via Lloyd's, is a licensed insurer in the states of Illinois and Kentucky and in the U.S. Virgin Islands (''USVI''). It is also an eligible surplus lines writer in all states other than Kentucky and in the USVI, and an accredited reinsurer in every state other than Michigan, Kansas and Arizona. XL Aerospace is licensed in California as a fire and casualty broker, surplus lines broker and special lines surplus lines broker.

The insurance laws of each state of the U.S. and of many foreign countries regulate the sale of insurance within their jurisdiction by alien insurers, such as XL Insurance and XL Re. The Company believes it is not in violation of the insurance laws of any state in the U.S. or any foreign country. From time to time, various proposals for federal legislation within the United States have been circulated which could require the Company to, among other things, register as a surplus lines insurer. The Company believes that generally it could meet and comply with the requirements to be registered as a surplus lines insurer and such compliance would not have a significant impact on the ability of the Company to conduct its business. There can be no assurances, however, that the activities of the Company will not be challenged in the future or that the Company will be able to successfully defend against such challenges or that legislation will not be enacted that will affect the Company's ability to conduct its business.

Ireland

XL Europe is permitted to underwrite risks throughout the European Community (subject to certain restrictions) pursuant to the ''Third Directive'' relating to non-life insurance. XL Europe's head office is in Ireland and it is subject to regulation under Irish regulatory authority. The principal legislation and regulations governing the insurance activities of Irish insurance companies are the Insurance Acts 1909 to 1990 (the ''Irish Acts'') and a comprehensive network of regulations and statutory provisions empowering the making of regulations of which the most relevant are the European Communities (Non-Life Insurance) Regulations, 1976, the European Communities (Non-Life Insurance

18. Statutory Financial Data (Continued)

Accounts) Regulations, 1995, the European Communities (Non-Life Insurance) Framework Regulations, 1994 and related administrative rules (the ''Irish Regulations'').

In addition, XL Europe's insurance activities are subject to minimum solvency and reserve standards and auditing and reporting requirements. The Minister for Enterprise, Trade and Employment has wide powers to supervise, investigate and intervene in the affairs of such insurers.

United Kingdom

The United Kingdom Financial Services Authority (''U.K. FSA'') regulates reinsurance entities that are ''effecting and carrying on'' insurance business in the United Kingdom. Through its branches and subsidiaries in London, the Company is deemed to ''effect and carry on'' business in the United Kingdom and certain of its subsidiaries are therefore regulated by the U.K. FSA.

Lloyd's

The Company, XL Brockbank and Denham are subject to the regulatory jurisdiction of the Council of Lloyd's (the ''Council''). Unlike other financial markets in the U.K., Lloyd's is not subject to direct U.K. government regulation through The Financial Services Act of 1986 but, instead, is self regulating by virtue of the Lloyd's Act of 1982 through the bye-laws, regulations and codes of conduct written by the Council, which governs the market. It is expected that the U.K. FSA will become ultimately responsible for Lloyds regulation in 2001. Under the Council, there are two boards, the Market Board and the Regulatory Board. The former is led by a number of the working members of the Council and is responsible for the development and growth of Lloyd's worldwide business. The Regulatory Board is responsible for developing and monitoring regulatory practice and procedures. Under the regulations, the approval of the Council has to be obtained before any person can be a ''major shareholder'' or ''controller'' of a corporate Name or managing agency. The Company has been approved as both a ''major shareholder'' and a ''controller'' of its corporate Names (the ''CCVs'') and managing agencies.

As a ''controller'', the Company is required to give certain undertakings, directed principally towards ensuring that there is no direct interference in the conduct of the business of the relevant managing agency, but there are no provisions in the Lloyd's Act of 1982, the bye-laws or the regulations which provide for any liabilities of the CCVs or the XL Brockbank group as a whole to be met by the Company. In addition, a managing agency is required to comply with various capital and solvency requirements and to submit to regular monitoring and compliance procedures. The CCVs, as corporate members of Lloyd's are each required to commit a specified amount approximately equal to 50% of their underwriting capacity on the syndicates to support its underwriting on those syndicates.

The Lloyd's Act of 1982 generally restricts certain direct or indirect equity cross-ownership between a Lloyd's broker and a Lloyd's managing agent.

Other Regulation

The Company is subject to regulation in Australia, Singapore, Spain, Latin America and Germany as a result of its representative offices and branches in such jurisdictions.

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

19. Earnings Per Share

The following table sets forth the computation of the basic and diluted earnings per share:

	Year ended December 31		
	2000	1999	1998
Basic earnings per share:			
Net income	$506,352	$470,509	$656,330
Weighted average ordinary shares outstanding	124,503	127,601	112,034
Basic earnings per share	$ 4.07	$ 3.69	$ 5.86
Diluted earnings per share:			
Net income	$506,352	$470,509	$656,330
Add back after-tax interest on convertible debentures	—	1,752	3,504
Adjusted net income	$506,352	$472,261	$659,834
Weighted average ordinary shares outstanding — basic	124,503	127,601	112,034
Average stock options outstanding (1)	1,194	1,872	2,152
Conversion of convertible debentures (2)	—	831	2,020
Weighted average ordinary shares outstanding — diluted	125,697	130,304	116,206
Diluted earnings per share	$ 4.03	$ 3.62	$ 5.68

(1) Net of shares repurchased under the treasury stock method.

(2) 1998 reflects the assumed conversion of the 5.25% Convertible Subordinated Debentures due 2000. The Debentures were called in June 1999 and the actual conversion is reflected in 1999.

20. Subsequent Events

XL Capital announced on February 15, 2001 that it has agreed to purchase Winterthur International from Winterthur Swiss Insurance Company (''Winterthur''), a subsidiary of the Credit Suisse Group (''CSG''). The Company will be purchasing a combination of insurance companies and selected Winterthur International insurance portfolios. The all-cash transaction is valued at approximately $600.0 million and may be funded by the Company with a combination of current resources and external financing. Winterthur International is the international, large commercial account property and casualty insurance business of Winterthur. Winterthur International operates in 27 countries, has more than 1,000 employees and in 2000 had gross premiums written and net premiums earned of approximately $1.3 billion and $600.0 million, respectively. In terms of premium volume, Winterthur International's top five markets are the U.K., Switzerland, Germany, the U.S. and France. As at September 30, 2000, Winterthur International (including certain operations to be retained by CSG) had investment assets of approximately $1.9 billion.

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

21. Unaudited Quarterly Financial Data

The following is a summary of the unaudited quarterly financial data for 2000 and 1999:

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2000				
Net premiums earned	$494,499	$503,375	$539,945	$497,421
Net investment income	128,527	136,440	134,624	142,909
Net realized gains (losses) on investments	68,707	5,075	1,026	(24,237)
Equity in net income of affiliates	17,479	25,756	18,447	12,673
Fee income and other	4,956	3,340	539	5,958
Total revenues	$714,168	$673,986	$694,581	$634,724
Income before income tax expense and minority interest	$215,817	$140,832	$138,317	$ (43,877)
Net income	$223,759	$142,484	$139,461	$ 648
Net income per share and share equivalent – basic	$ 1.78	$ 1.15	$ 1.13	$ 0.01
Net income per share and share equivalent – diluted	$ 1.77	$ 1.13	$ 1.10	$ 0.01
1999				
Net premiums earned	$386,753	$414,386	$488,729	$460,138
Net investment income	135,680	132,593	126,560	130,485
Realized gains on investments	67,476	17,584	(12,671)	21,967
Equity in net income (loss) of affiliates	(7,307)	16,642	15,372	16,200
Fee income and other	10,551	3,870	28,800	57,179
Total revenues	$593,153	$585,075	$646,790	$685,969
Income before income tax expense and minority interest	$214,114	$ 28,886	$139,427	$ 48,732
Net income	$209,811	$ 62,708	$137,402	$ 60,588
Net income per share and share equivalent – basic	$ 1.63	$ 0.49	$ 1.08	$ 0.48
Net income per share and share equivalent – diluted	$ 1.58	$ 0.48	$ 1.07	$ 0.47

In the fourth quarter of 2000, the Company incurred after-tax charges of $124.6 million, or $0.98 per share, which included certain reserve adjustments together with employee severance charges and other costs associated with the realignment of the Company's operations and the discontinuation of certain business lines. In the fourth quarter of 1999, the Company incurred after-tax losses of $125.0 million, or $0.97 per share, as a result of two major European windstorms in December 1999. The second quarter of 1999 included charges relating to merger with NAC.

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

22. Unaudited Condensed Pro Forma Financial Information

Unaudited condensed pro forma financial information shown below relates to the Company's acquisition of Mid Ocean in August 1998 and is based upon the assumption that Mid Ocean had been a part of the Company's operations since January 1, 1998.

	Pro Forma 1998
Net premiums earned	$1,588,791
Net investment income	494,389
Net realized gains on sale of investments	260,598
Equity in loss of affiliates	(1,897)
Fee income and other	28,006
Total revenues	2,369,887
Losses and loss expenses	921,018
Acquisition costs and operating expenses	514,877
Interest expense	44,839
Amortization of intangible assets	45,464
Total expenses	1,526,198
Income before minority interest and income tax expense	843,689
Minority interest and income tax	34,535
Net income	$ 809,154
Net income per share	
Basic	$ 6.33
Diluted	$ 6.13
Weighted average shares outstanding (000's)	
Basic	127,883
Diluted	132,036

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

There have been no changes in or any disagreements with accountants regarding accounting and financial disclosure within the twenty-four months ending December 31, 2000.

REPORT OF MANAGEMENT'S RESPONSIBILITIES

Management is responsible for the integrity of the consolidated financial statements and related notes, thereto, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The consolidated financial statements include management's estimates for transactions not yet complete or for which the ultimate effects cannot be precisely determined. Financial information presented elsewhere in this annual report is consistent with that in the consolidated financial statements.

The Company maintains internal accounting controls which have been designed to provide reasonable assurance that all assets are safeguarded against unauthorized use or disposition and that transactions are authorized, executed and recorded properly in accordance with management's authorization. The internal accounting controls are continually reviewed, evaluated and, as appropriate, modified for current conditions.

The Company engages PricewaterhouseCoopers LLP as independent auditors to audit the consolidated financial statements and express an opinion thereon. Their audits include a consideration of the Company's internal controls and systems, the testing of the accounting records and the procedures to the extent considered necessary to support the opinion. PricewaterhouseCoopers LLP has the right of full access to all records and members of management in conducting their audits.

The Audit Committee of the Board of Directors comprises independent directors and meets regularly with PricewaterhouseCoopers LLP to review the strategy and scope and results of the audit work performed. PricewaterhouseCoopers LLP has the right of full access to the Audit Committee, without the presence of management, to discuss any matter they believe should be brought to the attention of the Committee.

BRIAN M. O'HARA
President and Chief Executive Officer

ROBERT R. LUSARDI
Executive Vice President
and Chief Financial Officer

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and
Shareholders of XL Capital Ltd:

In our opinion, based upon our audits and the report of other auditors, the accompanying consolidated balance sheets, the related consolidated statements of income and comprehensive income, of shareholders' equity and of cash flows present fairly, in all material respects, the financial position of XL Capital Ltd and its subsidiaries at December 31, 2000 and 1999, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2000, in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedules listed in Item 14(a) of this Form 10-K, when considered in relation to the basic financial statements taken as a whole, present fairly, in all material respects, the information required to be included therein. These financial statements and financial statement schedules are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements and financial statement schedules based on our audits. We did not audit the financial statements or financial statement schedules of NAC Re Corp. as at December 31, 1998, which statements reflect total revenues of $699.4 million for the year ended December 31, 1998. Those statements were audited by other auditors whose report thereon has been furnished to us, and our opinion expressed herein, insofar as it relates to the amounts included for NAC Re Corp. for that date, is based solely on the report of the other auditors. The consolidated financial statements give retroactive effect to the merger with NAC Re Corp. on July 15, 1999 in a transaction accounted for as a pooling of interests, as described in Note 6 to the consolidated financial statements. We conducted our audits of these statements and schedules in accordance with generally accepted auditing standards in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

We previously audited and reported on the consolidated balance sheets, the related consolidated statements of income and comprehensive income, of shareholders' equity and of cash flows and the supplemental schedules of XL Capital Ltd and its subsidiaries as at and for the year ended November 30, 1998 prior to their restatement for the 1999 pooling of interests and change in fiscal year.

PRICEWATERHOUSECOOPERS LLP

New York, New York
February 15, 2001

CORPORATE SECTION

BOARD OF DIRECTORS & ADVISORY COUNCIL

Ian R. Heap*
Former Chairman, XL Capital Ltd (2) (3)

Brian M. O'Hara
President & Chief Executive Officer
XL Capital Ltd (3) (4)

Michael P. Esposito
Chairman, XL Capital Ltd (3) (4)

Robert J. Newhouse, Jr.**
Former Chairman of the Board
Mid Ocean Limited

Ronald L. Bornhuetter
Former Chairman
NAC Re Corporation (4)

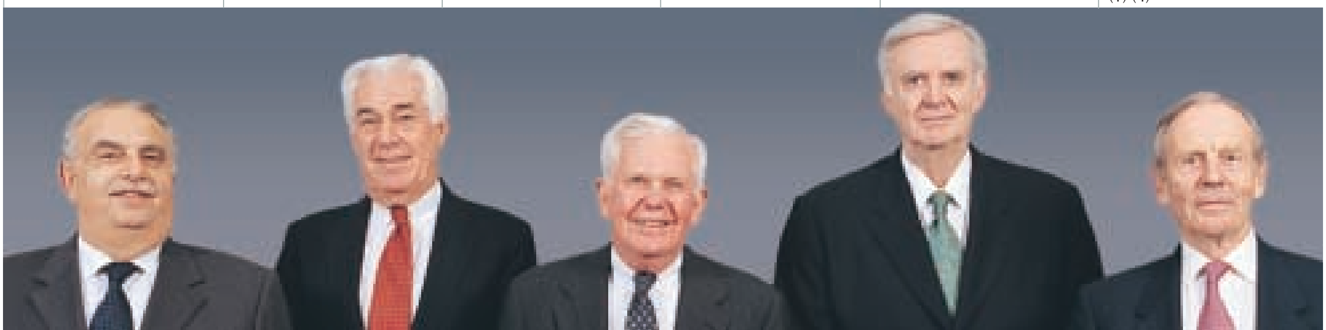
John W. Weiser
Chairman
The Graduate Theological Union (2) (4)

Ellen E. Thrower
President
The College of Insurance (1)

Michael A. Butt
Former President & CEO
Mid Ocean Limited (4)

Alan Z. Senter
Chairman, A Z Senter Consulting, LLC (4)

John T. Thornton
Former Executive Vice President & Financial Executive, Wells Fargo & Co.
(1) (4)



Paul E. Jeanbart
Chief Executive Officer
The Rolaco Group of Companies (1)

Cyril E. Rance
Retired Insurance Executive (1)

Daniel J. McNamara*
Of Counsel
Hughes Hubbard & Reed, LLP (1)

Robert S. Parker
Dean Emeritus & Professor
School of Business Administration, Georgetown University
(3) (4)

Sir F. Brian Corby
Former Chairman of the Board of The Brockbank Group, plc and Prudential Corporation plc
(1)

John Loudon
Chairman
Caneminster Limited
(2) (3) (4)

Robert R. Glauber
President & Chief Executive Officer, NASD (4)

Robert Clements
Chairman
Arch Capital Group Ltd. (3)

* Retiring May 2001
** Advisory Council Member

Committees of the Board:
(1) AUDIT
(2) COMPENSATION
(3) NOMINATING AND CORPORATE GOVERNANCE
(4) FINANCE

OFFICERS

Brian M. O'Hara	*President & Chief Executive Officer*
Nicholas M. Brown, Jr.	*Executive Vice President & Chief Executive* of Insurance Operations
K. Bruce Connell	*Executive Vice President* – Group Underwriting Officer
Jerry de St. Paer	*Executive Vice President & Chief Financial Officer*
Paul S. Giordano	*Executive Vice President, General Counsel & Secretary*
Christopher V. Greetham	*Executive Vice President & Chief Investment Officer*
Henry C.V. Keeling	*Executive Vice President & Chief Executive* of Reinsurance Operations
Fiona E. Luck	*Executive Vice President* of Group Operations
Robert R. Lusardi	*Executive Vice President & Chief Executive* of Financial Products and Services
Clive Tobin	*Executive Vice President*
Gavin R. Arton	*Senior Vice President,* Investor Relations Officer
Anthony E. Beale	*Senior Vice President,* Human Resources
Trevor Brookes	*Senior Vice President,* Internal Audit
William A. Robbie	*Senior Vice President,* Treasurer
Michael A. Siese	*Senior Vice President,* Controller
David B. Walsh	*Senior Vice President,* Chief Credit Officer

CORPORATE INFORMATION

Annual Meeting

The annual meeting of Shareholders of XL Capital Ltd will be held on Friday, May 11, 2001 at the Company's Head Office, XL House, One Bermudiana Road, Hamilton, Bermuda at 8:30 a.m. local time.

Common Stock Data

The Company's common stock, $0.01 par value, was first listed on the New York Stock Exchange on July 19, 1991 under the symbol XL.

The following table sets forth the high and low closing sales prices per share of the Company's Ordinary Shares, as reported on the New York Exchange Composite Tape for the four fiscal quarters of 2000 and 1999.

	2000		1999	
	High	**Low**	High	Low
	$	$	$	$
1st Quarter	**55.375**	**39.563**	75.188	56.750
2nd Quarter	**61.000**	**45.750**	66.500	56.750
3rd Quarter	**78.188**	**54.938**	57.688	42.188
4th Quarter	**88.563**	**69.375**	58.063	44.938

As of December 31, 2000, the approximate number of record holders of Ordinary Shares was 671.

Transfer Agent and Registrar

Mellon Investor Services, 85 Challenger Road, Richfield Park, New Jersey 07660, U.S.A. Shareholders can call into Mellon's Communication Center at 1-800-756-3353 or 1-201-329-8660 or via the Internet at www.mellon-investor.com.

Form 10-K

Form 10-K is filed with the Securities and Exchange Commission. Copies are available without charge by writing to Investor Relations, XL Capital Ltd, P.O. Box HM 2245, Hamilton HM JX, Bermuda.

Auditors

PricewaterhouseCoopers LLP, 1177 Avenue of the Americas, New York, NY 10019-6013, U.S.A.

Legal Counsel

Hunter & Hunter, The Hunt Law Building, P.O. Box 190 GT, Grand Cayman, Cayman Islands.

Cahill Gordon & Reindel, Eighty Pine Street, New York, NY 10005, U.S.A.

Registered Office

c/o Hunter & Hunter, The Hunt Law Building, P.O. Box 190 GT, Grand Cayman, Cayman Islands.

XL Capital Ltd

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