

LANCASHIRE HOLDINGS LIMITED

PROPOSED ACQUISITION OF CATHEDRAL CAPITAL LIMITED

7 August 2013

For immediate release

Today the board of directors (the “**Board**”) of Lancashire Holdings Limited (“**Lancashire**” or the “**Company**”) announces that it has entered into conditional agreements to acquire the entire issued and to be issued share capital of Cathedral Capital Limited (“**Cathedral**”), a privately owned Lloyd’s insurer, from Alchemy Partners and Cathedral management, together with loan notes issued by Cathedral’s subsidiary, Cathedral Capital (Investments) Limited for £266m, representing a multiple of 1.60x net tangible assets¹ of Cathedral as at 31 March 2013 (the “**Acquisition**”).

The consideration for the Acquisition will be satisfied by the payment of £266 million in cash on completion to Alchemy Partners and the other Cathedral shareholders, funded through a combination of internally available cash resources and the net proceeds of the placing of up to 16,843,382 new common shares in the Company, representing approximately 9.99% of the Company’s existing issued share capital, with institutional investors (the “**Placing**”).

The Board believes that Lancashire’s and Cathedral’s existing businesses are a strong complementary fit and expects the Acquisition to bring material benefits to the enlarged Lancashire Group following the Acquisition (the “**Enlarged Group**”). The transaction represents a rare opportunity to acquire a high-quality Lloyd’s business with a short-tail focus, strong business model fit and robust underwriting performance. The Enlarged Group will have access to an enhanced insurance and reinsurance platform and will benefit from direct participation in Lloyd’s, the world’s leading specialist insurance market. The Acquisition further provides Lancashire with flexibility to respond to the changing industry and market environment which increasingly requires multiple distribution capability.

Lancashire remains committed to its core strategic objectives. Cathedral is an underwriter-led and highly streamlined business with a track-record of excellence that is well aligned to Lancashire’s strategic priority of “underwriting comes first” and nimble operating approach. The acquisition provides Lancashire with scale in existing lines of business and opportunities for further organic growth.

Transaction highlights:

- ***The combination of Lancashire and Cathedral is expected to offer shareholders greater value, accretive growth and an enhanced return profile, at a time of change in the market.*** Maximising long-term risk-adjusted return remains Lancashire’s key focus and the transaction is expected to enhance Lancashire’s growth in fully-converted book value per share and risk-adjusted return. The Acquisition is expected to enhance Lancashire’s

¹ Including shareholders’ equity together with total preference shares and loan notes outstanding

competitive positioning and ability to win new business from clients and brokers, as well as bringing enhanced capital management and efficiency to Cathedral. Lancashire will also look to take advantage of capital and operational efficiencies from writing new business through the Lloyd's platform.

- ***The Acquisition will provide Lancashire with a platform at Lloyd's, the world's leading specialist insurance market.*** Lloyd's global access will provide Lancashire with the opportunity to expand into new business markets through Lloyd's existing licences. Access to Lloyd's market infrastructure and support services, coupled with capital benefits from Lloyd's strong financial rating, make the Acquisition a compelling proposition.
- ***The combination will strengthen Lancashire's core underwriting competencies and diversify exposure to specialty lines.*** Cathedral's strong underwriting track record across core business lines will enhance Lancashire's positioning in certain specialty lines with minimal overlap whilst building scale in existing lines.
- ***Lancashire's ability to operate a nimble capital management strategy will be further enhanced through the capital benefits from the Lloyd's Central Fund and Lloyd's financial ratings support.*** By retaining Lloyd's Names' participation in the Cathedral Syndicate 2010, Lancashire will continue to leverage third party capital to explore attractive new business opportunities and generate attractive fee income. The Board believes that the Acquisition provides a more sustainable business model in the event of a prolonged soft market plus the ability to leverage an additional operating platform in a hard market.
- ***The Acquisition has an attractive financial impact for the Enlarged Group as it is expected to be both book value and earnings accretive in the first year.*** The Acquisition represents an opportunity of digestible size and Lancashire expects the integration challenges to be manageable.

Information on Cathedral

Cathedral is an established specialty (re)insurance provider that operates exclusively in the Lloyd's insurance market and writes insurance and reinsurance business in property, direct and facultative property, aviation, satellite, marine cargo and contingency classes. Operating within the Lloyd's framework, Cathedral benefits from Lloyd's recognised status as the world's specialist insurance market, its security rating, worldwide licences and attractive capital regime.

Cathedral is London based and operates as an Integrated Lloyd's Vehicle which comprises a managing agent and two syndicates, Syndicate 2010 and Syndicate 3010. For the 2013 year of account, Cathedral owns 57.8% of the capacity on Syndicate 2010 and 100% of the capacity on Syndicate 3010. The remaining capacity (42.2%) on Syndicate 2010 is owned by Lloyd's Names, from which Cathedral receives ancillary income in the form of annual fees and profit commissions for the underwriting services it provides. For the 2012 year of account, Syndicate 2010 and Syndicate 3010 had underwriting capacity of £350 million and £30 million respectively.

In 2012, the syndicates had, in aggregate, £193m of gross written premium (on a group share basis). Property reinsurance, direct and facultative reinsurance and aviation reinsurance represented over 80% of Cathedral's portfolio.

Cathedral believes it has long standing relationships with its clients and brokers which allows it to write a diversified and seasoned portfolio across all of its core business lines. The business has experienced consistent growth in book value across the cycle (13% per annum since 2008), despite significant international property catastrophe market loss experience in 2010 and 2011.

The Cathedral group's main lines of business are summarised below:

- **Property Reinsurance** (£80.9m / 41.9% Cathedral 2012 GWP)
 - Largely international catastrophe and risk excess business with a US focus and a core book of small regional clients
 - 60% of the US property reinsurance cedents have been clients for over 20 years
 - Average net loss ratio of 65% in last 5 years of account
- **Direct and Facultative Property** (£62.5m / 32.3% Cathedral 2012 GWP)
 - Worldwide short-tail book with US bias, focusing on small / mid-sized business (90% with lines under \$5m)
 - Substantial binder account (c. 43% of income) with strong repeat business characteristics
 - Average net loss ratio of 60% in last 5 years of account
- **Aviation/Satellite** (£18.2m / 9.4% Cathedral 2012 GWP)
 - One of the major aviation reinsurance leaders world-wide with a focus on small, non-US portfolios
 - Other sub classes are retrocessional excess of loss, airline quota share, general aviation business, hull/war, war third party legal liability and satellite
 - Satellite business written primarily through SATEC, a relationship held over 15+ years
 - 5 year average net loss ratio in last 5 years of account of 53% and 52% on aviation and satellite accounts respectively
- **Contingency** (£3.4m / 1.7% Cathedral 2012 GWP)
 - Focused on music cancellation with strong reinsurance protection
 - Increasing focus on smaller clients away from the highly competitive music tours and festivals
 - Average net loss ratio of 49% in last 5 years of account
- **Cargo** (£28.3m / 14.6% Cathedral 2012 GWP)
 - Comprises over 90% of Syndicate 3010's business and includes specie (11% of GWP), fine art (5% GWP) and war (2% GWP)
 - Worldwide direct and reinsurance portfolio with pure cargo business representing 82% of the account
 - Average net loss ratio of 59% in last 5 years of account

In 2012, Cathedral reported operating profit before tax and financing costs of £24.9m and profit after tax of £11.6m on an IFRS basis, with an overall combined ratio of 83.4% (including its share of the Syndicates and non-underwriting corporate expenses net of other fees and income). The corporate investment return for the year was a profit of £3.7m which equates to a return of 1.9%. As at 31 December 2012, Cathedral had equity shareholders' funds of £54.7m and reported a return on equity of 26.9%. Further financial information on Cathedral Capital,

including latest 2012 audited financial accounts, can be accessed via their website at <http://www.cathedralcapital.com/>.

Financial effects:

The Acquisition is expected to be accretive to earnings and book value in the first year, with a pro forma book value of U.S.\$1,455m as at 30 June 2013. The pro forma tangible book value of the Lancashire Group as at 30 June 2013 is U.S.\$1,298m. The Enlarged Group's gearing following the Acquisition is maintained within management's appetite at 19.7%. The Board believes that there is potential further upside arising from more efficient capital management of the Cathedral business and Lancashire will work together with the Cathedral management team to explore these options further. Lancashire remains committed to its current dividend and capital management strategy and expects the Acquisition will deliver enhanced dividend capacity in the future.

Management and employees:

Cathedral has a strong underwriter-led management team with an excellent track-record and substantial experience in the Lloyd's market. Following completion of the Acquisition, Cathedral will continue to be run by its existing senior management team. Lancashire recognises the importance of the skills and experience of the existing management and employees of Cathedral and believes that they will be an important factor for continuing the success of Cathedral's business under Lancashire ownership.

Lancashire will accordingly put in place appropriate retention and incentivisation arrangements to ensure a smooth transition and appropriate recognition. The incentive arrangements will have a performance element, to be satisfied based on Lancashire share awards. The retention and incentive arrangements span over a period of approximately 5 years.

Lancashire plans do not involve any changes to the terms and conditions of employment of the Cathedral employees, nor are there any plans to change the location of Cathedral's business. The transaction will bring on board 14 underwriters with significant sector knowledge and experience. Lancashire plans to integrate Cathedral underwriting controls and Cathedral management is to be fully represented at Lancashire's ongoing fortnightly Risk and Reward Committee.

Current trading:

Lancashire published its Second Quarter 2013 Press Release as supplemented by the Second Quarter 2013 Financial Supplement in respect of the six month period to 30 June 2013 on 25 July 2013. Lancashire is of the view that there has been no significant change to the Group's trading and prospects since that date.

Cathedral's underwriting portfolio has performed well in the year to date and profitability was running ahead of target at the half year point of 30 June 2013. Cathedral's older underwriting years continue to mature well. Whilst general trading conditions remain competitive, Cathedral has the benefit of a good long standing business in highly focussed underwriting areas. Given

the nature of exposures within the reinsurance lines it writes, the results for the full year to 31 December 2013 will depend on second half loss activity.

Financing the Acquisition:

The Company intends to fund the Acquisition and associated expenses through a combination of the proceeds from the Placing of approximately £130m and the balance from internally available cash resources.

Completion of the Acquisition:

Completion of the Acquisition is conditional, amongst other things, on

- (i) approval being received from the Prudential Regulatory Authority, the Financial Conduct Authority and Lloyd's of London; and
- (ii) approval being received from the shareholders of the Company.

A Special General Meeting of the Company will be held in connection with the Acquisition and a shareholder circular incorporating the notice of Special General Meeting (together with the Form of Proxy and the Form of Direction, the "**Circular**") is expected to be posted to shareholders on or around 9 August 2013.

J.P. Morgan Cazenove is acting as sole financial advisor and sponsor to Lancashire with respect to the Acquisition. Kinmont and Willis Capital Markets & Advisory are advising Cathedral.

Commenting on the Acquisition, Lancashire's Chief Executive Officer, Richard Brindle said:

"Subject to shareholder and regulatory approval, I am delighted to announce that Lancashire has acquired Cathedral Capital which owns two top-performing syndicates in Lloyd's. We've spent a good deal of time with the management team looking at the Cathedral business and we've been impressed with their record and their approach.

The deal will broaden our business line exposure, and strengthens and diversifies our core underwriting. In addition it will allow us to continue our track record of financial flexibility and efficient capital management.

As you know we've been talking a lot this year about how important it is to remain relevant in such a rapidly changing marketplace. With LICL² and LUK³ operating nimbly in the London and Bermuda company markets, Kinesis developing our capital markets presence, and now Cathedral with an established and successful Lloyd's business, we have excellent distribution channels for all our classes and clients.

² Lancashire Insurance Company Limited

³ Lancashire Insurance Company (UK) Limited

My colleagues and I extend a warm welcome to Peter and the whole Cathedral team. We're enthusiastic about the opportunities to develop both the Lancashire and Cathedral business and to serve our clients and brokers even better."

Commenting on the Acquisition, Cathedral's Chief Executive Officer, Peter Scales said:

"I am delighted that we have successfully reached the conclusion of our sale process and will be taking our business forward within the Lancashire Group.

The aim of our process was to put Cathedral in a position where it could develop and build out the business within a wider capital base, with a shared underwriting and customer philosophy that is commensurate with the changing market place in which we find ourselves.

Whilst it will continue to be very much business as usual at Cathedral from a day to day trading perspective, I am excited by the additional value that we can bring to the existing Lancashire underwriting and third party capital business and the value they will bring to building out the Cathedral platform.

I believe that our business is not only going to thrive in its new home, but it is now part of a group where the shared experience and values of the teams, coupled with the flexibility of the wider platform, gives us a highly effective structure that is suited to take on the challenges of a changing market place.

On a personal note I would like to thank Richard and his team for the honest, direct and enthusiastic approach they exhibited through the process, which not only made the choice of new home easier but bodes very well for moving forward together."

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An analyst meeting will be held at the City Suite, Apex Hotel, 1 Seething Lane, London, EC3N 4AX at 9:30am. Dial-in facilities are available — UK Toll Number: 02031394830 / UK Toll Free Number: 08082370030 / Participant Pin Code: 91231278#

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