-CONFIDENTIAL-

LANCASHIRE HOLDINGS LIMITED

unaudited interim consolidated financial statements

for the six month period ended june 30, 2006

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INDEPENDENT REVIEW REPORT

TO THE SHAREHOLDERS

LANCASHIRE HOLDINGS LIMITED

Introduction

We have been instructed by the Lancashire Holdings Limited (the "Company") to review the financial information for the six months ended 30 June 2006 which comprises of the Consolidated Income Statement, Consolidated Balance Sheet, Consolidated Cash Flow Statement, Consolidated Statement of Changes in Equity and the related notes 1 to 28. We have read the other information contained in the interim report and considered whether it contains any apparent misstatements or material inconsistencies with the financial information.

This report is made solely to the Company having regard to guidance contained in International Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity". To the fullest extent permitted by the law, we do not accept or assume responsibility to anyone other than the Company, for our work, for this report, or for the conclusions we have formed.

Directors' responsibilities

The interim report, including the financial information contained therein, is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the interim report as required by the AIM Rules issued by the London Stock Exchange.

Review work performed

We conducted our review in accordance with International Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity". A review consists principally of making enquiries of management and applying analytical procedures to the financial information and underlying financial data, and based thereon, assessing whether the accounting policies and presentation have been consistently applied, unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit performed in accordance with International Standards on Auditing and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the financial information.

Review conclusion

On the basis of our review we are not aware of any material modifications that should be made to the financial information as presented for the six months ended 30 June 2006.

Ernst + Young

Chartered Accountants

August 2, 2006

consolidated income statement
for the period ended june 30, 2006

	notes	2006 $m	2005 $m
gross premiums written		316.3	2.6
outwards reinsurance premiums		(71.0)	-
net premiums written		**245.3**	**2.6**
change in unearned premiums		(241.4)	(2.6)
change in unearned premiums on premium ceded		60.4	-
net premiums earned		**64.3**	**-**
net investment income	3	24.2	2.1
net realised gains (losses)	3	(3.4)	-
net foreign exchange gains (losses)		(1.1)	0.3
total net revenue		**84.0**	**2.4**
insurance losses and loss adjustment expenses		7.4	-
insurance losses and loss adjustment expenses recoverable		-	-
net insurance losses		**7.4**	**-**
insurance acquisition expenses	4	7.6	-
other operating expenses	5, 6	24.2	10.0
total expenses		**39.2**	**10.0**
results of operating activities		**44.8**	**(7.6)**
finance costs		5.5	4.0
profit (loss) before tax		**39.3**	**(11.6)**
tax		-	-
profit (loss) for the period attributable to equity shareholders		**39.3**	**(11.6)**
earnings per share			
basic	23	$0.20	$(0.24)
diluted	23	$0.20	$(0.24)

consolidated balance sheet
as at june 30, 2006

	notes	2006 $m	2005 $m
assets			
cash and cash equivalents	9	215.0	1,072.4
accrued interest receivable	13	7.9	2.0
investments			
- fixed income securities	10	866.5	-
- equity securities	10	86.9	-
reinsurance assets			
- unearned premium on premium ceded	12	60.4	-
deferred acquisition costs	14	29.7	0.5
other receivables	13	80.6	0.3
inwards premium receivable from insureds and cedants	13	165.0	2.1
investment in associate	11	20.0	-
property, plant and equipment	17	0.6	0.4
total assets		**1,532.6**	**1,077.7**
liabilities			
insurance contracts			
- losses and loss adjustment expenses	12	7.4	-
- unearned premiums	12	244.0	2.6
amounts payable to reinsurers	12, 15	32.0	-
deferred acquisition costs ceded	16	5.6	-
other payables	15	124.7	2.2
accrued interest payable	18	0.5	0.4
long-term debt	18	127.1	125.4
total liabilities		**541.3**	**130.6**
shareholders’ equity			
share capital	20	97.9	97.9
share premium		871.4	860.8
fair value and other reserves	3	(5.7)	-
retained earnings (deficit)		27.7	(11.6)
total shareholders' equity attributable to equity shareholders		**991.3**	**947.1**
total liabilities and shareholders' equity		**1,532.6**	**1,077.7**

consolidated statement of changes in equity
for the six months ended june 30, 2006

	notes	share capital $m	share premium $m	fair value and other reserves $m	retained (deficit) earnings $m	total $m
balance as at october 12, 2005 (date of incorporation)		-	-	-	-	-
loss for the period		-	-	-	(11.6)	(11.6)
total recognised income for the period		**-**	**-**	**-**	**(11.6)**	**(11.6)**
issue of share capital	20	97.9	880.7	-	-	978.6
equity offering expenses		-	(58.6)	-	-	(58.6)
formation expenses		-	(36.1)	-	-	(36.1)
warrant issues - founders & sponsor	21	-	66.4	-	-	66.4
warrant issues - management	6	-	8.4	-	-	8.4
balance as at december 31, 2005		**97.9**	**860.8**	**-**	**(11.6)**	**947.1**
profit for the period		-	-	-	39.3	39.3
change in investment unrealised gains (losses)	3	-	-	(5.7)	-	(5.7)
total recognised income for the period		**-**	**-**	**(5.7)**	**39.3**	**33.6**
warrant issues - management and performance	6	-	9.8	-	-	9.8
options issues - management	6	-	0.8	-	-	0.8
balance as at june 30, 2006		**97.9**	**871.4**	**(5.7)**	**27.7**	**991.3**

consolidated cash flow statement
for the six months ended june 30, 2006

	notes	2006 $m	2005 $m
cash flows from operating activities			
profit (loss) before interest income and expense		19.4	(13.3)
interest income		25.0	2.1
interest expense		(5.1)	(0.4)
employee benefits expense	5	10.6	8.4
foreign exchange		1.1	(0.3)
realised (gains) losses on investments	3	3.4	-
accrued interest receivable		(5.9)	(2.0)
unearned premium on premium ceded		(60.4)	-
deferred acquisition costs		(29.2)	(0.5)
other receivables		(80.3)	(0.3)
inwards premium receivable from insureds and cedants		(162.6)	(2.1)
losses and loss adjustment expenses		7.4	-
unearned premiums		241.4	2.6
amounts payable to reinsurers		32.0	-
deferred acquisition costs ceded		5.6	-
other payables		122.4	1.3
accrued interest payable		0.1	0.4
net cash flows from (used in) operating activities		**124.9**	**(4.1)**

cash flows from investing activities			
purchase of property, plant and equipment	17	(0.3)	(0.4)
investment in associates	11	(20.0)	-
purchase of debt securities		(1,531.2)	-
purchase of equity securities		(85.5)	-
proceeds on maturity and disposal of debt securities		653.1	-
proceeds on disposal of equity securities		1.3	-
net cash flows used in investing activities		**(982.6)**	**(0.4)**

cash flows from financing activities			
proceeds from issue of share capital		-	978.6
transaction costs from issue of share capital		-	(12.2)
formation expenses		-	(15.2)
proceeds from issue of long-term debt		-	125.7
net cash flows from financing activities		**-**	**1,076.9**

net (decrease) increase in cash and cash equivalents		**(857.7)**	**1,072.4**
cash and cash equivalents at beginning of period		1,072.4	-
effect of exchange rate fluctuations on cash and cash equivalents		0.3	-
cash and cash equivalents at end of period		**215.0**	**1,072.4**

summary of significant accounting policies

The basis of preparation, consolidation principles and significant accounting policies adopted in the preparation of Lancashire Holdings Limited ("LHL") and its subsidiaries' (collectively "the Group") interim consolidated financial statements are set out below. The interim consolidated financial statements for the six months ended June 30, 2006 have not been audited.

basis of preparation

Given the significant development in the Group's business from the last audited consolidated financial statements, condensed interim consolidated financial statements have not been presented. As management's preference is to share these developments with shareholders and other users, the Group's interim consolidated financial statements are prepared in accordance with accounting principles generally accepted under International Financial Reporting Standards ("IFRS") endorsed by the European Commission. Subsequent interim period statements may be prepared in accordance with IAS 34: Interim Financial Reporting.

Where IFRS is silent, as it is in respect of the measurement of insurance products, the IFRS framework allows reference to another comprehensive body of accounting principles. In such instances, management determine appropriate measurement bases, to provide the most useful information to users of the interim consolidated financial statements, using their judgment and considering the accounting principles generally accepted in the United States ("US GAAP").

Comparative figures have been presented for the period from October 12, 2005, the date of incorporation, to December 31, 2005, as the Group was not in existence at June 30, 2005.

The new IFRS 7, Financial Instruments Disclosure, which has been issued but is not yet effective, has not been applied. IFRS 7 is not expected to have a material impact on the results reported in the interim consolidated financial statements.

The interim consolidated balance sheet of the Group is presented in order of decreasing liquidity.

use of estimates

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported and disclosed amounts at the balance sheet date and the reported and disclosed amounts of revenues and expenses during the reporting period. Actual results may differ materially from the estimates made.

basis of consolidation

i. subsidiaries

The Group's interim consolidated financial statements include the assets, liabilities, equity, revenues, expenses and cash flows of Lancashire Holdings Limited and its subsidiaries. A subsidiary is an entity in which the Group owns, directly or indirectly, more than 50% of the voting power of an entity or otherwise has the power to govern the operating and financial policies. The results of subsidiaries acquired are included in the interim consolidated financial statements from the date on which control is transferred to the Group. Intercompany balances, profits and transactions are eliminated.

Subsidiaries' accounting policies are consistent with the Group's accounting policies.

ii. associates

Investments in which the Group has significant influence over the operational and financial policies of the investee, are initially recognised at cost and thereafter accounted for using the equity method. Under this method, the Group records its proportionate share of income or loss from such investments in its results of operations for the period. Adjustments are made to associates' accounting policies, where necessary, in order to be consistent with the Group's accounting policies.

foreign currency translation

The functional currency for all Group entities is United States ("U.S.") dollars. The interim consolidated financial statements are presented in U.S. dollars. Items included in the financial statements of each of the Group's entities are measured using the functional currency, which is the currency of the primary economic environment in which operations are conducted.

Foreign currency transactions are recorded in the functional currency for each entity using the exchange rates prevailing at the dates of the transactions, or at the average rate for the period when this is a reasonable approximation. Monetary assets and liabilities denominated in foreign currencies are translated at period end exchange rates. The resulting exchange differences on translation are recorded in the interim consolidated income statement. Non-monetary assets and liabilities carried at historical cost denominated in a foreign currency are translated at historic rates. Non-monetary assets and liabilities carried at fair value denominated in a foreign currency are translated at the exchange rate at the date the fair value was determined, with resulting exchange differences recorded in the fair value reserves in shareholders' equity.

insurance contracts

i. classification

Insurance contracts are those contracts that transfer significant insurance risk at the inception of the contract. Contracts that do not transfer significant insurance risk are accounted for as investment contracts. Insurance risk is transferred when an insurer agrees to compensate a policyholder if a specified uncertain future event adversely affects the policyholder.

ii. premiums and acquisitions costs

Premiums are first recognised as written at the date that the contract is bound. The Group writes both excess of loss and pro-rata contracts. For the majority of excess of loss contracts, written premium is recorded based on the minimum and deposit or flat premium, as defined in the contract. Subsequent adjustments to the minimum and deposit premium are recognised in the period in which they are determined. For pro-rata contracts and excess of loss contracts where no deposit is specified in the contract, written premium is recognised based on estimates of ultimate premiums provided by the insureds or ceding companies. Initial estimates of written premium are recognised in the period in which the underlying risks incept. Subsequent adjustments, based on reports of actual premium by the insureds or ceding companies, or revisions in estimates, are recorded in the period in which they are determined.

Premiums are earned ratably over the term of the underlying risk period of the reinsurance contract, except where the period of risk differs significantly from the contract period. In these circumstances, premiums are recognised over the period of risk in proportion to the amount of insurance protection provided. The portion of the premium related to the unexpired portion of the risk period is reflected in unearned premium.

Where contract terms require the reinstatement of coverage after a ceding company's loss, the mandatory reinstatement premiums are recorded as written premium when the loss event occurs.

Inwards premiums receivable from insureds and cedants are recorded net of commissions, brokerage, premium taxes and other levies on premiums. These balances are reviewed for impairment, with any impairment loss recognised in income in the period in which they are determined.

Acquisition costs represent commissions, brokerage and other variable costs that relate directly to the securing of new contracts and the renewing of existing contracts. They are deferred over the period in which the related premiums are earned, to the extent they are recoverable out of future revenue margins. All other acquisition costs are recognised as an expense when incurred.

iii. outwards reinsurance

Outwards reinsurance premiums comprise the cost of reinsurance contracts entered into. Outwards reinsurance premiums are accounted for in the period in which the underlying risks incept. The provision for reinsurers' share of unearned premiums represents that part of reinsurance premiums written which is estimated to be earned in future financial periods. Unearned reinsurance commissions are recognised as a liability using the same principles. Any amounts recoverable from reinsurers are estimated using the same methodology as the underlying losses.

The Group monitors the credit worthiness of its reinsurers on an ongoing basis and assesses any reinsurance assets for impairment, with any impairment loss recognised in income in the period in which it is determined.

iv. losses

Losses comprise losses and loss adjustment expenses paid in the period and changes in the provision for outstanding losses, including the provision for losses incurred but not reported ("IBNR") and related expenses. Losses and loss adjustment expenses are charged to income as they are incurred and are mainly external costs related to the negotiation and settlement of claims.

A significant portion of the Group's business is property catastrophe and other classes with high attachment points of coverage. Reserving for losses in such programs is inherently complicated in that losses in excess of the attachment level of the Group's policies are characterised by high severity and low frequency and other factors which could vary significantly as losses are settled. This limits the volume of industry loss experience available from which to reliably predict ultimate losses following a loss event. In addition, the Group has limited past loss experience due to its short operating history, which increases the inherent uncertainty in estimating ultimate loss levels.

Losses and loss adjustment expenses represent the estimated ultimate cost of settling all losses and loss adjustment expenses arising from events which have occurred up to the balance sheet date, including a provision for IBNR. The Group does not discount its liabilities for unpaid losses. Outstanding losses are initially set on the basis of reports of losses received from third parties. Estimated IBNR reserves consist of a provision for additional development in excess of case reserves reported by ceding companies or insureds, as well as a provision for losses which have occurred but which have not yet been reported to us by ceding companies or insureds. IBNR reserves are estimated by management using various actuarial methods as well as a combination of our own loss experience, historical insurance industry loss experience, our underwriters' experience, estimates of pricing adequacy trends, and management's professional judgment. The Group's internal actuaries review the reserving assumptions and methodologies on a quarterly basis and the Group's loss estimates are subject to a semi-annual corroborative review by independent actuaries using generally accepted actuarial principles.

The estimation of the ultimate liability arising is a complex and judgmental process. It is reasonably possible that uncertainties inherent in the reserving process, delays in insureds or ceding companies reporting losses to the Group, together with the potential for unforeseen adverse developments, could lead to a material change in losses and loss adjustment expenses.

v. liability adequacy tests

At each balance sheet date, the Group performs a liability adequacy test using current best estimates of future cash flows generated by its insurance contracts, plus any investment income thereon. If, as a result of these tests, the carrying amount of the Group's insurance liabilities is found to be inadequate, the deficiency is charged to the consolidated income statement for the period initially by writing off deferred acquisition costs and subsequently by establishing a provision.

cash and cash equivalents

Cash and cash equivalents are carried in the interim consolidated balance sheet at cost and includes cash in hand, deposits held on call with banks and other short-term highly liquid investments with a maturity of three months or less at the date of purchase. Carrying amounts approximate fair value due to the short term nature of the instruments.

Interest income earned on cash and cash equivalents is recognised on the effective interest rate method. The carrying value of accrued interest income approximates fair value due to its short term nature.

investments

The Group's fixed income and equity investments are classified as available for sale and are carried at fair value. Other investments are recorded at estimated fair value based on financial information received and other information available to management, including factors restricting the liquidity of the investments. Regular way purchases and sales of investments are recognised at fair value less transaction costs on the trade date and are subsequently carried at fair value. Estimated fair value of quoted investments is determined based on bid prices from recognised exchanges. Investments are derecognised when the Group has transferred substantially all of the risks and rewards of ownership. Realised gains and losses are included in income in the period in which they arise. Unrealised gains and losses from changes in fair value are included in the fair value reserve in shareholders' equity. On derecognition of an investment, previously recorded unrealised gains and losses are removed from shareholders' equity and included in current period income.

Amortisation and accretion of premiums and discounts are calculated using the effective interest rate method and are recognised in current period net investment income. Dividends on equity securities are recorded as revenue on the date the dividends become payable to the holders of record. The carrying value of accrued interest income approximates fair value due to its short term nature.

The Group reviews the carrying value of its investments for evidence of impairment. An investment is impaired if its carrying value exceeds the estimated recoverable amount and there is objective evidence of impairment to the asset. Such evidence would include a prolonged decline in fair value below cost or amortised cost, where other factors do not support a recovery in value. If an impairment is deemed appropriate, the difference between cost or amortised cost and fair value is removed from the fair value reserve in shareholders' equity and charged to current period income.

Impairment losses on equity securities are not subsequently reversed.

derivative financial instruments

Derivatives are recognised at fair value on the date a contract is entered into, the trade date, and are subsequently carried at fair value. Derivative instruments with a positive value are recorded as derivative financial assets and those with a negative value are recorded as derivative financial liabilities.

Derivative financial instruments include swap, option, forward and future contracts. They derive their value from the underlying instrument and are subject to the same risks as that underlying instrument, including liquidity, credit and market risk. Fair values are based on exchange quotations, with changes in the fair value of instruments that do not qualify for hedge accounting recognised in current period income.

Derivative financial assets and liabilities are offset and the net amount reported in the interim consolidated balance sheet only to the extent there is a legally enforceable right of offset and there is an intention to settle on a net basis, or to realise the assets and liabilities simultaneously.

property, plant and equipment

Property, plant and equipment is carried at historical cost, less accumulated depreciation and any impairment in value. Depreciation is calculated to write-off the cost over the established useful economic life on a straight-line basis as follows:

IT equipment	33% per annum
Office furniture and equipment	33% per annum
Leasehold improvements	20% per annum

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

An item of property, plant or equipment is derecognised on disposal or when no future economic benefits are expected to arise from the continued use of the asset.

Gains and losses on the disposal of property, plant and equipment are determined by comparing proceeds with the carrying amount of the asset, and are included in the income statement. Costs for repairs and maintenance are charged to the consolidated income statement as incurred.

long term debt

Long-term debt is recognised initially at fair value, net of transaction costs incurred. Thereafter it is held at amortised cost, with the amortisation calculated using the effective interest rate method.

leases

Rentals payable under operating leases are charged to income on a straight-line basis over the lease term.

employee benefits

i. equity compensation plans

The Group operates a management warrant plan and an option plan. The fair value of the equity instrument granted is estimated on the date of grant. The fair value is recognised as an expense pro-rata over the vesting period of the instrument. The total amount to be expensed is determined by reference to the fair value of the awards estimated at the grant date, excluding the impact of any non-market vesting conditions.

At each balance sheet date, the Group revises its estimate of the number of warrants and options that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the consolidated income statement, and a corresponding adjustment is made to shareholders' equity over the remaining vesting period.

On vesting or exercise, the differences between the expense charged to the consolidated income statement and the actual cost to the Group is transferred to retained earnings. Where new shares are issued, the proceeds received are credited to share capital and share premium.

ii. pensions

The Group operates a defined contribution plan. On payment of contributions to the plan there is no further obligation to the Group. Contributions are recognised as employee benefits in the consolidated income statement in the period to which they relate.

founder and sponsor warrants

The Group issued warrants to certain founding shareholders and a sponsor on listing. The fair value of the equity instruments granted were estimated on the date of grant.

Warrants issued to founding shareholders were treated as a capital transaction and the associated fair value was credited to the share premium account. The fair value of warrants issued to the sponsor for assistance with incorporation and other start-up services was credited to the share premium account. The total amount to be credited was determined by reference to the fair value of the awards estimated at the grant date, excluding the impact of any non-market vesting conditions.

taxation

Income tax expense represents the sum of the tax currently payable and any deferred tax. The tax payable is calculated based on taxable profit for the period. Taxable profit for the period can differ from that reported in the consolidated income statement due to certain items which are not tax deductible or which are deferred to subsequent periods.

Deferred tax is recognised on differences between the assets and liabilities in the consolidated balance sheet and their tax base. Deferred tax assets or liabilities are accounted for using the balance sheet liability method.

risk disclosures: introduction

The Group enters into contracts that directly accept and transfer insurance risk. This in turn creates exposure for the Group to insurance risk and financial risk.

The Group's appetite for accepting risk is established by the Board of Directors. The management of risks is described below.

A. insurance risk

The Group underwrites contracts that transfer insurance risk. The Group's underwriters assess the likely losses using their experience and knowledge of past loss experience and current circumstances. This allows them to estimate the premium sufficient to meet likely losses and expenses. The Group considers insurance risk at an individual contract level and at an aggregate portfolio level. The Group's exposure in connection with such contracts is, in the event of insured losses, whether premium will be sufficient to cover the loss payments and expenses.

The Group underwrites worldwide short tail insurance and reinsurance property risks, including risks exposed to natural catastrophes. The four principal classes are property, energy, marine and aviation. The Group does not currently underwrite a material amount of casualty business. The level of risk tolerance per class is set by the Board of Directors, who delegate day to day responsibility to senior management.

A number of controls are deployed to limit the amount of insurance exposure underwritten:

- A business plan is produced annually which targets premium by class
- The business plan is monitored and reviewed on an on-going basis
- Each authorised class has a pre-determined normal maximum line structure proposed by management and agreed by the Board
- The Group has a pre-determined target limit on probabilistic loss of capital for certain catastrophic events
- A daily underwriting meeting is held to peer review all risks
- Sophisticated pricing models are utilised in the underwriting process, and are updated frequently to latest versions
- Computer modeling tools are deployed to simulate catastrophes and resultant losses to the portfolio
- Reinsurance is purchased to mitigate losses in peak areas of exposure

The Group has established an internal audit function which is independent of the underwriting process. The head of internal audit reports directly to the Audit Committee. The internal audit function is required to perform risk reviews on the underwriting function to ensure compliance with Group policies and required procedures.

The Group establishes targets for the maximum proportion of capital, including long term debt, that can be lost in a single extreme event. As of June 30, 2006, the impact of a 1 in 100 year U.S. hurricane event was 20% of capital, after collection of reinsurance and after payment and collection of reinstatement premiums. There can be no guarantee that the assumptions and techniques deployed in calculating this figure are accurate. There could also be an unmodeled loss which exceeds these figures. In addition, a loss with an occurrence probability of greater than 1 in 100 years could cause a larger loss to capital.

The Group commenced underwriting in December 2005, but wrote an insignificant amount of business for the period from incorporation to December 31, 2005. Comparatives have therefore not been presented in the analysis provided in section A: insurance risk.

Details of gross premiums written by line of business are provided below for the six month period ending June 30, 2006:

	$m	%
property	129.4	40.9
energy	151.2	47.8
marine	21.7	6.9
aviation	14.0	4.4
total	**316.3**	**100.0**

Details of gross premiums written by geographic area of risks insured are provided below for the six month period ending June 30, 2006:

	$m	%
worldwide offshore	111.8	35.3
USA and Canada	79.5	25.1
worldwide [(1)]	76.2	24.1
worldwide, excluding the US [(2)]	25.2	8.0
middle east	6.5	2.1
far east	6.1	1.9
others	11.0	3.5
total	**316.3**	**100.0**

(1) Worldwide comprises insurance and reinsurance contracts that insure or reinsure risks in more than one geographic area.
(2) Worldwide, excluding the U.S. comprises insurance and reinsurance contracts that insure or reinsure risks in more than one geographic area, but that specifically exclude the United States of America and Canada.

Sections a to d below describe the risks in each of the four principal classes of business written by the Group.

a. property

Gross premium written, for the six months through June 30, 2006:

	$m
property retrocession	86.4
property direct and facultative	39.1
terrorism	3.6
property cat excess of loss	0.3
total	**129.4**

Property retrocession is written on an excess of loss basis through treaty arrangements. Programs are generally written on a pillared basis, with separate geographic zonal limits for risks in the U.S. and Canada and for risks outside the U.S. and Canada. The gross limit on exposure to property retrocession risks in 2006 has been limited to $300 million per geographic zone in the aggregate. As at June 30, 2006, the gross exposure is less than $300 million. Reinsurance has also been purchased to mitigate gross losses in the U.S. and Canada. Property cat excess of loss may be written in a similar manner to property retrocession but is not written on a pillared basis. The Group is exposed to large catastrophic losses such as wind and earthquake loss from assuming property retrocession risks. The Group's appetite and exposure guidelines to large losses are set out on page 13.

Property direct and facultative is written for the full value of the risk, on a primary or excess of loss basis. Cover is generally provided to large commercial enterprises with high value locations. Perils covered are typically fire, explosion, flood and business interruption, although catastrophe covers for wind and earthquake damage may also be given in some cases.

Terrorism cover is provided for U.S. and worldwide property risks, but excludes nuclear, chemical and biological coverage in most territories.

b. energy

Gross premium written, for the six months through June 30, 2006:

	$m
gulf of mexico offshore energy	120.6
worldwide offshore energy	24.4
onshore energy	3.3
other energy	2.9
total	**151.2**

Energy risks are mostly written on a direct basis. Gulf of Mexico energy programs cover elemental (natural catastrophe) and non-elemental risks. The largest exposure is from hurricanes in the Gulf of Mexico. Exposure to such events is controlled and measured through loss modeling but the accuracy of this exposure analysis is limited by the quality of data and effectiveness of the modeling. It is possible that a catastrophic event exceeds the expected event loss. The Group's appetite and exposure guidelines to large losses are set out on page 13. Policies have sub-limits on coverage for elemental losses, and significant policy restrictions on other areas of cover such as business interruption and control of well. Reinsurance protection has been purchased to protect a portion of loss from elemental energy claims. Non-elemental energy risks include fire and explosion.

Worldwide offshore energy programs are generally for non-elemental risks. Onshore energy risks can include onshore Gulf of Mexico and worldwide energy installations and are largely subject to the same loss events as described above.

Other energy primarily comprises insurance of energy installations under construction.

c. marine

Gross premium written, six months through June 30, 2006

	$m
marine hull and total loss	5.8
marine P&I clubs	4.7
marine excess of loss	4.3
other marine	6.9
total	**21.7**

Marine hull and total loss is generally written on a direct basis and covers marine risks on a worldwide basis primarily for physical damage and loss. Marine P&I is the reinsurance of The International Group of Protection and Indemnity Clubs. Marine excess of loss is generally written on a treaty basis.

Other marine includes marine war, which is direct insurance of loss of vessels from war or terrorist attack, and insurance for marine property under construction. Marine cargo programs are not normally written. The largest exposure is from physical loss rather than from elemental loss events.

d. aviation

	$m
AV 52	14.0
other aviation	-
total	**14.0**

Aviation AV52 is written on a direct basis and provides coverage for third party liability resulting from acts of war or hijack against aircraft.

Other aviation business may include aviation hull war risks and industry loss warranty programs in the future, although no such programs had been written by June 30, 2006.

reinsurance

The Group, in the normal course of business and in accordance with its risk management practices, seeks to reduce the loss that may arise from events that could cause unfavourable underwriting results by entering into reinsurance arrangements. Reinsurance does not relieve the Group of its obligations to policyholders. Under the Group's reinsurance security policy, reinsurers are generally required to be rated A- or better by A.M. Best. The Group considers reinsurers that are not rated or do not fall within the above rating category on a case by case basis, and may require therefore collateral to be posted to support obligations. The Group monitors the credit worthiness of its reinsurers on an ongoing basis.

The Group purchases excess of loss reinsurance, including industry loss warranty covers, and proportional reinsurance. To date, the reinsurance purchased reduces the Group's net exposure to a large natural catastrophe loss in the U.S. which is the Group's largest gross exposure to loss. The Group has not currently purchased reinsurance for risks outside the U.S.

There is no guarantee that reinsurance coverage will be available to meet all potential loss circumstances, as it is possible that the cover purchased is not sufficient. Any loss amount which exceeds the program would be retained by the Group. Some parts of the reinsurance program have limited reinstatements therefore the number of claims which may be recovered from second or subsequent losses is limited.

insurance liabilities

For most insurance and reinsurance companies, the most significant judgment made by management is the estimation of loss and loss adjustment expense reserves. The estimation of the ultimate liability arising from claims made under insurance and reinsurance contracts is a critical estimate for the Group.

Under generally accepted accounting principles, loss reserves are not permitted until the occurrence of an event which may give rise to a claim. As a result, only loss reserves applicable to losses incurred up to the reporting date are established, with no allowance for the provision of a contingency reserve to account for expected future losses. Claims arising from future catastrophic events can be expected to require the establishment of substantial reserves from time to time.

However, loss and loss adjustment expense reserves are maintained to cover the Group's estimated liability for both reported and unreported claims. Reserving methodologies that calculate a point estimate for the ultimate losses are utilised, and then a range is developed around the point estimate. The point estimate represents management's best estimate of ultimate loss and loss adjustment expenses. The Group's internal actuaries review the reserving assumptions and methodologies on a quarterly basis with loss estimates being subject to a semi-annual corroborative review by independent actuaries, using generally accepted actuarial principles.

The extent of reliance on management judgment in the reserving process differs as to whether the business is insurance or reinsurance, whether it is short-tail or long-tail and as to whether the business is written on an excess of loss or on a pro-rata basis. Over a typical annual period, the Group expects to write approximately 70% of programs on a direct basis and 30% as reinsurance. Typically, over 80% of programs are expected to be written on an excess of loss basis. The Group does not currently write a significant amount of long-tail business.

a. insurance versus reinsurance

Loss reserve calculations for direct insurance business are not precise in that they deal with the inherent uncertainty of future contingent events. Estimating loss reserves requires management to make assumptions regarding future reporting and development patterns, frequency and severity trends, claims settlement practices, potential changes in the legal environment and other factors such as inflation. These estimates and judgments are based on numerous factors, and may be revised as additional experience or other data becomes available or reviewed as new or improved methodologies are developed or as current laws change.

Furthermore, as a broker market reinsurer for both excess of loss and proportional contracts, management must rely on loss information reported to brokers by primary insurers who must estimate their own losses at the policy level, often based on incomplete and changing information. The information management receives varies by cedant and may include paid losses, estimated case reserves, and an estimated provision for incurred but not reported losses (“IBNR reserves”). Additionally, reserving practices and the quality of data reporting may vary among ceding companies which adds further uncertainty to the estimation of the ultimate losses.

b. short-tail versus long-tail

In general, claims relating to short tail property risks, such as those underwritten by the Group, are reported more promptly by third parties than those relating to long tail risks, including the majority of casualty risks. However, the timeliness of reporting can be affected by such factors as the nature of the event causing the loss, the location of the loss, and whether the losses are from policies in force with primary insurers or with reinsurers.

c. excess of loss versus proportional

For excess of loss business, management are aided by the fact that each treaty has a defined limit of liability arising from one event. Once that limit has been reached, there is no further exposure to additional losses from that treaty for the same event. For proportional treaties, generally an initial estimated loss and loss expense ratio (the ratio of losses and loss adjustment expenses incurred to premiums earned) is used, based upon information provided by the insured or ceding company and/or their broker and management’s historical experience of that treaty, if any, and the estimate is adjusted as actual experience becomes known.

d. time lags

There is a time lag inherent in reporting from the original claimant to the primary insurer to the broker and then to the reinsurer, especially in the case of excess of loss reinsurance contracts. Also, the combination of low claim frequency and high severity make the available data more volatile and less useful for predicting ultimate losses. In the case of proportional contracts, reliance is placed on an analysis of a contract's historical experience, industry information, and the professional judgment of underwriters in estimating reserves for these contracts. In addition, if available, reliance is placed partially on ultimate loss ratio forecasts as reported by cedants, which are normally subject to a quarterly or six month lag.

e. uncertainty

As a result of the time lag described above, an estimation must be made of IBNR reserves, which consist of a provision for additional development in excess of the case reserves reported by ceding companies, as well as a provision for claims which have occurred but which have not yet been reported by ceding companies. Because of the degree of reliance that is necessarily placed on ceding companies for claims reporting, the associated time lag, the low frequency/high severity nature of much of the business that the Group underwrites, and the varying reserving practices among ceding companies, reserve estimates are highly dependent on management judgment and therefore uncertain. During the loss settlement period, which may be years in duration, additional facts regarding individual claims and trends often will become known, and current laws and case law may change, with consequent impact on reserving.

The claim count on the types of insurance and reinsurance that the Group writes, which are low frequency and high severity in nature, is generally low.

For certain catastrophic events there is greater uncertainty underlying the assumptions and associated estimated reserves for losses and loss adjustment expenses. Complexity resulting from problems such as policy coverage issues, multiple events affecting one geographic area and the resulting impact on claims adjusting (including allocation of claims to event and the effect of demand surge on the cost of building materials and labour) by, and communications from, ceding companies, can cause delays to the timing with which the Group is notified of changes to loss estimates.

In the six months to June 30, 2006, management were not notified or made aware of any losses of a material size. As such, at June 30, 2006 management's estimates for IBNR represented approximately 100% of total loss reserves. The majority of the estimate relates to potential claims on non-elemental risks where timing delays in cedant reporting may mean losses have occurred which management were not made aware of by June 30, 2006.

B. financial risk disclosures

The Group is exposed if proceeds from financial assets are not sufficient to fund obligations arising from its insurance contracts.

The Group segments its investment portfolio into two main components: A category to meet expected insurance liabilities ("core portfolio") and a balancing category which represents funds in excess of those required to meet expected insurance liabilities ("surplus portfolio").

The core portfolio needs to be sufficiently liquid to settle claims. The core portfolio is invested in fixed income securities and cash and cash equivalents and with a bias towards shorter durations and higher quality assets.

risk disclosures
for the six months ended june, 30 2006

The surplus portfolio is invested in fixed income, cash and cash equivalents and a modest amount of equity securities. Currently, the Group does not hold any alternative investments such as hedge funds.

Investment guidelines are established by the Investment Committee of the Board of Directors. Separate investment guidelines exist for the core portfolio, the surplus portfolio and the Group's consolidated portfolio. Investment guidelines set parameters within which investment managers must operate. Important parameters include guidelines on permissible assets, duration ranges, credit quality, and maturity. Investment guidelines are monitored on a monthly basis.

Asset allocation is as follows:

	june 30, 2006			december 31, 2005		
	$m	$m	$m	$m	$m	$m
	core	**surplus**	**total**	**core**	**surplus**	**total**
fixed income securities	434.0	432.5	866.5	-	-	-
equity securities	-	86.9	86.9	-	-	-
cash	123.3	91.7	215.0	1,072.4	-	1,072.4
total	**557.3**	**611.1**	**1,168.4**	**1,072.4**	**-**	**1072.4**

	%	**%**	**%**	%	%	%
fixed income securities	37.1	37.0	74.1	-	-	-
equity securities	-	7.4	7.4	-	-	-
cash	10.6	7.9	18.5	100.0	-	100.0
total	**47.7**	**52.3**	**100.0**	**100.0**	**-**	**100.0**

The investment mix of the fixed income portfolio is as follows:

	june 30, 2006			december 31, 2005		
	$m	$m	$m	$m	$m	$m
	core	**surplus**	**total**	**core**	**surplus**	**total**
U.S. treasuries	35.1	57.2	92.3	-	-	-
U.S. government agencies	135.1	36.6	171.7	-	-	-
asset backed securities	72.5	37.3	109.8	-	-	-
mortgage backed securities	82.4	242.5	324.9	-	-	-
corporate bonds	101.1	58.9	160.0	-	-	-
other	7.8	-	7.8	-	-	-
total	**434.0**	**432.5**	**866.5**	**-**	**-**	**-**

	%	**%**	**%**	%	%	%
U.S. treasuries	4.0	6.6	10.6	-	-	-
U.S. government agencies	15.6	4.2	19.8	-	-	-
asset backed securities	8.4	4.3	12.7	-	-	-
mortgage backed securities	9.5	28.0	37.5	-	-	-
corporate bonds	11.7	6.8	18.5	-	-	-
other	0.9	-	0.9	-	-	-
total	**50.1**	**49.9**	**100.0**	**-**	**-**	**-**

Both the core and surplus fixed income portfolios are managed by two external investment managers with identical mandates. The equity portfolio is managed by one investment manager. The equity portfolio is invested predominantly in U.S. and Canadian securities in a diversified range of sectors. The performance of the managers is monitored on an on-going basis.

An analysis of the most important components of financial risk is detailed in a to e below.

a. valuation risk

The Group's net asset value is directly impacted by movements in the value of investments held. Values can be impacted by movements in interest rates, credit ratings, economic environment and outlook, and exchange rates.

The impact of a 10% fall in the value of the Group's equity portfolio at June 30, 2006 would be $8.6 million. Valuation risk in the equity portfolio is mitigated by adopting a deep value strategic approach and by diversifying the portfolio across asset classes and geographic zones.

b. interest rate risk

The majority of the Group's investments comprise fixed income securities. The fair value of the Group's fixed income portfolio is inversely correlated to movements in market interest rates. If market interest rates fall, the fair value of the Group's fixed income investments would tend to rise and vice versa. The sensitivity of the price of fixed income securities is indicated by its duration[1]. The greater a security's duration, the greater its percentage price volatility.

The sensitivity of the Group's fixed income portfolio at June 30, 2006 to interest rate movements is as follows:

immediate shift in yield (basis points)	%	$m
100	-2.6	(22.4)
75	-1.9	(16.8)
50	-1.3	(11.2)
25	-0.7	(5.6)
-25	0.7	5.6
-50	1.3	11.2
-75	1.9	16.8
-100	2.6	22.4

The Board limits interest rate risk on its investment portfolio by establishing and monitoring duration ranges within investment guidelines. The duration of the fixed income portfolios at June 30, 2006 was 1.59 for the core portfolio and 3.59 for the surplus portfolio.

[1] Duration is the weighted average maturity of a security's cash flows, where the present values of the cash flows serve as the weights.

Insurance contract liabilities are not directly sensitive to the level of market interest rates, as they are undiscounted and contractually non-interest bearing.

The Group has issued long-term debt as described in note 18. The loan notes bear interest at a floating rate plus a fixed margin of 3.7%. The Group is subject to interest rate risk on the coupon payments of the long-term debt. The Group has mitigated the interest rate risk by entering into swap contracts as follows:

	maturity date	**prepayment date[1]**	**interest hedged[2]**
senior loan notes €24 million	june 15, 2035	march 15, 2011	50%
subordinated loan notes $97 million	december 15, 2035	december 15, 2011	50%

[1] The subordinated note can be prepaid from 16 December 2005, with a sliding scale redemption price penalty which reduces to zero by 15 December 2011.
[2] The Group has entered into swaps to fix the interest rate on 50% of the principal through the prepayment dates specified above.

The current Euribor interest rate on 50% of the senior loan notes has been fixed at 2.96%. The current LIBOR interest rate on 50% of the subordinated loan notes has been fixed at 5.33%. The Group remains exposed to interest risk on the portion of the notes which have not been hedged.

c. liquidity risk

The Group can be exposed to daily calls on its available investment assets, principally from insurance claims. Liquidity risk is the risk that cash may not be available to pay obligations when they are due without incurring an unreasonable cost.

The maturity dates of the Group's fixed income portfolio at June 30, 2006 were as follows:

	$m	$m	$m
	core	**surplus**	**total**
less than one year	3.3	-	3.3
between one year and two years	169.3	19.9	189.2
between two and three years	55.6	26.4	82.0
between three and four years	63.6	29.1	92.7
between four and five years	30.5	45.5	76.0
over five years	106.0	311.6	417.6
	428.3	432.5	860.8
perpetual and non-dated securities	5.7	-	5.7
total	**434.0**	**432.5**	**866.5**

Actual maturities may differ from contractual maturities because certain borrowers have the right to call or pre-pay certain obligations with or without call or prepayment penalties.

The Board limits liquidity risk in several ways. First, a portion of the investment portfolio is segregated for the short term liquidity requirements arising from insurance obligations. The core portfolio is highly liquid with short maturity. All core portfolio securities are quoted on major exchanges. Secondly, the Board has established asset allocation and maturity parameters within investment guidelines such that the vast majority of the Group's investments are in high quality assets which could be converted into cash promptly and at minimal expense.

d. currency risk

The Group currently underwrites out of a single location, Bermuda, however risks are assumed on a worldwide basis. Risks assumed are predominantly denominated in U.S. dollars. The Group is exposed to currency risk to the extent its assets are denominated in different currencies to its liabilities. The Group is also exposed to non-retranslation risk on non-monetary assets such as unearned premiums. At each balance sheet date exchange gains and losses can impact the consolidated income statement.

The Group has hedged the large majority of currency risk by closely matching the U.S. dollar liabilities with U.S. dollar assets. The Group's main foreign currency exposure relates to its insurance obligations and the €24 million senior notes long-term debt liability. While the unhedged balances are not large, in the second half of 2006, the Group expects to more closely hedge these currency exposures by modestly increasing investments in non U.S. dollar assets or holding larger balances of non U.S. dollar cash.

The Group's assets and liabilities, categorised by currency at their translated carrying amount was as follows:

assets	$m	$m	$m	$m	$m
	U.S. $	**sterling**	**euro**	**other**	**total**
cash and cash equivalents	213.2	0.5	1.2	0.1	215.0
accrued interest receivable	7.9	-	-	-	7.9
investments	953.4	-	-	-	953.4
unearned premium on premium ceded	60.4	-	-	-	60.4
deferred acquisition costs	27.6	0.1	1.4	0.6	29.7
other receivables	80.6	-	-	-	80.6
inwards premium receivable from insureds	147.8	1.1	13.1	3.0	165.0
investment in associate	20.0	-	-	-	20.0
property, plant and equipment	0.6	-	-	-	0.6
total assets as at june 30, 2006	**1,511.5**	**1.7**	**15.7**	**3.7**	**1,532.6**

liabilities	$m	$m	$m	$m	$m
	U.S. $	**sterling**	**euro**	**other**	**total**
losses and loss adjustment expenses	7.1	0.1	0.2	-	7.4
unearned premiums	224.6	1.9	13.8	3.7	244.0
amounts payable to reinsurers	32.0	-	-	-	32.0
deferred acquisition costs ceded	5.6	-	-	-	5.6
other payables	124.2	0.2	-	0.3	124.7
accrued interest payable	0.4	-	0.1	-	0.5
long-term debt	97.0	-	30.1	-	127.1
total liabilities as at june 30, 2006	**490.9**	**2.2**	**44.2**	**4.0**	**541.3**

assets	$m	$m	$m	$m	$m
	U.S. $	**sterling**	**euro**	**other**	**total**
cash and cash equivalents	1,072.4	-	-	-	1,072.4
accrued interest receivable	2.0	-	-	-	2.0
investments	-	-	-	-	-
unearned premium on premium ceded	-	-	-	-	-
deferred acquisition costs	0.5	-	-	-	0.5
other receivables	0.3	-	-	-	0.3
inwards premium receivable from insureds	2.1	-	-	-	2.1
investment in associate	-	-	-	-	-
property, plant and equipment	0.4	-	-	-	0.4
total assets as at december 31, 2005	**1,077.7**	**-**	**-**	**-**	**1,077.7**

liabilities	$m	$m	$m	$m	$m
	U.S. $	**sterling**	**euro**	**other**	**total**
losses and loss adjustment expenses	-	-	-	-	-
unearned premiums	2.6	-	-	-	2.6
amounts payable to reinsurers	-	-	-	-	-
deferred acquisition costs ceded	-	-	-	-	-
other payables	2.2	-	-	-	2.2
accrued interest payable	0.4	-	-	-	0.4
long-term debt	97.0	-	28.4	-	125.4
total liabilities as at december 31, 2005	**102.2**	**-**	**28.4**	**-**	**130.6**

e. credit risk

Credit risk is the risk that a counterparty may fail to pay, or repay, a debt or obligation. The Group is exposed to credit risk on its fixed income investment portfolio, its inwards premium receivable from insureds and cedants, and on any amounts recoverable from reinsurers.

Credit risk on the fixed income portfolio is managed by establishing investment guidelines that set parameters on the absolute credit ratings of holdings and the concentration of holdings within credit rating bandings. The guidelines also place limits on the size of investment in a single issuer or class of issuer. Compliance with guidelines is regularly monitored.

Credit risk from reinsurance recoverables is primarily managed by review and approval of reinsurer security by the Group's reinsurance security committee as discussed on page 17.

The table below presents an analysis of the Group's major exposures to counterparty credit risk, based on Standard & Poor's or equivalent rating. The table includes amounts due from policyholders and unsettled investment trades. The quality of these receivables is not graded, but based on managements historical experience there is limited default risk associated with these amounts. Outstanding claims, including IBNR, recoverable from reinsurers was zero at June 30, 2006 and December 31, 2005, and therefore has not been included.

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	june 30, 2006		december 31, 2005	
	$m	$m	$m	$m
	cash & fixed income	**premium & other receivables**	**cash & fixed income**	**premium & other receivables**
AAA	927.3	-	1,072.4	-
AA+, AA, AA-	30.2	-	-	-
A+, A, A-	78.9	-	-	-
BBB+, BBB, BBB-	38.7	-	-	-
other	6.4	245.6	-	2.1
	1,081.5	**245.6**	**1,072.4**	**2.1**

1. general information

The Group is a provider of global property insurance and reinsurance products. LHL was incorporated under the laws of Bermuda on October 12, 2005. LHL is listed on the Alternative Investment Market ("AIM"), a subsidiary market of the London Stock Exchange. The registered office of LHL is Clarendon House, 2 Church Street, Hamilton HM 11, Bermuda. LHL has three wholly owned subsidiaries: Lancashire Insurance Company Limited ("LICL"), Lancashire Insurance Holdings (UK) Limited ("LIHUKL") and Lancashire Insurance Marketing Services Limited ("LIMSL"). LICL is the Group's principal operating subsidiary and was incorporated under the laws of Bermuda as a Class 4 insurer on October 28, 2005. LICL provides insurance and reinsurance products to its customers, with an emphasis on property, energy, marine and aviation lines of business. LIMSL is authorised by the United Kingdom Financial Services Authority to undertake insurance mediation activities. LIMSL provides business introduction and other support services to LICL, and was incorporated under the laws of the United Kingdom on October 7, 2005. LIHUKL is a holding company for two non-operating wholly owned subsidiaries.

2. segmental reporting

Management and the Board review the Group's business primarily by its four principal classes: property, energy, marine and aviation. Management has therefore deemed these classes to be its business and primary segments for the purposes of segmental reporting. Further sub classes of business are underwritten within each primary segment. The Group commenced underwriting in December 2005, but wrote an insignificant amount of business in the period from incorporation to December 31, 2005. Comparatives have therefore not been presented for segments.

revenue and expense by business segment

	$m	$m	$m	$m	$m
	property	**energy**	**marine**	**aviation**	**total**
gross premiums written	**129.4**	**151.2**	**21.7**	**14.0**	**316.3**
analysed by geographical segment					
worldwide offshore	-	97.3	14.5	-	111.8
USA and Canada	54.3	25.0	0.2	-	79.5
worldwide including the U.S.	40.8	19.8	1.7	13.9	76.2
worldwide excluding the U.S.	24.8	-	0.4	-	25.2
middle east	1.4	4.6	0.4	0.1	6.5
far east	3.4	0.2	2.5	-	6.1
rest of world	4.7	4.3	2.0	-	11.0
total	**129.4**	**151.2**	**21.7**	**14.0**	**316.3**
outwards reinsurance premiums	(39.8)	(31.2)	-	-	(71.0)
change in unearned premiums	(91.3)	(123.7)	(15.5)	(10.9)	(241.4)
change in unearned premiums ceded	32.3	28.1	-	-	60.4
insurance losses and loss adjustment expenses	(2.1)	(3.5)	(1.8)	-	(7.4)
insurance acquisition expenses	(3.1)	(2.9)	(1.0)	(0.6)	(7.6)
net underwriting profit	**25.4**	**18.0**	**3.4**	**2.5**	**49.3**

	$m	$m	$m	$m	$m
	property	**energy**	**marine**	**aviation**	**total**
net investment return					20.8
net foreign exchange gains (losses)					(1.1)
other operating expenses					(24.2)
finance costs					(5.5)
profit before tax					**39.3**
loss ratio	6.9%	14.3%	29.0%	0.0%	11.6%
acquisition cost ratio	10.1%	11.9%	16.1%	19.4%	11.8%
expense ratio	-	-	-	-	37.6%
combined ratio	**17.0%**	**26.2%**	**45.1%**	**19.4%**	**61.0%**

assets and liabilities by business segment

assets	$m	$m	$m	$m	$m
	property	**energy**	**marine**	**aviation**	**total**
attributable to business segments	110.4	123.8	14.6	12.6	261.4
other assets					1,271.2
total assets					**1,532.6**

liabilities	$m	$m	$m	$m	$m
attributable to business segments	100.7	160.1	17.3	10.9	289.0
other liabilities	-	-	-	-	252.3
total liabilities					**541.3**
total net assets					**991.3**

The Group's net assets are located primarily in Bermuda.

3. investment return

The total investment return for the Group is as follows:

	2006 $m	2005 $m
investment income		
- interest on fixed income securities	10.8	-
- net amortisation of premium (discount)	0.4	-
- interest income on cash and cash equivalents	13.0	2.1
net investment income	**24.2**	**2.1**
net realised gains (losses)		
- fixed income securities	(3.4)	-
net realised gains (losses)	**(3.4)**	**-**
unrealised gains (losses) recognised in shareholders’ equity		
- fixed income securities	(8.4)	-
- equity securities	2.7	-
net unrealised gains (losses) recognised in shareholders' equity	**(5.7)**	**-**
total investment return	**15.1**	**2.1**

4. insurance acquisition expenses

	2006 $m	2005 $m
insurance acquisition expenses	31.2	0.5
changes in deferred insurance acquisition expenses	(23.6)	(0.5)
total	**7.6**	**-**

5. other operating expenses

	2006 $m	2005 $m
operating expenses unrelated to underwriting	13.6	1.6
equity based compensation	10.6	8.4
total	**24.2**	**10.0**

6. employee benefits

	2006 $m	2005 $m
wages and salaries	1.9	0.2
pension costs	0.2	-
other benefits	2.4	-
equity based compensation	10.6	8.4
total	**15.1**	**8.6**

As at June 30, 2006, the Group had 25 (2005 – 4) employees.

equity based compensation

There are two forms of equity based compensation: warrants and a long term incentive plan.

On admission to AIM, warrants to purchase common shares were issued for immediate allocation to certain members of management or reserved for later allocation to employees of the Group. There are two forms of warrant: Management Team Ordinary Warrants and Management Team Performance Warrants.

All warrants issued to management will expire ten years from the date of issue and will be exercisable at an initial price per share of US$5.00 equal to the price per share paid by investors in the initial public offering. Settlement is at the discretion of the Group and may be in cash or shares.

management team ordinary warrants ("ordinary warrants")

Ordinary warrants do not have associated performance criteria. 25% of such warrants vested immediately upon issuance. Thereafter, 25% of such warrants will vest on the first, second and third anniversary of the grant date.

On December 16, 2005, ordinary warrants to purchase 12,708,695 common shares were issued, representing the full allocation of ordinary warrants.

management team performance warrants ("performance warrants")

Performance warrants vest over a four year period and are dependent on certain performance criteria with specific measurement dates of December 31, 2007, December 31, 2008 and December 31, 2009. Half of these warrants will vest only on achievement of a fully diluted book value per share in comparison to a planned appreciation threshold of between 70% and 100% at certain dates. The remaining half of these warrants will vest only on achievement of an IRR in comparison to a planned IRR of between 70% and 100% at certain dates.

On 16 December, 2005, performance warrants to purchase 7,625,218 common shares were issued, representing the full allocation of performance warrants.

The fair value of each warrant was estimated on the date of grant using the Black-Scholes option-pricing model. Assumptions used for valuation of these grants were as follows: risk free interest rate of 4.93%; an expected life of ten years; volatility of 30% being the maximum contractual rate; performance targets will be met; dividend yield of nil due to contractual dividend protection; the Group will settle in shares; no forfeitures, other than leavers which are assumed to be 10% of total employees, and no dilutive events.

Warrants	Number Thousands	Weighted Average Exercise Price US$
Allocated as at December 31, 2005	14,463	$5.00
Allocated during the period	2,567	$5.00
Allocated as at June 30, 2006	17,030	$5.00
Exercisable at June 30, 2006 and December 31, 2005	2,498	-

The fair value of warrants granted for the period ended June 30, 2006 was $2.62 (2005 - $2.62) per share. A share-based payment expense of $9.8 million (2005 - $8.4 million) is included in other operating expenses in the interim consolidated income statement.

long term incentive plan ("LTIP")

Options may be granted under the LTIP at the discretion of the remuneration committee. Options granted under the LTIP are limited to 5% of the common share capital in issue at the date of grant. All options issued will expire ten years from date of issue and the exercise price is equal to or greater than the average market value of the shares on the twenty previous trading days prior to grant. 25% of such options vested immediately upon issuance. Thereafter, 25% of such options will vest on the first, second and third anniversary of the grant date. There are no associated performance criteria.

On March 9, 2006, certain members of staff were issued options to purchase 2,249,439 common shares.

The fair value of each option was estimated on the date of grant using the Black-Scholes option-pricing model. Assumptions used for valuation of these grants were as follows: risk free interest rate of 5.125%; an expected life of six years; volatility of 30% being the maximum contractual rate; performance targets will be met; dividend yield of nil due to contractual dividend protection; the Group will settle in shares; no forfeitures, other than leavers which are assumed to be 10% of total employees, and no dilutive events.

Options	**Number Thousands**	**Weighted Average Exercise Price US$**
Granted during the period and outstanding at June 30, 2006	2,249	$5.65
Exercisable at June 30, 2006	-	-

The fair value of options granted during the period ended June 30, 2006 was $2.27 per share. A share-based payment expense of $0.8 million (2005 - $nil) is included in other operating expenses in the interim consolidated income statement.

7. results of operating activities

Results of operating activities are stated after charging the following amounts:

	2006 $m	2005 $m
depreciation on owned assets	0.1	-
operating lease charges	0.2	-
auditors remuneration		
- group audit fees	0.4	0.1
- other services	0.3	0.6
total	**1.0**	**0.7**

Fees paid to the Group’s auditors for other services are approved by the Group’s audit committee. Such fees comprise the following amounts:

	2006 $m	2005 $m
taxation advice	0.1	-
FSA regulatory advice	0.2	-
other	-	0.6
total	**0.3**	**0.6**

8. tax

Bermuda
The Group has received an undertaking from the Bermuda government exempting it from all local income, withholding and capital gains taxes until March 28, 2016. At the present time no such taxes are levied in Bermuda.

United States
The Group does not consider itself to be engaged in trade or business in the United States and, accordingly, does not expect to be subject to United States taxation.

United Kingdom
The UK subsidiaries are subject to normal UK tax on all profits. For the period ended June 30, 2006 there was no corporation tax liability.

9. cash and cash equivalents

	2006 $m	2005 $m
cash at bank and in hand	72.6	12.2
cash equivalents	142.4	1,060.2
total	**215.0**	**1,072.4**

Cash equivalents have an original maturity of three months or less. The carrying amount of these assets approximates to their fair value.

Cash and cash equivalents totaling $10.5 million (2005 - $5.4 million) were on deposit in various trust accounts for the benefit of policyholders or counterparties to agreements to cover their credit risk.

10. investments

as at june 30, 2006	$m	$m	$m	$m
	cost or amortised cost	**gross unrealised gain**	**gross unrealised loss**	**estimated fair value**
fixed income				
- U.S. treasuries	93.2	0.1	(1.0)	92.3
- U.S. government agencies	173.1	-	(1.4)	171.7
- asset backed securities	110.5	-	(0.7)	109.8
- mortgage backed securities	328.1	0.4	(3.6)	324.9
- corporate bonds	162.2	-	(2.2)	160.0
- other	7.8	-	-	7.8
	874.9	0.5	(8.9)	866.5
equity securities	84.2	4.3	(1.6)	86.9
total	**959.1**	**4.8**	**(10.5)**	**953.4**

Equity securities are generally deemed non-current. Fixed income maturities are presented in the risk disclosures section.

In 2005 the Group's assets were held entirely in cash and cash equivalents. Comparatives for the above table have therefore not been presented.

11. investment in associate

On June 15, 2006 the Group made an investment of $20.0 million which represents a 21% interest in Sirocco Holdings Limited ("Sirocco"), a company incorporated in Bermuda. Sirocco's operating subsidiary, Sirocco Reinsurance Limited ("Sirocco Re"), is authorised as a Class 3 insurer by the Bermuda Monetary Authority. Sirocco Re was established to assume Gulf of Mexico energy risks from the Group. Sirocco is an unquoted investment and its shares do not trade in any active market. Sirocco is carried at $20.0 million, representing management's best estimate of fair value at June 30, 2006.

	2006 $m
as at january 1, 2006	-
acquisition	20.0
as at june 30, 2006	**20.0**

Investments in associates are generally deemed non-current. Key financial information for Sirocco for the period ending June 30, 2006 is as follows:

	$m
assets	116.9
liabilities	19.4
revenues	3.1
profit (loss)	2.5

12. insurance contracts and reinsurance assets

insurance liabilities	$m	$m	$m
	losses & loss adjustment expenses	**unearned premiums**	**total**
as at october 12, 2005 (date of incorporation)	-	-	-
movement in period	-	2.6	2.6
exchange adjustments	-	-	-
as at december 31, 2005	**-**	**2.6**	**2.6**
movement in period	7.4	241.4	248.8
exchange adjustments	-	-	-
as at june 30, 2006	**7.4**	**244.0**	**251.4**

reinsurance assets	$m	$m	$m
	unearned premiums	**reinsurance payable**	**total**
as at october 12, 2005 (date of incorporation)	-	-	-
movement in period	-	-	-
exchange adjustments	-	-	-
as at december, 31 2005	**-**	**-**	**-**
movement in period	60.4	(32.0)	28.4
exchange adjustments	-	-	-
as at june 30, 2006	**60.4**	**(32.0)**	**28.4**

Further information on the calculation of loss reserves and the risks associated with them is provided in the risk disclosures section, which starts on page 13. The risks associated with general insurance contracts are complex and do not readily lend themselves to meaningful sensitivity analysis. The impact of an unreported event could lead to a significant increase in our loss reserves. Management believe that the loss reserves established as at June 30, 2006 are adequate, however a 20% increase in unpaid losses would lead to a $1.4m (2005 - $nil) increase in loss reserves.

The split of losses and loss adjustments expenses between notified outstanding losses and losses incurred but not reported is shown below:

	2006 $m	2005 $m
outstanding losses	-	-
losses incurred but not reported	7.4	-
losses and loss adjustment expense reserves	**7.4**	**-**

It is estimated that 100% of the losses and loss adjustment expenses above will settle in the next 12 months.

claims development

The development of insurance liabilities is indicative of the Group's ability to estimate the ultimate value of its insurance liabilities. The Group began writing insurance and reinsurance business in December 2005. Due to the underlying risks and lack of known loss events occurring during the period to December 31, 2005, the Group does not expect to incur any losses from coverage provided in 2005. Accordingly, a loss development table has not been included.

13. insurance and other receivables

	2006 $m	2005 $m
inwards premium receivable from insureds and cedants	165.0	2.1
other receivables	80.6	0.3
accrued interest receivable	7.9	2.0
total receivables	**253.5**	**4.4**

Other receivables consist primarily of unsettled investment trades. All receivables are considered current other than $0.2 million (2005 - $nil) related to multi-year contracts. The carrying value approximates fair value due to the short term nature of the receivables. There are no provisions in place for impairment or irrecoverable balances. There is no significant concentration of credit risk within the Group's receivables.

14. deferred acquisition costs

The reconciliation between opening and closing deferred acquisition costs is shown below:

	$m
balance as at october 12, 2005 (date of incorporation)	-
movement in period	0.5
balance as at december 31, 2005	**0.5**
movement in period	29.2
balance as at june 30, 2006	**29.7**

15. reinsurance and other payables

	2006 $m	2005 $m
amounts payable to reinsurers	32.0	-
other payables	124.7	2.2
total payables	**156.7**	**2.2**

Other payables consist primarily of unsettled investment trades. All payables are considered current. The carrying value approximates fair value due to the short-term value of the payables.

16. deferred acquisition costs ceded

The reconciliation between opening and closing deferred acquisition costs ceded is shown below:

	$m
balance as at october 12, 2005 (date of incorporation)	-
movement in period	-
balance as at december 31, 2005	-
movement in period	5.6
balance as at june 30, 2006	**5.6**

17. property, plant and equipment

	IT equipment $m
cost	
as at october 12, 2005 (date of incorporation)	-
additions	0.4
as at december 31, 2005	**0.4**
accumulated depreciation	
as at october 12, 2005 (date of incorporation)	-
charge for the period	-
as at december, 31 2005	**0.4**
net book value	
as at october 12, 2005 (date of incorporation)	-
as at december 31, 2005	**0.4**

	IT equipment $m
cost	
as at january 1, 2006	0.4
additions	0.3
as at june 30, 2006	**0.7**
accumulated depreciation	
as at january 1, 2006	-
charge for the period	0.1
as at june 30, 2006	**0.1**
net book value	
as at january 1,2006	0.4
as at june 30, 2006	**0.6**

18. long term debt and financing arrangements

	2006 $m	2005 $m
senior loan note of €12.0 million	15.1	14.2
senior loan note of €12.0 million	15.0	14.2
subordinated loan note of $97.0 million	97.0	97.0
carrying value and fair value	**127.1**	**125.4**

On December 15, 2005 the Group issued $97 million in aggregate principal amount of subordinated loan notes and €24 million in aggregate principal amount of senior loan notes ("long-term debt") at an issue price of $1,000 and €1,000 of their principal amounts respectively.

The Euro senior loan notes are repayable on June 15, 2035 with a prepayment option available from March 15, 2011. Interest on the principal is based on a set margin (3.7%) above Euribor and is payable quarterly.

The US dollar subordinated loan notes are repayable on December 15, 2035 with a sliding scale redemption price from December 16, 2005. Interest on the principal is based on a set margin (3.7%) above Libor and is payable quarterly.

The Group is exposed to cash flow interest rate risk and currency risk. Further information is provided in the risk disclosures section.

The interest accrued on the loans payable was $0.5 million (2005 - $0.4 million) at the balance sheet date.

Due to the long term nature of the loans and the floating interest rates, the carrying value approximates fair value.

letters of credit

As LICL is not an admitted insurer or reinsurer throughout the U.S., the terms of certain contracts require LICL to provide letters of credit to policyholders as collateral. On May 17, 2006, LICL entered into a syndicated collateralised three year credit facility in the amount of $350 million. This facility is available for the issue of letters of credit to ceding companies. It also contains a $75m loan sub-limit available for general corporate purposes. As at June 30, 2006 no letters of credit had been issued and there was no outstanding debt under this facility.

19. derivative financial instruments

The Group hedges a portion of its floating rate borrowings using interest rate swaps to transfer floating to fixed rate. These instruments are held at fair value through the consolidated income statement. During the period, $nil (2005 - $nil) was credited to other income in respect of the interest rate swap. The net fair value position to the Group was $nil (2005 - $nil). The Group has the right to net settle this instrument. The next cash settlement due on this instrument is negligible (2005 - $nil) and is due on September 15, 2006.

20. share capital

authorised ordinary shares of $0.50 each	number	$m
as at december 31, 2005 and june 30, 2006	3,000,000,000	1,500

allocated, called up and fully paid	number	$m
as at october 12, 2005 (date of incorporation)	-	-
shares issued	195,713,902	97.9
as at december 31, 2005 and june 30, 2006	**195,713,902**	**97.9**

LHL issued 16,000,000 new shares on October 27, 2005 as part of its initial capitalisation and launch. On December 9, 2005, LHL's outstanding shares were consolidated on a 5:1 basis into 3,200,000 shares. On December 16, 2005, an aggregate of 192,513,902 new shares were issued as part of LHL's private placement in the U.S. and initial public offering in the U.K., which included shares issued on the exercise of an over-allotment option. As a result of all the shares issued, a total of $978.6 million was raised, $97.9 million of which is included in share capital and $880.7 million of which was included in share premium, net of $19.9 million of offering expenses, formation expenses and warrants issued to management, founders and a sponsor.

21. warrants and options

	founder warrants	**sponsor warrants**	**management ordinary warrants**	**management performance warrants**	**options**
	number	number	number	number	number
as at october 12, 2005 (date of incorporation)	-	-	-	-	-
issued	17,791,919	7,625,217	12,708,695	7,625,218	-
exercised	-	-	-	-	-
as at december 31, 2005	**17,791,919**	**7,625,217**	**12,708,695**	**7,625,218**	**-**
issued	-	-	-	-	2,249,439
exercised	-	-	-	-	-
as at june 30, 2006	**17,791,919**	**7,625,217**	**12,708,695**	**7,625,218**	**2,249,439**

warrants

All warrants issued will expire ten years from the date of issue and are exercisable at an initial price per share of US$5.00 equal to the price per share paid by investors in the initial public offering. The warrant holder may elect a cashless exercise. The method of settlement is at the discretion of the Group and may be in cash or shares.

founders

The Group's founders provided industry expertise, resources and relationships during the fourth quarter of 2005. For the founders position and consideration, the Group issued warrants to certain founding shareholders to purchase in the aggregate, up to 17,791,919 common shares. These warrants were granted on December 12, 2005 and were fully vested and exercisable upon issuance.

sponsor

In consideration for incorporation services received, warrants have been issued to Benfield Advisory Limited to purchase 7,625,217 common shares. These warrants were granted on December 16, 2005 and were fully vested and exercisable upon issuance.

Management warrants and options are discussed in note 6.

22. lease commitments

The Group has payment obligations in respect of operating leases for certain items of office equipment and office space. Operating lease expenses for the period were $0.2 million (2005 - $nil). Lease payments under non-cancellable operating leases are as follows:

	2006 $m	2005 $m
due in less than one year	-	-
due between one and five years	1.9	-
due in more than five years	2.4	-
total	**4.3**	**-**

23. earnings per share

Basic earnings or loss per share amounts are calculated by dividing net profit or loss for the period attributable to shareholders by the weighted average number of common shares outstanding during the year.

Diluted earnings or loss per share amounts are calculated by dividing the net profit or loss attributable to shareholders by the weighted average number of common shares outstanding during the year plus the weighted average number of common shares that would be issued on the conversion of all dilutive potential common shares into common shares.

The following reflects the loss and share data used in the basic and diluted loss per share computations:

	2006 $m	2005 $m
Profit (loss) for the period attributable to shareholders	39.3	(11.6)

	Number of shares Thousands	Number of shares Thousands
Basic weighted average number of shares	195,714	48,320
Potentially dilutive shares related to share-based compensation	4,195	5,733
Diluted weighted average number of shares	199,909	54,053

Share based payments are only treated as dilutive when their conversion to common shares would decrease earnings per share or increase loss per share from continuing operations. In the prior period, incremental shares from the assumed exercising of warrants are not included in calculating the diluted earnings or loss per share as it would drive the loss per share further negative.

24. related party disclosures

The interim consolidated financial statements include Lancashire Holdings Limited and the subsidiaries listed below:

Name	**Domicile**
Lancashire Insurance Company Limited	Bermuda
Lancashire Insurance Marketing Services Limited	United Kingdom
Lancashire Holdings Financing Trust I	United States
Lancashire Insurance Holdings (UK) Limited	United Kingdom
Lancashire Insurance Services (UK) Limited	United Kingdom
Lancashire Insurance Services Limited	United Kingdom

All subsidiaries are wholly owned, either directly or indirectly.

The Group has issued loan notes via a trust vehicle - Lancashire Holdings Financing Trust I (the “Trust”) (see Note 18). The Group has 100% of the voting rights in the Trust, provided that there is no default on the loan notes. While the ability of the Group to influence the actions of the Trust is limited by the Trust Agreement, the Trust was set up by the Group with the sole purpose of issuing the loan notes. The Trust is in essence controlled by the Group, operates exclusively for the benefit of the Group, and is therefore consolidated.

key management compensation

Remuneration for key management for the period ending June 30, 2006 was as follows:

	2006 $m	2005 $m
short-term compensation	0.8	-
share based compensation	7.5	5.2
total	**8.3**	**5.2**

transactions with directors and shareholders

Significant shareholders have a representation on the Board of Directors. During the period the Group paid $0.3 million (2005 - $nil) in directors' fees and expenses. A further $0.2 million (2005 - $nil) was paid in respect of monitoring fees for significant shareholders pursuant to Monitoring Agreements, the terms of which are as disclosed in the application to list on AIM.

transactions with associates

During the period the Group ceded $22.2 million (2005 - $nil) of premium to Sirocco and received $4.3 million (2005 - $nil) of commission income.

transactions with sponsor

During the period the Group incurred net brokerage and consulting costs of $4.5 million with Benfield Group.

25. non-cash transactions

Accrued formation expenses of $nil (2005 - $0.9 million) have been recorded directly in shareholders' equity. This amount represents a non-cash transaction and therefore is not included within the change in operational assets and liabilities in the consolidated cashflow statement.

26. statutory requirements and dividend restrictions

As a holding company, LHL relies on dividends from its subsidiaries to provide cash flow required for debt service and dividends to shareholders. LICL's ability to pay dividends and make capital distributions is subject to certain regulatory restrictions based principally on the amount of LICL's premiums written and reserves for losses and loss expenses, subject to an overall minimum solvency requirement of $100 million. LICL is required to maintain a minimum statutory liquidity ratio. At June 30, 2006, LICL's statutory capital and surplus was $1,090.8 million (2005 - $1,069.6 million) and the minimum amount of statutory capital and surplus required to be maintained was $100 million. Statutory capital and surplus is different from shareholders' equity due to certain items that are capitalised under IFRS but expensed, have a different valuation basis, or are not admitted under the Bermuda Insurance Act 1978 and related Regulations (the "Act").

In addition, LICL is required to maintain a minimum liquidity ratio, whereby relevant assets, as defined in the Act, must exceed 75% of relevant liabilities. As at June 30, 2006 and December 31, 2005 the liquidity ratio was met.

27. presentation

Certain amounts in the December 31, 2005 consolidated financial statements have been re-presented to conform with the current year's presentation and format. These changes in presentation have no effect on the previously reported net loss.

28. subsequent events

On July 21, 2006 the UK Financial Services Authority ("FSA") notified the Group that it is minded to grant authorisation to a new underwriting company to be based in London. The Group expects to satisfy the remaining conditions of the FSA approval in due course and commence underwriting shortly thereafter. The new underwriting company will be capitalised from existing resources and will not change the existing Group business plan or lines of business.