AXIS CAPITAL HOLDINGS LTD
Form 10-Q
October 30, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2007
Commission file number 001-31721

AXIS CAPITAL HOLDINGS LIMITED

(Exact name of registrant as specified in its charter)

BERMUDA

(State or other jurisdiction of incorporation or organization)

98-0395986

(I.R.S. Employer Identification No.)

92 Pitts Bay Road, Pembroke, Bermuda HM 08

(Address of principal executive offices and zip code)

(441) 496-2600

(Registrant s telephone number, including area code)

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

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

Large accelerated filer x Accelerated filer o Non-accelerated filer o

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

As of October 26, 2007 there were 151,285,506 Common Shares, $0.0125 par value per share, of the registrant outstanding.

AXIS CAPITAL HOLDINGS LIMITED

INDEX TO FORM 10-Q

PART I. FINANCIAL INFORMATION

Cautionary Statement Regarding Forward-looking Statements

This quarterly report contains forward-looking statements within the meaning of the U.S. federal securities laws. We intend these forward-looking statements to be covered by the safe harbor provisions for forward-looking statements in the United States securities laws. In some cases, these statements can be identified by the use of forward-looking words such as may, should, could, anticipate, estimate, expect plan, believe, predict, potential, and intend . Forward-looking statements contained in this report include information regarding our estimates losses related to hurricanes and other catastrophes, our expectations regarding pricing and other market conditions, our growth prospects, the amount of our acquisition costs, the amount of our net losses and loss reserves, the projected amount of our capital expenditures, managing interest rate and foreign currency risks, valuations of potential interest rate shifts and foreign currency rate changes and measurements of potential losses in fair values of our investment portfolio. Forward-looking statements only reflect our expectations and are not guarantees of performance. These statements involve risks, uncertainties and assumptions. Actual events or results may differ materially from our expectations. Important factors that could cause actual events or results to be materially different from our expectations include (1) our limited operating history, (2) the occurrence of natural and man-made disasters, (3) actual claims exceeding our loss reserves, (4) the failure of any of the loss limitation methods we employ, (5) the effects of emerging claims and coverage issues, (6) the failure of our cedants to adequately evaluate risks, (7) the loss of one or more key executives, (8) a decline in our ratings with rating agencies, (9) loss of business provided to us by our major brokers, (10) changes in governmental regulations, (11) increased competition, (12) general economic conditions, (13) changes in the political environment of certain countries in which we operate or underwrite business and (14) the other matters set forth under Item 1A, Risk Factors and Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended December 31, 2006 filed with the SEC on March 1, 2007. We undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

AXIS CAPITAL HOLDINGS LIMITED

CONSOLIDATED BALANCE SHEETS
SEPTEMBER 30, 2007 (UNAUDITED) AND DECEMBER 31, 2006

(in thousands)		**2007**		**2006**
Assets				
Investments:				
Fixed maturity investments available for sale, at fair value *(Amortized cost 2007: $7,837,591; 2006: $6,574,249)*	**$**	**7,814,855**	$	6,532,723
Other investments, at fair value		**612,429**		1,130,664
Total investments		**8,427,284**		7,663,387
Cash and cash equivalents		**1,830,852**		1,989,287
Accrued interest receivable		**76,257**		76,967
Insurance and reinsurance premium balances receivable		**1,385,486**		1,125,822
Reinsurance recoverable balances		**1,247,720**		1,293,660
Reinsurance recoverable balances on paid losses		**97,047**		65,494
Deferred acquisition costs		**331,290**		251,799
Prepaid reinsurance premiums		**246,027**		241,821
Securities lending collateral		**861,280**		794,149
Goodwill and intangible assets		**61,967**		29,041
Other assets		**146,694**		133,860
Total assets	**$**	**14,711,904**	$	13,665,287
Liabilities				
Reserve for losses and loss expenses	**$**	**5,531,379**	$	5,015,113
Unearned premiums		**2,433,339**		2,015,556
Insurance and reinsurance balances payable		**255,922**		294,374
Securities lending payable		**858,546**		791,744
Senior notes		**499,234**		499,144
Liability under repurchase agreement				400,000
Net payable for investments purchased		**49,023**		62,185
Other liabilities		**140,869**		174,524
Total liabilities		**9,768,312**		9,252,640
Shareholders equity				
Preferred shares - Series A and B	**$**	**500,000**	$	500,000
Common shares *(2007: 147,936; 2006: 149,982 shares issued)*		**1,849**		1,875
Additional paid-in capital		**1,859,067**		1,929,406
Accumulated other comprehensive loss		**(28,444)**		(44,638)
Retained earnings		**2,690,742**		2,026,004
Treasury shares, at cost *(2007: 2,226; 2006: nil shares)*		**(79,622)**		
Total shareholders equity		**4,943,592**		4,412,647
Total liabilities and shareholders equity	**$**	**14,711,904**	$	13,665,287

See accompanying notes to consolidated financial statements.

AXIS CAPITAL HOLDINGS LIMITED

CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006

	Three months ended 2007	2006	Nine months ended 2007	2006
	(in thousands, except per share amounts)			
Revenues				
Net premiums earned	**$ 685,845**	$ 692,780	**$ 2,065,090**	$ 2,005,473
Net investment income	**118,908**	98,787	**357,873**	284,018
Net realized investment losses	**(1,192)**	(1,722)	**(5,548)**	(22,428)
Other insurance related income	**1,005**	804	**3,638**	1,866
Total revenues	**804,566**	790,649	**2,421,053**	2,268,929
Expenses				
Net losses and loss expenses	**328,193**	365,958	**1,079,714**	1,096,598
Acquisition costs	**100,039**	103,615	**293,923**	295,151
General and administrative expenses	**79,813**	68,470	**210,993**	181,538
Foreign exchange (gains) losses	**(7,202)**	2,738	**(16,477)**	(25,427)
Interest expense and financing costs	**13,929**	8,239	**43,241**	24,639
Total expenses	**514,772**	549,020	**1,611,394**	1,572,499
Income before income taxes	**289,794**	241,629	**809,659**	696,430
Income tax expense	**10,677**	6,181	**32,943**	23,540
Net income	**279,117**	235,448	**776,716**	672,890
Preferred share dividends	**9,142**	9,226	**27,573**	28,083
Net income available to common shareholders	**$ 269,975**	$ 226,222	**$ 749,143**	$ 644,807
Weighted average common shares and common share equivalents:				
Basic	**146,845**	149,884	**148,753**	149,657
Diluted	**164,064**	164,701	**165,458**	163,863
Earnings per common share:				
Basic	**$ 1.84**	$ 1.51	**$ 5.04**	$ 4.31
Diluted	**$ 1.65**	$ 1.37	**$ 4.53**	$ 3.94
Cash dividends declared per common share	**$ 0.165**	$ 0.15	**$ 0.495**	$ 0.45

See accompanying notes to the consolidated financial statements.

6

AXIS CAPITAL HOLDINGS LIMITED

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006

	Three months ended		Nine months ended	
	2007	**2006**	**2007**	**2006**
		(in thousands)		
Net income	**$ 279,117**	$ 235,448	**$ 776,716**	$ 672,890
Other comprehensive income, net of tax				
Change in unrecognized prior period service cost on the supplemental executive retirement plan (SERP)	**562**		**1,687**	(384)
Unrealized gains arising during the period	**77,803**	110,046	**10,109**	3,670
Adjustment for re-classification of investment (gains) losses realized in net income	**(116)**	1,861	**4,398**	19,840
Comprehensive income	**$ 357,366**	$ 347,355	**$ 792,910**	$ 696,016

See accompanying notes to consolidated financial statements.

7

AXIS CAPITAL HOLDINGS LIMITED

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY (UNAUDITED)
NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006

	2007	2006
	(in thousands)	
Common shares (shares outstanding)		
Balance at beginning of period	**149,982**	148,869
Shares issued, net	**729**	1,125
Shares repurchased for treasury	**(2,226)**	
Shares repurchased and cancelled	**(2,775)**	
Balance at end of period	**145,710**	149,994
Preferred shares - Series A and B		
Balance at beginning and end of period	**$ 500,000**	$ 500,000
Common shares (par value)		
Balance at beginning of period	**1,875**	1,861
Shares issued	**9**	14
Shares repurchased and cancelled	**(35)**	
Balance at end of period	**1,849**	1,875
Additional paid-in capital		
Balance at beginning of period	**1,929,406**	1,886,356
Share-based compensation expense	**25,404**	19,604
Shares issued	**1,294**	(28)
Stock options exercised	**6,399**	17,237
Shares repurchased and cancelled	**(103,436)**	
Balance at end of period	**1,859,067**	1,923,169
Accumulated other comprehensive loss		
Balance at beginning of period	**(44,638)**	(77,798)
Change in unrealized losses on fixed maturity investments	**15,891**	23,825
Change in unrecognized prior period service cost on the SERP	**1,687**	(384)
Change in deferred taxes	**(1,384)**	(316)
Balance at end of period	**(28,444)**	(54,673)
Retained earnings		
Balance at beginning of period	**2,026,004**	1,201,932
Net income	**776,716**	672,890
Series A and B preferred share dividends	**(27,573)**	(28,083)
Common share dividends	**(84,405)**	(76,161)
Balance at end of period	**2,690,742**	1,770,578
Treasury shares, at cost		
Balance at beginning of period		
Shares repurchased for treasury	**(79,622)**	
Balance at end of period	**(79,622)**	
Total shareholders equity	**$ 4,943,592**	$ 4,140,949

See accompanying notes to consolidated financial statements.

AXIS CAPITAL HOLDINGS LIMITED

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006

	2007	2006
	(in thousands)	
Cash flows from operating activities:		
Net income	**$ 776,716**	$ 672,890
Adjustments to reconcile net income to net cash provided by operating activities:		
Net realized investment losses	**5,548**	23,774
Net change in fair value of other investments	**(14,300)**	(12,545)
Amortization/accretion of fixed maturity investments	**(13,808)**	23,569
Other amortization and depreciation	**17,566**	2,808
Share-based compensation expense	**25,404**	19,604
Changes in:		
Accrued interest receivable	**710**	(5,451)
Reinsurance recoverable balances	**14,387**	153,428
Deferred acquisition costs	**(79,491)**	(75,722)
Prepaid reinsurance premiums	**(4,206)**	6,607
Reserve for loss and loss expenses	**516,266**	251,736
Unearned premiums	**417,783**	406,897
Insurance and reinsurance balances, net	**(298,116)**	(232,937)
Other items	**(86,153)**	(4,924)
Net cash provided by operating activities	**1,278,306**	1,229,734
Cash flows from investing activities:		
Purchases of available-for-sale fixed maturities	**(5,579,091)**	(3,861,569)
Sales and maturities of available-for-sale fixed maturities	**4,310,846**	3,384,106
Purchases of other investments	**(65,250)**	(301,267)
Sales of other investments	**585,395**	
Purchase of assets	**(38,261)**	
Net cash used in investing activities	**(786,361)**	(778,730)
Cash flows from financing activities:		
Repayment of repurchase agreement	**(400,000)**	
Repurchase of shares	**(183,093)**	
Dividends paid - common shares	**(83,806)**	(68,030)
Dividends paid - preferred shares	**(27,573)**	(28,083)
Proceeds from exercise of stock options	**6,399**	
Proceeds from issuance of common shares	**1,303**	17,223
Net cash used in financing activities	**(686,770)**	(78,890)
Effect of exchange rate changes on foreign currency cash	**36,389**	(12,190)
(Decrease) increase in cash and cash equivalents	**(158,436)**	359,924
Cash and cash equivalents - beginning of period	**1,989,287**	1,280,990
Cash and cash equivalents - end of period	**$ 1,830,851**	$ 1,640,914

See accompanying notes to the consolidated financial statements.

9

AXIS CAPITAL HOLDINGS LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. BASIS OF PRESENTATION AND ACCOUNTING POLICIES

Basis of Presentation

Our consolidated balance sheet at September 30, 2007 and the consolidated statements of operations, comprehensive income, shareholders equity and cash flows for the periods ended September 30, 2007 and 2006 have not been audited. The balance sheet at December 31, 2006 is derived from the audited financial statements.

These statements have been prepared in accordance with U.S. Generally Accepted Accounting Principles (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, these financial statements reflect all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of our financial position and results of operations as at the end of and for the periods presented. The results of operations for any interim period are not necessarily indicative of the results for a full year. All significant inter-company accounts and transactions have been eliminated. In these notes, the terms we, us, our, or the Company refer to AXIS Capital Holdings Limited and its direct and indirect subsidiaries.

The following information is unaudited and should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2006. Tabular dollars and share amounts are in thousands, except per share amounts. Certain reclassifications have been made to prior period amounts to conform to the current period presentation. In particular, we reclassified the additional capital above par value on our Series A and B preferred shares from additional paid-in capital to the preferred shares caption in our Consolidated Balance Sheets and Statements of Changes in Shareholders Equity.

Adoption of New Accounting Standards

The terms FAS and FASB used in these notes refer to Statements of Financial Accounting Standards issued by the United States Financial Accounting Standards Board.

On July 13, 2006, the FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109 (FIN 48). This Interpretation prescribes detailed guidance for the financial statement recognition, measurement and disclosure of uncertain tax positions recognized in an enterprise s financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. Under FIN 48, the tax benefits of uncertain tax positions may only be recognized when the position is more-likely-than-not to be sustained upon audit by the relevant taxing authorities. The amount recognized represents the largest amount of tax benefit that is greater than fifty percent likely of being recognized. We adopted the provisions of FIN 48 on January 1, 2007. There were no unrecognized tax benefits as of the date of adoption and there was no change in the liability for unrecognized tax benefits. Our U.S. subsidiaries are not under examination but remain subject to examination in the U.S. for tax years 2003-2006. Our various European operating subsidiaries and branch operations in Ireland, the United Kingdom, and Switzerland are not under examination in any of these tax jurisdictions, but generally remain subject to examination for tax years 2002-2006.

Accounting Standards Not Yet Adopted

In September 2006, the FASB issued FAS No. 157, *Fair Value Measurement* (FAS 157). This Statement provides guidance for using fair value to measure assets and liabilities. Under this standard, the definition of fair value focuses on the price that would be received to sell the asset or paid to transfer the liability (an exit price), not the price that would be paid to acquire the asset or received to assume the liability (an entry price). FAS 157 clarifies that fair value is a market-based measurement, not an entity-specific measurement, and sets out a fair value hierarchy with the highest priority being quoted prices in active markets and the lowest priority to unobservable data. Further, FAS 157 requires tabular disclosures of the fair value measurements by level within the fair value hierarchy. FAS 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Although early adoption was permitted as of January 1, 2007, we have not yet adopted FAS 157 and are evaluating the potential impact of adoption on our financial condition and results of operations.

1. BASIS OF PRESENTATION AND ACCOUNTING POLICIES (Continued)

In February 2007, the FASB issued FAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (FAS 159). This standard permits an entity to irrevocably elect fair value on a contract-by-contract basis as the initial and subsequent measurement attribute for many financial instruments and certain other items including insurance contracts. An entity electing the fair value option would be required to recognize changes in fair value in earnings and provide disclosure that will assist investors and other users of financial information to more easily understand the effect of the company s choice to use fair value on its earnings. Further, the entity is required to display the fair value of those assets and liabilities for which the company has chosen to use fair value on the face of the balance sheet. This standard does not eliminate the disclosure requirements about fair value measurements included in FAS 157 and FAS 107, *Disclosures about Fair Value of Financial Instruments*. FAS 159 is effective for fiscal years beginning after November 15, 2007. Although early adoption was permitted as of January 1, 2007, we have not yet adopted FAS 159.

2. SEGMENT INFORMATION

Our underwriting operations are organized around our two global underwriting platforms, AXIS Insurance and AXIS Re and therefore we have determined that we have two reportable segments, insurance and reinsurance. We do not allocate our assets by segment as we evaluate the underwriting results of each segment separately from the results of our investment portfolio.

Insurance

Our insurance segment provides insurance coverage on a worldwide basis. In January 2007, we announced the reorganization of AXIS Insurance to further strengthen the global operations of the segment. This reorganization reflects the management of AXIS Insurance along global product lines rather than by geographical location. The new structure enables us to design insurance programs on a global basis in alignment with the global needs of many of our clients. Through December 31, 2006, we subdivided our insurance segment into two sub-segments: global insurance and U.S insurance. However, as a result of the reorganization such sub-segment information is no longer relevant.

The following are the lines of business in our insurance segment:

Property: provides physical damage and business interruption coverage primarily for industrial and commercial properties and physical damage, business interruption and liability coverage for onshore energy properties and operations. The book consists of both primary and excess risks, some of which are catastrophe-exposed.

Marine: provides coverage for hull, liability, cargo and specie and recreational marine risks. These risks include property damage or physical loss to ships, pollution damage caused by vessels on a sudden and accidental basis, protection for general cargo and the contents of armored cars, vaults, exhibitions and museums, and specific war related risks. This line of business also provides physical damage, business interruption and liability coverage for offshore energy property and operations.

Terrorism: provides coverage for physical damage and business interruption of an insured following an act of terrorism.

Aviation: includes hull and liability and specific war coverage for passenger and cargo airlines and privately owned aircraft as well as select aviation product liability coverage.

Political risk: generally provides protection against sovereign default or sovereign actions resulting in impairment of cross-border investments for banks and major corporations. It also provides protection on structured credit based transactions where lenders seek to mitigate some of the non-payment risk of their borrowers, both public and private.

2. SEGMENT INFORMATION (Continued)

Professional lines: primarily consists of coverage for directors and officers liability, errors and omissions liability and employment practices liability.

Liability: primarily targets general liability and umbrella and excess liability in the U.S. excess and surplus lines markets. Target classes include mercantile, manufacturing and building/premises, with particular emphasis on commercial and consumer products, commercial construction and miscellaneous general liability.

Accident & Health: primarily provides employee medical coverage for self-insured, small and medium sized employers for losses in excess of a retention.

Reinsurance

Our reinsurance segment provides property and casualty reinsurance to insurance companies on a worldwide basis. The following are the lines of business we write on both a treaty and facultative basis in our reinsurance segment:

Catastrophe: provides protection for most catastrophic losses that are covered in the underlying insurance policies written by our ceding company clients. The exposure in the underlying policies is principally property exposure but also covers other exposures including workers compensation, personal accident and life. The principal perils in this portfolio are hurricane and windstorm, earthquake, flood, tornado, hail and fire. In some instances, terrorism may be a covered peril or the only peril. We underwrite catastrophe reinsurance principally on an excess of loss basis, meaning that our exposure only arises when our customers claims exceed a certain retained amount.

Property: includes reinsurance written on both a pro rata and a per risk basis and covers underlying personal lines and commercial property exposures. Property pro rata treaty reinsurance covers a cedent s aggregate losses from all events in the covered period on a proportional basis. Property per risk treaty reinsurance reinsures a portfolio of particular property risks of ceding companies on an excess of loss basis.

Professional Liability: covers directors and officers liability, employment practices liability, medical malpractice and miscellaneous errors and omissions insurance risks.

Credit and Bond: consists principally of reinsurance of trade credit insurance products and includes both proportional and excess-of loss structures. The underlying insurance indemnifies sellers of goods and services against a payment default by the buyer of those goods and services. Also included in this book is coverage for ceding insurers against losses arising from a broad array of surety bonds issued by bond insurers principally to satisfy regulatory demands in a variety of jurisdictions around the world, but predominantly in Europe.

Motor: provides coverage to insurers for motor liability losses arising out of any one occurrence. The occurrence can involve one or many claimants where the ceding insurer aggregates the claims from the occurrence.

Liability: provides coverage to insurers of standard casualty lines, including auto liability, general liability, personal and commercial umbrella and workers compensation.

Other: includes aviation, engineering, marine, personal accident and crop reinsurance.

2. SEGMENT INFORMATION (Continued)

The following tables summarize the underwriting results of our operating segments:

Three months ended September 30:

	2007			2006		
	Insurance	**Reinsurance**	**Total**	**Insurance**	**Reinsurance**	**Total**
Gross premiums written	**$ 480,729**	**$ 274,495**	**$ 755,224**	$ 453,116	$ 281,794	$ 734,910
Net premiums written	**315,605**	**268,297**	**583,902**	323,618	282,295	605,913
Net premiums earned	**301,925**	**383,920**	**685,845**	327,701	365,079	692,780
Other insurance related income	**610**	**395**	**1,005**	412	392	804
Net losses and loss expenses	**(113,092)**	**(215,101)**	**(328,193)**	(182,280)	(183,678)	(365,958)
Acquisition costs	**(34,721)**	**(65,318)**	**(100,039)**	(40,796)	(62,819)	(103,615)
General and administrative expenses	**(43,262)**	**(15,828)**	**(59,090)**	(36,141)	(12,162)	(48,303)
Underwriting income	**$ 111,460**	**$ 88,068**	**199,528**	$ 68,896	$ 106,812	175,708
Corporate expenses			**(20,723)**			(20,167)
Net investment income			**118,908**			98,787
Net realized investment losses			**(1,192)**			(1,722)
Foreign exchange gains (losses)			**7,202**			(2,738)
Interest expense and financing costs			**(13,929)**			(8,239)
Income before income taxes			**$ 289,794**			$ 241,629
Net loss and loss expense ratio	**37.5%**	**56.0%**	**47.9%**	55.6%	50.3%	52.8%
Acquisition cost ratio	**11.5%**	**17.0%**	**14.6%**	12.4%	17.2%	15.0%
General and administrative expense ratio	**14.3%**	**4.1%**	**11.6%**	11.0%	3.3%	9.9%
Combined ratio	**63.3%**	**77.1%**	**74.1%**	79.0%	70.8%	77.7%

2. SEGMENT INFORMATION (Continued)

Nine months ended September 30:

	2007			2006		
	Insurance	**Reinsurance**	**Total**	**Insurance**	**Reinsurance**	**Total**
Gross premiums written	**$ 1,529,888**	**$ 1,487,337**	**$ 3,017,225**	$ 1,519,771	$ 1,375,259	$ 2,895,030
Net premiums written	**1,004,536**	**1,474,066**	**2,478,602**	1,053,794	1,365,179	2,418,973
Net premiums earned	**915,102**	**1,149,988**	**2,065,090**	973,985	1,031,488	2,005,473
Other insurance related income	**1,737**	**1,901**	**3,638**	1,474	392	1,866
Net losses and loss expenses	**(432,612)**	**(647,102)**	**(1,079,714)**	(486,235)	(610,363)	(1,096,598)
Acquisition costs	**(97,512)**	**(196,411)**	**(293,923)**	(117,006)	(178,145)	(295,151)
General and administrative expenses	**(117,952)**	**(45,794)**	**(163,746)**	(104,069)	(34,377)	(138,446)
Underwriting income	**$ 268,763**	**$ 262,582**	**531,345**	$ 268,149	$ 208,995	477,144
Corporate expenses			**(47,247)**			(43,092)
Net investment income			**357,873**			284,018
Net realized investment losses			**(5,548)**			(22,428)
Foreign exchange gains			**16,477**			25,427
Interest expense and financing costs			**(43,241)**			(24,639)
Income before income taxes			**$ 809,659**			$ 696,430
Net loss and loss expense ratio	**47.3%**	**56.3%**	**52.3%**	49.9%	59.2%	54.7%
Acquisition cost ratio	**10.7%**	**17.1%**	**14.2%**	12.0%	17.3%	14.7%
General and administrative expense ratio	**12.9%**	**4.0%**	**10.2%**	10.7%	3.3%	9.1%
Combined ratio	**70.9%**	**77.4%**	**76.7%**	72.6%	79.8%	78.5%

3. INVESTMENTS

a) Gross unrealized losses

The following tables summarize fixed maturity investments in an unrealized loss position, including the length of time the security has continuously been in the unrealized loss position:

	September 30, 2007					
	12 months or greater		Less than 12 months		Total	
Type of Investment	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
U.S. government and agency securities	**$ 287,144**	**$ (2,836)**	**$ 179,718**	**$ (847)**	**$ 466,862**	**$ (3,683)**
Non-U.S. government securities			**461**	**(2)**	**461**	**(2)**
Corporate securities	**280,180**	**(5,765)**	**533,348**	**(28,091)**	**813,528**	**(33,856)**
Mortgage-backed securities	**1,260,435**	**(31,734)**	**997,024**	**(10,294)**	**2,257,459**	**(42,028)**
Asset-backed securities	**87,689**	**(1,167)**	**271,300**	**(4,068)**	**358,989**	**(5,235)**
Municipals	**94,638**	**(718)**	**33,352**	**(150)**	**127,990**	**(868)**
Total	**$ 2,010,086**	**$ (42,220)**	**$ 2,015,203**	**$ (43,452)**	**$ 4,025,289**	**$ (85,672)**

	December 31, 2006					
	12 months or greater		Less than 12 months		Total	
Type of Investment	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
U.S. government and agency securities	$ 536,403	$ (13,909)	$ 364,668	$ (2,519)	$ 901,071	$ (16,428)
Non-U.S. government securities	4,957	(151)	131,457	(2,620)	136,414	(2,771)
Corporate securities	421,943	(7,556)	449,679	(2,507)	871,622	(10,063)
Mortgage-backed securities	1,420,196	(33,607)	536,721	(3,935)	1,956,917	(37,542)
Asset-backed securities	149,673	(1,961)	166,200	(356)	315,873	(2,317)
Municipals	105,832	(1,803)	130,511	(457)	236,343	(2,260)
Total	$ 2,639,004	$ (58,987)	$ 1,779,236	$ (12,394)	$ 4,418,240	$ (71,381)

At September 30, 2007, 2,010 securities (2006: 1,945) were in an unrealized loss position with a fair value of $4,025 million (2006: $4,418 million) of which 1,416 securities (2006: 1,497) have been in an unrealized loss position for 12 months or greater and have a fair value of $2,010 million (2006: $2,639 million). The unrealized losses from these securities were not a result of credit, collateral or structural issues. In the first nine months of 2007, we recorded an impairment charge of $2.1 million (2006: $1.6 million) relating to 11 securities (2006: 33) that we determined to be other than temporarily impaired which were included in net realized investment losses in the Consolidated Statements of Operations.

3. INVESTMENTS (Continued)

b) Other Investments

The table below summarizes the composition of our other investments portfolio:

	September 30, 2007		December 31, 2006	
Life settlement contracts	$	0%	$ 377,767	33%
Hedge funds	**272,768**	45%	235,377	21%
Collateralized loan obligations	**131,180**	22%	263,621	23%
Credit funds	**154,492**	25%	156,337	14%
Short duration high yield fund	**45,210**	7%	97,562	9%
Other	**8,779**	1%		0%
Total other investments	**$ 612,429**	100%	$ 1,130,664	100%

Life Settlement Contracts

On December 20, 2006, we purchased a 20-year asset-backed note (Note) in the amount of $400.0 million issued by a special-purpose entity (SPE). Through the purchase of this Note, we assumed longevity risk on 222 life insurance policies for a period of 20 years. We determined the SPE was a variable interest entity (VIE) and through ownership of the Note we became its primary beneficiary. Accordingly, we consolidated the SPE, as well as the underlying SPEs, in our December 31, 2006 Consolidated Balance Sheet and eliminated all inter-company balances including the Note. At December 31, 2006, the consolidated assets and liabilities of the SPEs consisted primarily of restricted cash of $65.0 million, life settlement contracts portfolio of $377.8 million and other liability of $42.8 million.

On September 26, 2007, we sold the Note for a cash consideration of $400.0 million to a related party of the SPE (buyer), resulting in the deconsolidation of the SPE (see Note 8). Accordingly, from September 27, 2007, we have not included the results, assets and liabilities of the SPE in our Consolidated Financial Statements. For the three and nine months ended September 30, 2007, we recognized net investment income of $20.6 million and $nil, respectively, relating to the results of the SPE. The $400.0 million repurchase agreement used to finance the purchase of the Note was also terminated on September 26, 2007. For the three and nine months ended September 30, 2007, we recorded interest expense of $6.0 million and $19.2 million, respectively, relating to the repurchase agreement.

Collateralized loan obligations (CLOs)

We have invested in various CLOs with the investments in equity and combination notes. At September 30, 2007, we had invested in 12 (2006: 26) different CLOs with underlying assets totaling $7.4 billion (2006: $13.6 billion). During the three and nine months ended September 30, 2007 we sold 11 and 15 CLOs, respectively, at a net realized loss of $3.8 million and $1.3 million, respectively.

3. INVESTMENTS (Continued)

c) Restricted investments

We are required to maintain assets on deposit with various regulatory authorities to support our insurance and reinsurance operations. The assets on deposit are available to settle insurance and reinsurance liabilities. We also utilize trust accounts in certain large transactions for the benefit of ceding companies. These trust accounts generally take the place of Letter of Credit requirements. The assets in trust as collateral are primarily highly rated fixed maturity securities. Additionally, prior to its termination on September 26, 2007, the repurchase agreement was securitized by the Note. The components of the fair value of restricted assets are as follows:

	September 30 2007	December 31 2006
Assets used for collateral in Trust for inter-company agreements	$ 763,282	$ 734,938
Life settlement contracts		377,767
Deposits with U.S. regulatory authorities	28,668	27,934
Assets used for collateral in Trust for third party agreements	106,582	72,321
Total restricted investments	$ 898,532	$ 1,212,960

4. RESERVE FOR LOSSES AND LOSS EXPENSES

The following table represents an analysis of paid and unpaid losses and loss expenses and a reconciliation of the beginning and ending unpaid losses and loss expenses for the nine months ended September 30:

	2007	2006
Gross unpaid losses and loss expenses at beginning of period	$ 5,015,113	$ 4,743,338
Less reinsurance recoverable balances	(1,293,660)	(1,455,248)
Less reinsurance recoverable balances on paid losses	(65,494)	(62,862)
Net balance at beginning of period	3,655,959	3,225,228
Net incurred losses related to:		
Current year	1,324,690	1,278,704
Prior years	(244,976)	(182,106)
	1,079,714	1,096,598
Net paid losses related to:		
Current year	(99,972)	(76,579)
Prior years	(479,276)	(625,237)
	(579,248)	(701,816)
Foreign exchange loss	30,187	10,382
Net unpaid losses and loss expenses at end of period	4,186,612	3,630,392
Reinsurance recoverable balances	1,247,720	1,315,395
Reinsurance recoverable balances on paid losses	97,047	49,287
Gross unpaid losses and loss expenses at end of period	$ 5,531,379	$ 4,995,074

4. RESERVE FOR LOSSES AND LOSS EXPENSES (Continued)

Net incurred losses include net favorable prior period reserve development of $245 million and $182 million during the nine months ended September 30, 2007 and 2006, respectively. Prior period development arises from changes to loss estimates recognized in the current period that relate to losses incurred in previous calendar years. These reserve changes were made as part of our regular quarterly reserving process and primarily arose from better than expected emergence of actual claims relative to expectations. The net favorable development in 2007 was predominately related to our short tail lines from accident year 2006 and to a lesser extent, accident years 2005 and 2004. For these lines, accident year 2006 has largely proven to be a benign loss year with limited late reported loss activity and minimal deterioration of previously reported claims. The net favorable development in 2006 was related to our short tail lines of business and was primarily generated from accident years 2004 and 2005.

5. STOCK-BASED COMPENSATION

In May 2007, our shareholders approved the AXIS Capital Holdings Limited 2007 Long-Term Equity Compensation Plan (2007 Plan). The 2007 Plan provides for, among other things, the grant of restricted stock awards and units, non-qualified and incentive stock options, and other equity based awards to our employees and directors. The maximum number of our common shares that may be delivered under our 2007 Plan is 5,000,000. As a result of the adoption of the 2007 Plan, the 2003 Long-Term Equity Compensation and 2003 Directors Long-Term Equity Compensation Plan were terminated, except that all related outstanding awards will remain in effect.

During the three months ended September 30, 2007 and 2006, we incurred compensation costs of $8.9 million and $6.9 million, respectively, for all stock compensation plans, and recorded tax benefits thereon of $1.6 million and $0.9 million, respectively. For the first nine months of 2007 and 2006, we incurred compensation costs of $25.4 million and $19.6 million, respectively, for all stock compensation plans, and recorded tax benefits thereon of $5.2 million and $3.6 million, respectively.

The following is a summary of activity under our existing stock compensation plans for the first nine months in 2007 and 2006:

<u>Restricted Stock</u>

	2007			**2006**		
	Number of Restricted Stock		**Weighted Average Grant Date Fair Value**	**Number of Restricted Stock**		**Weighted Average Grant Date Fair Value**
Unvested - beginning of year	**2,229**	**$**	**29.95**	1,176	$	28.40
Granted	**1,594**		**33.02**	1,298		31.00
Vested	**(440)**		**29.67**	(119)		27.61
Forfeited	**(41)**		**31.25**	(104)		21.01
Unvested - end of period	**3,342**	**$**	**31.43**	2,251	$	30.28

At September 30, 2007, there was $55.3 million of unrecognized compensation cost related to restricted stock awards, which is expected to be recognized over a weighted average period of 1.4 years. The total fair value of shares vested during the first nine months of 2007 was $13.0 million.

5. STOCK-BASED COMPENSATION (Continued)

Stock Options

	2007			2006		
	Number of Stock Options		Weighted Average Exercise Price	Number of Stock Options		Weighted Average Exercise Price
Outstanding - beginning of year	**5,147**	**$**	**18.75**	6,174	$	19.11
Granted				45		26.90
Exercised	**(289)**		**22.12**	(912)		18.91
Forfeited	**(5)**		**28.02**	(113)		29.09
Outstanding - end of period	**4,853**	**$**	**18.54**	5,194	$	18.99

At September 30, 2007, there was $0.2 million of unrecognized compensation cost related to the stock option awards which will be fully recognized during the remainder of 2007. The total intrinsic value of options exercised during the first nine months of 2007 was $4.2 million, for which we received proceeds of $6.4 million.

6. EARNINGS PER COMMON SHARE

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

	Three months ended September 30				Nine months ended September 30			
		2007		2006		2007		2006
Basic earnings per common share								
Net income available to common shareholders	**$**	**269,975**	$	226,222	**$**	**749,143**	$	644,807
Weighted average common shares outstanding		**146,845**		149,884		**148,753**		149,657
Basic earnings per common share	**$**	**1.84**	$	1.51	**$**	**5.04**	$	4.31
Diluted earnings per common share								
Net income available to common shareholders	**$**	**269,975**	$	226,222	**$**	**749,143**	$	644,807
Weighted average common shares outstanding		**146,845**		149,884		**148,753**		149,657
Share equivalents:								
Warrants		**13,124**		11,782		**12,937**		11,474
Options		**2,385**		2,010		**2,354**		1,941
Restricted stock		**1,710**		1,025		**1,414**		791
Weighted average common shares outstanding - diluted		**164,064**		164,701		**165,458**		163,863
Diluted earnings per common share	**$**	**1.65**	$	1.37	**$**	**4.53**	$	3.94

For the nine months ended September 30, 2006, there were 1,175,973 restricted shares and options, which would have resulted in the issuance of common shares that were excluded in the computation of diluted earnings per share because the effect would be anti-dilutive. There were no such anti-dilutive restricted shares or options for the three months ended September 30, 2006 or the three and nine months ended September 30, 2007.

7. SHAREHOLDERS EQUITY

On May 10, 2007, we repurchased from Trident II, L.P and affiliated entities, an aggregate of 2,700,000 shares of our common stock at $37.25 per share, for a total purchase price of $100.6 million. These shares were subsequently cancelled. During August, 2007, we repurchased from the open market, a further 2,224,833 shares at an average price of $35.77 per share, for a total cost of $79.6 million, which are held as treasury shares at September 30, 2007.

8. DERIVATIVE INSTRUMENTS

Insurance & Reinsurance Contracts

On September 26, 2007, following the sale of the Note (see Note 3b), we entered into an insurance contract with the buyer whereby we agreed to indemnify the buyer in the event of non payment on the principal of its investment in a new $400.0 million asset-backed note. The asset-backed note has a 10 year term with the full principal amount due at maturity and is collateralized by a portfolio of life settlement contracts and cash held by the same SPE as disclosed in Note 3b. Through our insurance contract, we hold an implicit variable interest in the SPE; but management has determined that the Company is not its primary beneficiary.

We have recorded the insurance contract as a derivative contract, with an initial fair value of $nil. The fair value was determined by calculating the present value of the estimated loss payment on September 26, 2017, and estimated risk margin, net of the present value of the contractual insurance premiums. At September 30, 2007, the fair value of the derivative contract remained at $nil and our maximum exposure to a loss is $400.0 million on an undiscounted basis.

9. COMMITMENTS AND CONTINGENCIES

a) Legal Proceedings

Except as noted below, we are not a party to any material legal proceedings. From time to time, we are subject to routine legal proceedings, including arbitrations, arising in the ordinary course of business. These legal proceedings generally relate to claims asserted by or against us in the ordinary course of insurance or reinsurance operations. In our opinion, the eventual outcome of these legal proceedings is not expected to have a material adverse effect on our financial condition or results of operations.

In 2005, a putative class action lawsuit was filed against our U.S. insurance subsidiaries. In re Insurance Brokerage Antitrust Litigation was filed on August 15, 2005 in the United States District Court for the District of New Jersey and includes as defendants numerous insurance brokers and insurance companies. The lawsuit alleges antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) violations in connection with the payment of contingent commissions and manipulation of insurance bids and seeks damages in an unspecified amount. On October 3, 2006, the District Court granted, in part, motions to dismiss filed by the defendants, and ordered plaintiffs to file supplemental pleadings setting forth sufficient facts to allege their antitrust and RICO claims. After plaintiffs filed their supplemental pleadings, defendants renewed their motions to dismiss. On April 15, 2007, the District Court dismissed without prejudice plaintiffs complaint, as amended, and granted plaintiffs thirty (30) days to file another amended complaint and/or revised RICO Statement and Statements of Particularity. In May 2007, plaintiffs filed (i) a Second Consolidated Amended Commercial Class Action complaint, (ii) a Revised Particularized Statement Describing the Horizontal Conspiracies Alleged in the Second Consolidated Amended Commercial Class Action Complaint, and (iii) a Third Amended Commercial Insurance Plaintiffs RICO Case Statement Pursuant to Local Rule 16.1(B)(4). On June 21, 2007, the defendants filed renewed motions to dismiss. On September 28, 2007, the District Court dismissed with prejudice plaintiffs antitrust and RICO claims and declined to exercise supplemental jurisdiction over plaintiffs remaining state law claims. On October 10, 2007, plaintiffs filed a notice of appeal of all adverse orders and decisions to the United States Court of Appeals for the Third Circuit. We believe that the lawsuit is completely without merit and we continue to vigorously defend the filed action.

9. COMMITMENTS AND CONTINGENCIES (Continued)

b) Dividends for Common Shares and Preferred Shares

On September 7, 2007 the Board of Directors declared a dividend of $0.165 per common share to shareholders of record at September 28, 2007 and payable on October 15, 2007. Additionally, the Board of Directors declared a dividend of $0.453125 per Series A 7.25% Preferred share and a dividend of $1.875 per Series B 7.5% Preferred share. The Series A Preferred share is payable on October 15, 2007, to shareholders of record at September 28, 2007 and the Series B Preferred share is payable on December 3, 2007 to shareholders of record at November 16, 2007.

c) Reinsurance Purchase Commitment

During 2007, we purchased reinsurance coverage for our insurance lines of business. The minimum reinsurance premiums are contractually due on a quarterly basis in advance. Accordingly at September 30, 2007, we have an outstanding reinsurance purchase commitment of $98 million (2006: $47 million).

d) Life Premiums Commitment

At December 31, 2006, we had a commitment of $637 million relating to the estimated life insurance premiums due on our life settlement contracts portfolio. This was due to be paid over the life of the underlying contracts. Following the sale of the Note on September 26, 2007 (see Note 3b), we have no remaining commitment to pay estimated life insurance premiums.

e) Investment Commitment

During September 2007, we made an investment commitment of $75 million in an alternative investment fund, which was fully outstanding at September 30, 2007. We expect to fund this commitment over the next 12 months

Item 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following is a discussion and analysis of our financial condition and results of operations. This should be read in conjunction with the consolidated financial statements and related notes included in Item 1 of this report and also our Management s Discussion and Analysis of Results of Operations and Financial Condition contained in our Annual Report on Form 10-K for the year ended December 31, 2006. Tabular dollars are in thousands, except per share amounts. Amounts in tables may not reconcile due to rounding differences.

Financial Measures

We believe the following financial indicators are important in evaluating our performance and measuring the overall growth in value generated for our common shareholders:

Annualized return on average common equity (ROACE): ROACE represents the level of net income available to common shareholders generated from the average of the opening and closing common shareholders equity during the period. Our objective is to generate superior returns on capital that appropriately reward our shareholders for the risks we assume and to grow revenue only when we deem the returns meet or exceed our requirements. ROACE was 25.0% and 23.9 % for the three and nine months ended September 30, 2007, respectively, compared to 26.0% and 25.8% for the same periods of 2006.

Diluted book value per common share: This is a non-GAAP financial measure; for further information refer to Non-GAAP Financial Measures at the end of Item 2. We consider diluted book value per common share an appropriate measure of our returns to common shareholders, as we believe growth in our book value on a diluted basis ultimately translates into growth of our stock price. Diluted book value per share increased from $24.02 at December 31, 2006 to $27.52 at September 30, 2007. The increase was substantially due to earnings generated in the first nine months of 2007.

Cash dividends per common share: Our dividend policy is an integral part of the value we create for our shareholders. Our quarterly cash dividend was $0.165 per common share in the first three quarters of 2007 compared to $0.15 per common share in the first three quarters of 2006. In December 2006, our Board of Directors authorized a 10% increase in the quarterly dividend.

RESULTS OF OPERATIONS: THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006

Overview

The following tables break out our net income to common shareholders:

	Three months ended September 30			Nine months ended September 30		
	2007	**2006**	**Change**	**2007**	**2006**	**Change**
Underwriting income:						
Insurance	**$ 111,460**	$ 68,896	62%	**$ 268,763**	$ 268,149	0%
Reinsurance	**88,068**	106,812	(18)%	**262,582**	208,995	26%
Net investment income and net realized losses	**117,716**	97,065	21%	**352,325**	261,590	35%
Other revenues and expenses	**(38,127)**	(37,325)	2%	**(106,954)**	(65,844)	62%
Net income	**279,117**	235,448	19%	**776,716**	672,890	15%
Preferred share dividends	**(9,142)**	(9,226)	(1)%	**(27,573)**	(28,083)	(2)%
Net income available to common shareholders	**$ 269,975**	$ 226,222	19%	**$ 749,143**	$ 644,807	16%
Ratios:						
Loss ratio	**47.9%**	52.8%	(4.9)%	**52.3%**	54.7%	(2.4)%
Acquisition cost ratio	**14.6%**	15.0%	(0.4)%	**14.2%**	14.7%	(0.5)%
General and administrative expense ratio	**11.6%**	9.9%	1.7%	**10.2%**	9.1%	1.1%
Combined ratio	**74.1%**	77.7%	(3.6)%	**76.7%**	78.5%	(1.8)%

The main factors contributing towards the 19% increase in income in the third quarter of 2007 compared to the third quarter of 2006 were:

Additional underwriting income in our insurance segment. This was driven by an 18.1 percentage point reduction in the segment loss ratio due to better loss experience in the current accident year (7.2 percentage points) and higher net favorable prior period reserve development (10.9 percentage points).

An increase in net investment income driven by a combination of a larger average investment base and higher yields on our fixed maturity investments.

These favorable factors were partially offset by a reduction in underwriting income in our reinsurance segment. This was driven by a 5.7 percentage point increase in the segment loss ratio which was mostly associated with *a higher incidence of mid-sized natural catastrophe events.*

The main factors contributing towards the 16% increase in income in the first nine months of 2007 compared to the same period in 2006 were:

An increase in net investment income driven by a combination of a higher average investment balances and average investment yields across our investment portfolio.

Additional underwriting income in our reinsurance segment, primarily due to increased net favorable prior period reserve development.

These favorable factors were partially offset by higher interest and income tax expenses and lower foreign exchange gains (all included in other revenues and expenses).

Underwriting Results

Premiums: Gross and net premiums written by segment were as follows:

	Gross Premiums Written					
	Three months ended September 30			Nine months ended September 30		
	2007	2006	Change	2007	2006	Change
Insurance	**$ 480,729**	$ 453,116	6%	**$ 1,529,888**	$ 1,519,771	1%
Reinsurance	**274,495**	281,794	(3)%	**1,487,337**	1,375,259	