NAVIGATORS GROUP INC
Form 10-Q
August 09, 2013
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# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**WASHINGTON, D.C. 20549**

# FORM 10-Q

x **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
**For the quarterly period ended June 30, 2013**

**or**

¨ **Transitional Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
**For the transition period from _________ to _________**

**Commission file number 0-15886**

# The Navigators Group, Inc.

**(Exact name of registrant as specified in its charter)**

| | |
|---|---|
| **Delaware** | **13-3138397** |
| **(State or other jurisdiction of** | **(IRS Employer** |
| **incorporation or organization)** | **Identification No.)** |
| **6 International Drive, Rye Brook, New York** | **10573** |
| **(Address of principal executive offices)** | **(Zip Code)** |

**(914) 934-8999**

**(Registrant s telephone number, including area code)**

**(Former name, former address and former fiscal year, if changed since last report.)**

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definition of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check One):

| | | | |
|---|---|---|---|
| Large accelerated filer | ¨ | Accelerated filer | x |
| Non-accelerated filer | ¨ | Smaller reporting company | ¨ |

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

The number of common shares outstanding as of July 25, 2013 was 14,133,953.

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**THE NAVIGATORS GROUP, INC. AND SUBSIDIARIES**

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**PART I. FINANCIAL INFORMATION**

***Item 1. Financial Statements***

**THE NAVIGATORS GROUP, INC. AND SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS**

(In thousands, except share amounts)

| | June 30, 2013 (Unaudited) | December 31, 2012 |
|---|---|---|
| **ASSETS** | | |
| Investments and cash: | | |
| Fixed maturities, available-for-sale, at fair value (amortized cost: 2013, $1,988,507; 2012, $2,034,765) | $ 2,007,806 | $ 2,121,833 |
| Equity securities, available-for-sale, at fair value (cost: 2013, $115,221; 2012, $85,004) | 138,549 | 101,297 |
| Short-term investments, at cost which approximates fair value | 124,726 | 153,788 |
| Cash | 101,960 | 45,336 |
| Total investments and cash | $ 2,373,041 | $ 2,422,254 |
| Premiums receivable | 394,395 | 320,182 |
| Prepaid reinsurance premiums | 251,046 | 221,015 |
| Reinsurance recoverable on paid losses | 52,569 | 49,282 |
| Reinsurance recoverable on unpaid losses and loss adjustment expenses | 881,962 | 880,139 |
| Deferred policy acquisition costs | 65,109 | 61,005 |
| Accrued investment income | 13,691 | 12,587 |
| Goodwill and other intangible assets | 6,785 | 7,093 |
| Deferred income tax, net | 25,882 | 3,216 |
| Receivable for investments sold | 25 | 4,310 |
| Other assets | 32,005 | 26,587 |
| Total assets | $ 4,096,510 | $ 4,007,670 |
| **LIABILITIES AND STOCKHOLDERS EQUITY** | | |
| Liabilities: | | |
| Reserves for losses and loss adjustment expenses | $ 2,116,384 | $ 2,097,048 |
| Unearned premiums | 729,568 | 642,407 |
| Reinsurance balances payable | 183,683 | 165,813 |
| Senior Notes | 114,502 | 114,424 |
| Current income tax payable, net | 6,324 | 2,133 |
| Payable for investments purchased | 21,428 | 58,345 |
| Accounts payable and other liabilities | 50,669 | 48,015 |
| Total liabilities | $ 3,222,558 | $ 3,128,185 |
| Stockholders equity: | | |
| Preferred stock, $.10 par value, authorized 1,000,000 shares, none issued | $ | $ |
| Common stock, $.10 par value, authorized 50,000,000 shares, issued 17,645,043 shares for 2013 and 17,558,046 shares for 2012 | 1,764 | 1,755 |
| Additional paid-in capital | 333,954 | 329,452 |

| | | |
|---|---|---|
| Treasury stock, at cost (3,511,380 shares for 2013 and 2012) | (155,801) | (155,801) |
| Retained earnings | 656,718 | 628,871 |
| Accumulated other comprehensive income | 37,317 | 75,208 |
| Total stockholders equity | $ 873,952 | $ 879,485 |
| Total liabilities and stockholders equity | $ 4,096,510 | $ 4,007,670 |

The accompanying Notes to Interim Consolidated Financial Statements are an integral part of these financial statements.

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**THE NAVIGATORS GROUP, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF INCOME (Unaudited)**

(In thousands, except share and per share amounts)

| | Three Months Ended June 30, 2013 | Three Months Ended June 30, 2012 | Six Months Ended June 30, 2013 | Six Months Ended June 30, 2012 |
|---|---|---|---|---|
| Gross written premiums | $ 332,128 | $ 322,987 | $ 725,350 | $ 666,136 |
| Revenues: | | | | |
| Net written premiums | $ 198,469 | $ 190,252 | $ 467,921 | $ 433,297 |
| Change in unearned premiums | 7,345 | 5,765 | (59,779) | (54,161) |
| Net earned premiums | 205,814 | 196,017 | 408,142 | 379,136 |
| Net investment income | 14,246 | 15,777 | 27,903 | 27,035 |
| Total other-than-temporary impairment losses | | (496) | (42) | (693) |
| Portion of loss recognized in other comprehensive income (before tax) | | | | 43 |
| Net other-than-temporary impairment losses recognized in earnings | | (496) | (42) | (650) |
| Net realized gains (losses) | 3,345 | 4,217 | 8,159 | 6,059 |
| Other income (expense) | (915) | 387 | (297) | 1,298 |
| Total revenues | $ 222,490 | $ 215,902 | $ 443,865 | $ 412,878 |
| Expenses: | | | | |
| Net losses and loss adjustment expenses | $ 131,148 | $ 123,407 | $ 262,490 | $ 241,392 |
| Commission expenses | 28,391 | 29,503 | 54,946 | 58,953 |
| Other operating expenses | 40,678 | 39,819 | 81,552 | 76,126 |
| Interest expense | 2,052 | 2,049 | 4,103 | 4,098 |
| Total expenses | 202,269 | 194,778 | 403,091 | 380,569 |
| Income (loss) before income taxes | 20,221 | 21,124 | 40,774 | 32,309 |
| Income tax expense (benefit) | 6,284 | 6,225 | 12,927 | 9,506 |
| Net income (loss) | $ 13,937 | $ 14,899 | $ 27,847 | $ 22,803 |
| Net income per common share: | | | | |
| Basic | $ 0.99 | $ 1.06 | $ 1.97 | $ 1.63 |
| Diluted | $ 0.97 | $ 1.05 | $ 1.93 | $ 1.60 |
| Average common shares outstanding: | | | | |
| Basic | 14,131,422 | 14,006,361 | 14,108,747 | 13,992,901 |
| Diluted | 14,428,117 | 14,208,759 | 14,434,232 | 14,245,947 |

The accompanying Notes to Interim Consolidated Financial Statements are an integral part of these financial statements.

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**THE NAVIGATORS GROUP, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)**

(In thousands)

| | Three Months Ended June 30, 2013 | Three Months Ended June 30, 2012 |
|---|---|---|
| Net income (loss) | $ 13,937 | $ 14,899 |
| Other comprehensive income (loss): | | |
| Change in net unrealized gains (losses) on investments: | | |
| Unrealized gains (losses) on investments arising during the period, net of deferred tax of $19,404 and $3,790 in 2013 and 2012, respectively | $ (36,123) | $ 9,113 |
| Reclassification adjustment for net realized (gains) losses included in net income net of deferred tax of $870 and $865 in 2013 and 2012, respectively | (1,616) | (1,607) |
| Change in net unrealized gains (losses) on investments | $ (37,739) | $ 7,506 |
| Change in other-than-temporary impairments: | | |
| Non-credit other-than-temporary impairments arising during the period, net of deferred tax of $13 and $53 in 2013 and 2012, respectively | $ 24 | $ 98 |
| Reclassification adjustment for non-credit other-than-temporary impairment losses recognized in net income | | |
| Change in other-than-temporary impairments | $ 24 | $ 98 |
| Change in foreign currency translation gains (losses), net of deferred tax of $566 and $452 in 2013 and 2012, respectively | (1,051) | (840) |
| Other comprehensive income (loss) | $ (38,766) | $ 6,764 |
| Comprehensive income (loss) | $ (24,829) | $ 21,663 |

| | Six Months Ended June 30, 2013 | Six Months Ended June 30, 2012 |
|---|---|---|
| Net income (loss) | $ 27,847 | $ 22,803 |
| Other comprehensive income (loss): | | |
| Change in net unrealized gains (losses) on investments: | | |
| Unrealized gains (losses) on investments arising during the period, net of deferred tax of $19,037 and $8,237 in 2013 and 2012, respectively | $ (35,335) | $ 17,371 |
| Reclassification adjustment for net realized (gains) losses included in net income net of deferred tax of $2,390 and $719 in 2013 and 2012, respectively | (4,438) | (1,335) |
| Change in net unrealized gains (losses) on investments | $ (39,773) | $ 16,036 |
| Change in other-than-temporary impairments: | | |
| Non-credit other-than-temporary impairments arising during the period, net of deferred tax of $163 and $263 in 2013 and 2012, respectively | $ 303 | $ 489 |
| Reclassification adjustment for non-credit other-than-temporary impairment losses recognized in net income net of deferred tax of $15 in 2012 | | 28 |
| Change in other-than-temporary impairments | $ 303 | $ 517 |
| Change in foreign currency translation gains (losses), net of deferred tax of $975 and $1,851 in 2013 and 2012, respectively | 1,579 | (3,812) |

| | | |
|---|---|---|
| Other comprehensive income (loss) | $ (37,891) | $ 12,741 |
| Comprehensive income (loss) | $ (10,044) | $ 35,544 |

The accompanying Notes to Interim Consolidated Financial Statements are an integral part of these financial statements.

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**THE NAVIGATORS GROUP, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY (Unaudited)**

(In thousands, except share amounts)

| | Common Stock | | Additional Paid-in | Treasury Stock | | Retained | Accumulated Other Comprehensive Income | Total Stockholders |
|---|---|---|---|---|---|---|---|---|
| | Shares | Amount | Capital | Shares | Amount | Earnings | (Loss) | Equity |
| **Balance, December 31, 2012** | 17,558,046 | $ 1,755 | $ 329,452 | 3,511,380 | $ (155,801) | $ 628,871 | $ 75,208 | $ 879,485 |
| Net income | | | | | | 27,847 | | 27,847 |
| Changes in other comprehensive income: | | | | | | | | |
| Change in net unrealized gain (loss) on investments | | | | | | | (39,773) | (39,773) |
| Change in net non-credit other-than-temporary impairment losses | | | | | | | 303 | 303 |
| Change in foreign currency translation gain (loss) | | | | | | | 1,579 | 1,579 |
| Total other comprehensive income | | | | | | | (37,891) | (37,891) |
| Shares issued under stock plan | 86,997 | 9 | 1,028 | | | | | 1,037 |
| Share-based compensation | | | 3,474 | | | | | 3,474 |
| **Balance, June 30, 2013** | 17,645,043 | $ 1,764 | $ 333,954 | 3,511,380 | $ (155,801) | $ 656,718 | $ 37,317 | $ 873,952 |

The accompanying Notes to Interim Consolidated Financial Statements are an integral part of these financial statements.

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**THE NAVIGATORS GROUP, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)**

(In thousands)

| | Six Months Ended June 30, 2013 | Six Months Ended June 30, 2012 |
|---|---|---|
| Operating activities: | | |
| Net income (loss) | $ 27,847 | $ 22,803 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| Depreciation & amortization | 1,953 | 2,040 |
| Deferred income taxes | (2,457) | (9,800) |
| Net realized (gains) losses | (8,159) | (6,059) |
| Net other-than-temporary losses recognized in earnings | 42 | 650 |
| Changes in assets and liabilities: | | |
| Reinsurance recoverable on paid and unpaid losses and loss adjustment expenses | (5,110) | 3,741 |
| Reserves for losses and loss adjustment expenses | 19,336 | 5,845 |
| Prepaid reinsurance premiums | (30,031) | (46,927) |
| Unearned premiums | 87,161 | 101,292 |
| Premiums receivable | (74,213) | (119,834) |
| Deferred policy acquisition costs | (4,104) | (525) |
| Accrued investment income | (1,104) | 413 |
| Reinsurance balances payable | 17,870 | 35,379 |
| Current income tax payable, net | 4,191 | 1,497 |
| Other | 15,263 | 24,513 |
| Net cash provided by (used in) operating activities | $ 48,485 | $ 15,028 |
| Investing activities: | | |
| Fixed maturities | | |
| Redemptions and maturities | $ 121,340 | $ 97,345 |
| Sales | 411,634 | 526,753 |
| Purchases | (491,255) | (747,421) |
| Equity securities | | |
| Sales | 11,439 | 1,600 |
| Purchases | (38,094) | (3,397) |
| Change in payable for securities | (32,632) | 70,265 |
| Net change in short-term investments | 29,062 | (39,763) |
| Purchase of property and equipment | (4,855) | (2,353) |
| Net cash provided by (used in) investing activities | $ 6,639 | $ (96,971) |
| Financing activities: | | |
| Proceeds of stock issued from employee stock purchase plan | $ 374 | $ 313 |
| Proceeds of stock issued from exercise of stock options | 1,126 | 112 |
| Net cash provided by (used in) financing activities | $ 1,500 | $ 425 |
| Increase (decrease) in cash | $ 56,624 | $ (81,518) |
| Cash at beginning of year | 45,336 | 127,360 |
| Cash at end of period | $ 101,960 | $ 45,842 |

| | | |
|---|---|---|
| Supplemental cash information: | | |
| Income taxes paid, net | $ 9,223 | $ 14,188 |
| Interest paid | $ 4,025 | $ 4,025 |
| Issuance of stock to directors | $ 400 | $ 242 |

The accompanying Notes to Interim Consolidated Financial Statements are an integral part of these financial statements.

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THE NAVIGATORS GROUP, INC. AND SUBSIDIARIES

Notes to Interim Consolidated Financial Statements

(Unaudited)

**Note 1. Accounting Policies**

The accompanying interim consolidated financial statements are unaudited and reflect all adjustments which, in the opinion of management, are necessary to fairly present the results of The Navigators Group, Inc. and its subsidiaries for the interim periods presented on the basis of United States generally accepted accounting principles ( GAAP or U.S. GAAP ). All such adjustments are of a normal recurring nature. All significant intercompany transactions and balances have been eliminated. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported revenues and expenses during the reporting periods. The results of operations for any interim period are not necessarily indicative of results for the full year. The term the Company as used herein is used to mean The Navigators Group, Inc. and its subsidiaries, unless the context otherwise requires. The terms Parent or Parent Company are used to mean The Navigators Group, Inc. without its subsidiaries. These financial statements should be read in conjunction with the consolidated financial statements and notes contained in the Company s 2012 Annual Report on Form 10-K.

**Note 2. Recent Accounting Pronouncements**

***Recently Adopted Accounting Pronouncements***

In February 2013, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) 2013 -02 amending Codification topic 220 Comprehensive Income. The amendments do not change the current requirements for reporting net income or other comprehensive income in the financial statements. The guidance requires an entity to present information about significant items reclassified out of Accumulated Other Comprehensive Income ( AOCI ) by component and for items reclassified out of AOCI and into net income, the entity must disclose the effect of such items on the affected net income line item. The Company adopted this standard effective January 1, 2013, and presents this information on the consolidated statements of comprehensive income. Adoption of this standard did not have any impact on the Company s consolidated balance sheets, results of operations or cash flows.

In July 2012, the FASB issued ASU 2012-02 amending Codification topic 350 Intangibles Goodwill and Other. The amendment is intended to reduce cost and complexity, in addition to enhancing consistency of impairment testing guidance among long-lived asset categories by permitting entities to assess qualitative factors to determine whether it is necessary to calculate an asset s fair value when testing an indefinite-lived asset for impairment. The amendment is effective for fiscal years beginning after September 15, 2012. The Company adopted this standard effective January 1, 2013. Adoption of this standard did not have any impact on the Company s consolidated financial position, results of operating or cash flows.

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**Note 3. Segment Information**

The Company classifies its business into two underwriting segments consisting of the Insurance Companies segment ( Insurance Companies ) and the Lloyd s Operations segment ( Lloyd s Operations ), which are separately managed, and a Corporate segment ( Corporate ). Segment data for each of the two underwriting segments include allocations of the operating expenses of the wholly-owned underwriting management companies and the Parent Company s operating expenses and related income tax amounts. The Corporate segment consists of the Parent Company s investment income, interest expense and the related tax effect.

The Company evaluates the performance of each underwriting segment based on its underwriting and GAAP results. The Insurance Companies and the Lloyd s Operations results are measured by taking into account net earned premiums, net losses and loss adjustment expenses ( LAE ), commission expenses, other operating expenses and other income (expense). Each segment maintains its own investments on which it earns income and realizes capital gains or losses. The Company s underwriting performance is evaluated separately from the performance of its investment portfolios.

The Insurance Companies segment consists of Navigators Insurance Company, which includes a United Kingdom Branch (the U.K. Branch ), and Navigators Specialty Insurance Company, which underwrites specialty and professional liability insurance on an excess and surplus lines basis. All of the insurance business written by Navigators Specialty Insurance Company is fully reinsured by Navigators Insurance Company pursuant to a 100% quota share reinsurance agreement. The insurance and reinsurance business written by our Insurance Companies is underwritten through our wholly-owned underwriting management Companies, Navigators Management Company, Inc. ( NMC ) and Navigators Management (UK) Ltd. ( NMUK ).

Our Lloyd s Operations segment includes Navigators Underwriting Agency Ltd. ( NUAL ), a Lloyd s of London ( Lloyd s ) underwriting agency which manages Lloyd s Syndicate 1221 ( Syndicate 1221 ). Our Lloyd s Operations primarily underwrite marine and related lines of business along with offshore energy, construction coverages for onshore energy business and professional liability insurance at Lloyd s through Syndicate 1221. We control 100% of Syndicate 1221 s stamp capacity through our wholly-owned subsidiary, Navigators Corporate Underwriters Ltd. ( NCUL ), which is referred to as a corporate name in the Lloyd s market.

The Insurance Companies and the Lloyd s Operations underwriting results are measured based on underwriting profit or loss and the related combined ratio, which are both non-GAAP measures of underwriting profitability. Underwriting profit or loss is calculated from net earned premiums, less the sum of net losses and LAE, commission expenses, other operating expenses and other income (expense). The combined ratio is derived by dividing the sum of net losses and LAE, commission expenses, other operating expenses and other income (expense) by net earned premiums. A combined ratio of less than 100% indicates an underwriting profit and greater than 100% indicates an underwriting loss.

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Financial data by segment for the three and six months ended June 30, 2013 and 2012 were as follows:

| | Three Month Ended June 30, 2013 | | | |
|---|---|---|---|---|
| In thousands | Insurance Companies | Lloyd s Operations | Corporate[1] | Total |
| Gross written premiums | $ 228,565 | $ 103,563 | $ | $ 332,128 |
| Net written premiums | 143,380 | 55,089 | | 198,469 |
| Net earned premiums | 156,547 | 49,267 | | 205,814 |
| Net losses and loss adjustment expenses | (106,668) | (24,480) | | (131,148) |
| Commission expenses | (20,573) | (8,335) | 517 | (28,391) |
| Other operating expenses | (29,829) | (10,849) | | (40,678) |
| Other income (expense) | 689 | (1,087) | (517) | (915) |
| Underwriting profit (loss) | $ 166 | $ 4,516 | $ | $ 4,682 |
| Net investment income | 12,515 | 1,728 | 3 | 14,246 |
| Net realized gains (losses) | 3,099 | 242 | 4 | 3,345 |
| Interest expense | | | (2,052) | (2,052) |
| Income (loss) before income taxes | $ 15,780 | $ 6,486 | $ (2,045) | $ 20,221 |
| Income tax expense (benefit) | 4,785 | 2,206 | (707) | 6,284 |
| Net income (loss) | $ 10,995 | $ 4,280 | $ (1,338) | $ 13,937 |
| Identifiable assets | $ 3,097,754 | $ 947,736 | $ 51,020 | $ 4,096,510 |
| Losses and loss adjustment expenses ratio | 68.1% | 49.7% | | 63.7% |
| Commission expense ratio | 13.1% | 16.9% | | 13.8% |
| Other operating expense ratio [2] | 18.7% | 24.2% | | 20.2% |
| Combined ratio | 99.9% | 90.8% | | 97.7% |

(1) - Includes Corporate segment intercompany eliminations.
(2) - Includes Other operating expenses and Other income.

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| In thousands | Three Month Ended June 30, 2012 Insurance Companies | Lloyd s Operations | Corporate[1] | Total |
|---|---|---|---|---|
| Gross written premiums | $ 214,064 | $ 108,923 | $ | $ 322,987 |
| Net written premiums | 134,065 | 56,187 | | 190,252 |
| Net earned premiums | 141,577 | 54,440 | | 196,017 |
| Net losses and loss adjustment expenses | (100,003) | (23,404) | | (123,407) |
| Commission expenses | (21,117) | (8,938) | 552 | (29,503) |
| Other operating expenses | (28,914) | (10,905) | | (39,819) |
| Other income (expense) | 879 | 60 | (552) | 387 |
| Underwriting profit (loss) | $ (7,578) | $ 11,253 | $ | $ 3,675 |
| Net investment income | 13,286 | 2,454 | 37 | 15,777 |
| Net realized gains (losses) | 2,325 | 1,396 | | 3,721 |
| Interest expense | | | (2,049) | (2,049) |
| Income (loss) before income taxes | $ 8,033 | $ 15,103 | $ (2,012) | $ 21,124 |
| Income tax expense (benefit) | 2,101 | 5,207 | (1,083) | 6,225 |
| Net income (loss) | $ 5,932 | $ 9,896 | $ (929) | $ 14,899 |
| Identifiable assets | $ 2,933,334 | $ 967,862 | $ 37,870 | $ 3,939,066 |
| Losses and loss adjustment expenses ratio | 70.6% | 43.0% | | 63.0% |
| Commission expense ratio | 14.9% | 16.4% | | 15.1% |
| Other operating expense ratio [2] | 19.9% | 19.9% | | 20.0% |
| Combined ratio | 105.4% | 79.3% | | 98.1% |

(1) - Includes Corporate segment intercompany eliminations.

(2) - Includes Other operating expenses and Other income.

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| In thousands | Six Month Ended June 30, 2013<br>Insurance Companies | Lloyd s Operations | Corporate[1] | Total |
|---|---|---|---|---|
| Gross written premiums | $ 530,193 | $ 195,157 | $ | $ 725,350 |
| Net written premiums | 359,699 | 108,222 | | 467,921 |
| Net earned premiums | 310,878 | 97,264 | | 408,142 |
| Net losses and loss adjustment expenses | (213,653) | (48,837) | | (262,490) |
| Commission expenses | (39,090) | (16,956) | 1,100 | (54,946) |
| Other operating expenses | (59,172) | (22,380) | | (81,552) |
| Other income (expense) | 1,348 | (545) | (1,100) | (297) |
| Underwriting profit (loss) | $ 311 | $ 8,546 | $ | $ 8,857 |
| Net investment income | 24,466 | 3,430 | 7 | 27,903 |
| Net realized gains (losses) | 7,891 | 222 | 4 | 8,117 |
| Interest expense | | | (4,103) | (4,103) |
| Income (loss) before income taxes | $ 32,668 | $ 12,198 | $ (4,092) | $ 40,774 |
| Income tax expense (benefit) | 10,199 | 4,242 | (1,514) | 12,927 |
| Net income (loss) | $ 22,469 | $ 7,956 | $ (2,578) | $ 27,847 |
| Identifiable assets | $ 3,097,754 | $ 947,736 | $ 51,020 | $ 4,096,510 |
| Losses and loss adjustment expenses ratio | 68.7% | 50.2% | | 64.3% |
| Commission expense ratio | 12.6% | 17.4% | | 13.5% |
| Other operating expense ratio [2] | 18.6% | 23.6% | | 20.0% |
| Combined ratio | 99.9% | 91.2% | | 97.8% |

(1) - Includes Corporate segment intercompany eliminations.

(2) - Includes Other operating expenses and Other income.

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| In thousands | Six Month Ended June 30, 2012 Insurance Companies | Lloyd s Operations | Corporate[1] | Total |
|---|---|---|---|---|
| Gross written premiums | $ 462,402 | $ 203,734 | $ | $ 666,136 |
| Net written premiums | 315,315 | 117,982 | | 433,297 |
| Net earned premiums | 273,125 | 106,011 | | 379,136 |
| Net losses and loss adjustment expenses | (191,180) | (50,212) | | (241,392) |
| Commission expenses | (40,418) | (19,824) | 1,289 | (58,953) |
| Other operating expenses | (54,259) | (21,867) | | (76,126) |
| Other income (expense) | 2,521 | 66 | (1,289) | 1,298 |
| Underwriting profit (loss) | $ (10,211) | $ 14,174 | $ | $ 3,963 |
| Net investment income | 22,221 | 4,737 | 77 | 27,035 |
| Net realized gains (losses) | 4,200 | 1,209 | | 5,409 |
| Interest expense | | | (4,098) | (4,098) |
| Income (loss) before income taxes | $ 16,210 | $ 20,120 | $ (4,021) | $ 32,309 |
| Income tax expense (benefit) | 3,980 | 6,933 | (1,407) | 9,506 |
| Net income (loss) | $ 12,230 | $ 13,187 | $ (2,614) | $ 22,803 |
| Identifiable assets | $ 2,933,334 | $ 967,862 | $ 37,870 | $ 3,939,066 |
| Losses and loss adjustment expenses ratio | 70.0% | 47.4% | | 63.7% |
| Commission expense ratio | 14.8% | 18.7% | | 15.5% |
| Other operating expense ratio [2] | 18.9% | 20.5% | | 19.8% |
| Combined ratio | 103.7% | 86.6% | | 99.0% |

(1) - Includes Corporate segment intercompany eliminations.

(2) - Includes Other operating expenses and Other income.

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The following tables provide additional financial data by segment for the three and six months ended June 30, 2013 and 2012:

| | Three Months Ended June 30, 2013 | | |
|---|---|---|---|
| **In thousands** | **Insurance Companies** | **Lloyd s Operations** | **Total** |
| Gross written premiums: | | | |
| Marine | $ 43,077 | $ 45,893 | $ 88,970 |
| Property casualty | 152,095 | 41,217 | 193,312 |
| Professional liability | 33,393 | 16,453 | 49,846 |
| Total | $ 228,565 | $ 103,563 | $ 332,128 |
| Net written premiums: | | | |
| Marine | $ 27,366 | $ 34,060 | $ 61,426 |
| Property casualty | 90,711 | 12,181 | 102,892 |
| Professional liability | 25,303 | 8,848 | 34,151 |
| Total | $ 143,380 | $ 55,089 | $ 198,469 |
| Net earned premiums: | | | |
| Marine | $ 31,798 | $ 34,623 | $ 66,421 |
| Property casualty | 99,477 | 8,562 | 108,039 |
| Professional liability | 25,272 | 6,082 | 31,354 |
| Total | $ 156,547 | $ 49,267 | $ 205,814 |

| | Three Months Ended June 30, 2012 | | |
|---|---|---|---|
| **In thousands** | **Insurance Companies** | **Lloyd s Operations** | **Total** |
| Gross written premiums: | | | |
| Marine | $ 49,896 | $ 47,037 | $ 96,933 |
| Property casualty | 130,627 | 48,978 | 179,605 |
| Professional liability | 33,541 | 12,908 | 46,449 |
| Total | $ 214,064 | $ 108,923 | $ 322,987 |
| Net written premiums: | | | |
| Marine | $ 31,786 | $ 33,492 | $ 65,278 |
| Property casualty | 76,842 | 15,705 | 92,547 |
| Professional liability | 25,437 | 6,990 | 32,427 |
| Total | $ 134,065 | $ 56,187 | $ 190,252 |
| Net earned premiums: | | | |
| Marine | $ 35,535 | $ 34,272 | $ 69,807 |
| Property casualty | 82,175 | 15,272 | 97,447 |
| Professional liability | 23,867 | 4,896 | 28,763 |
| Total | $ 141,577 | $ 54,440 | $ 196,017 |

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| In thousands | Six Months Ended June 30, 2013 Insurance Companies | Lloyd s Operations | Total |
|---|---|---|---|
| Gross written premiums: | | | |
| Marine | $ 93,924 | $ 99,537 | $ 193,461 |
| Property casualty | 371,059 | 66,275 | 437,334 |
| Professional liability | 65,210 | 29,345 | 94,555 |
| Total | $ 530,193 | $ 195,157 | $ 725,350 |
| Net written premiums: | | | |
| Marine | $ 68,507 | $ 73,618 | $ 142,125 |
| Property casualty | 240,662 | 19,493 | 260,155 |
| Professional liability | 50,530 | 15,111 | 65,641 |
| Total | $ 359,699 | $ 108,222 | $ 467,921 |
| Net earned premiums: | | | |
| Marine | $ 68,523 | $ 68,668 | $ 137,191 |
| Property casualty | 192,195 | 16,441 | 208,636 |
| Professional liability | 50,160 | 12,155 | 62,315 |
| Total | $ 310,878 | $ 97,264 | $ 408,142 |

| In thousands | Six Months Ended June 30, 2012 Insurance Companies | Lloyd s Operations | Total |
|---|---|---|---|
| Gross written premiums: | | | |
| Marine | $ 111,761 | $ 108,812 | $ 220,573 |
| Property casualty | 286,546 | 73,274 | 359,820 |
| Professional liability | 64,095 | 21,648 | 85,743 |
| Total | $ 462,402 | $ 203,734 | $ 666,136 |
| Net written premiums: | | | |
| Marine | $ 74,651 | $ 81,550 | $ 156,201 |
| Property casualty | 191,374 | 25,060 | 216,434 |
| Professional liability | 49,290 | 11,372 | 60,662 |
| Total | $ 315,315 | $ 117,982 | $ 433,297 |
| Net earned premiums: | | | |
| Marine | $ 70,810 | $ 67,536 | $ 138,346 |
| Property casualty | 156,543 | 29,774 | 186,317 |
| Professional liability | 45,772 | 8,701 | 54,473 |
| Total | $ 273,125 | $ 106,011 | $ 379,136 |

The Insurance Companies net earned premiums include $12.7 million and $18.2 million of net earned premiums from the U.K. Branch for the three months ended June 30, 2013 and 2012, respectively, and $22.8 million and $39.1 million of net earned premiums from the U.K. Branch for the six months ended June 30, 2013 and 2012, respectively.

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**Note 4. Reinsurance Ceded**

The Company s ceded earned premiums were $115.3 million and $120.7 million for the three months ended June 30, 2013 and 2012 and $226.3 million and $185.8 million for the six months ended June 30, 2013 and 2012, respectively.

The Company s ceded incurred losses were $77.6 million and $61.7 million for the three months ended June 30, 2013 and 2012 and $131.1 million and $123.2 million for the six months ended June 30, 2013 and 2012, respectively.

The following table lists the Company s 20 largest reinsurers measured by the amount of reinsurance recoverable for ceded losses and loss adjustment expenses ( LAE ) and ceded unearned premium (constituting 73.4% of the total recoverable), together with the reinsurance recoverable and collateral as of June 30, 2013, and the reinsurers ratings from A.M. Best Company ( A.M. Best ) and Standard & Poor s ( S&P ):

| | Reinsurance Recoverables | | | | | |
|---|---|---|---|---|---|---|
| In thousands | Unearned Premium | Paid/ Unpaid Losses | Total [1] | Collateral Held [2] | A.M. Best | S&P |
| National Indemnity Company | $ 53,397 | $ 64,605 | $ 118,002 | $ 35,018 | A++ | AA+ |
| Swiss Reinsurance America Corporation | 5,949 | 86,684 | 92,633 | 7,685 | A+ | AA- |
| Transatlantic Reinsurance Company | 20,597 | 70,872 | 91,469 | 8,971 | A | A+ |
| Everest Reinsurance Company | 21,219 | 69,516 | 90,735 | 8,025 | A+ | A+ |
| Munich Reinsurance America Inc. | 7,923 | 80,115 | 88,038 | 4,133 | A+ | AA- |
| Lloyd s Syndicate #2003 | 10,938 | 39,381 | 50,319 | 12,490 | A | A+ |
| Partner Reinsurance Europe | 10,485 | 37,600 | 48,085 | 20,108 | A+ | A+ |
| Scor Global P&C SE | 11,642 | 27,768 | 39,410 | 10,455 | A | A+ |
| Allied World Reinsurance | 12,803 | 26,519 | 39,322 | 3,872 | A | A |
| Tower Insurance Company | 13,397 | 16,537 | 29,934 | 8,462 | A- | NR |
| General Reinsurance Corporation | 194 | 25,967 | 26,161 | 1,092 | A++ | AA+ |
| Validus Reinsurance Ltd. | 2,695 | 22,860 | 25,555 | 12,884 | A | A |
| Berkley Insurance Company | 1,653 | 19,389 | 21,042 | 405 | A+ | A+ |
| Scor Holding (Switzerland) AG | 691 | 18,159 | 18,850 | 8,681 | A | A+ |
| AXIS Re Europe | 4,182 | 13,102 | 17,284 | 4,718 | A | A+ |
| Atlantic Specialty Insurance | 8,658 | 7,550 | 16,208 | 3,102 | A | A- |
| Employers Mutual Casualty Company | 10,867 | 5,317 | 16,184 | 10,557 | A | NR |
| Platinum Underwriters Re | 304 | 13,899 | 14,203 | 1,696 | A | A- |
| Ace Property and Casualty Insurance Company | 730 | 13,297 | 14,027 | | A+ | AA- |
| QBE Reinsurance Corp | 6,362 | 6,950 | 13,312 | 2,094 | A | A+ |
| Top 20 Reinsurers | $ 204,686 | $ 666,087 | $ 870,773 | $ 164,448 | | |
| Others | 46,360 | 268,444 | 314,804 | 79,424 | | |
| Total | $ 251,046 | $ 934,531 | $ 1,185,577 | $ 243,872 | | |

(1) - Net of reserve for uncollectible reinsurance of approximately $10.8 million.

(2) - Collateral of $243.9 million consists of $183.7 million in ceded balances payable, $57.2 million in letters of credit, and $3.0 million of other balances held by the Company s Insurance Companies and Lloyd s Operations.

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**Note 5. Stock-Based Compensation**

Stock-based compensation granted under the Company s stock plans is expensed in tranches over the vesting period. Options and non-performance based grants generally vest equally over a three or four year period and the options have a maximum term of ten years. Certain non-performance based grants vest over five years with one-third vesting in each of the third, fourth and fifth years. The Company s performance based share grants generally consist of two types of awards. The restricted stock units issued in 2011 and after will cliff vest on the third anniversary of the date of grant, with 50% vesting in full, and 50% dependent on the rate of compound annual growth in book value per share for the three years immediately prior to the vesting date, with actual shares that vest ranging between 150% to 0% of that portion of the original award. Those performance based restricted stock units issued prior to 2011 generally vest over five years with one-third vesting in each of the third, fourth and fifth years, dependent on the rolling three-year average return on equity based on the three years prior to the year in which the vesting occurs, with actual shares that vest ranging between 150% to 0% of the original award.

The amounts charged to expense for stock-based compensation for the three and six months ended June 30, 2013 and 2012 are presented in the following table:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| **In thousands** | **2013** | **2012** | **2013** | **2012** |
| Restricted stock units | $ 2,116 | $ 1,974 | $ 3,474 | $ 3,186 |
| Directors restricted stock grants(1) | 106 | 60 | 206 | 120 |
| Employee stock purchase plan | 38 | 41 | 47 | 15 |
| Total stock based compensation | $ 2,260 | $ 2,075 | $ 3,727 | $ 3,321 |

(1) - Relates to non-employee directors serving on the Parent Company s Board of Directors, all of whom have been elected by the Company s stockholders, as well as non-employee directors serving on NUAL s Board of Directors.

**Note 6. Lloyd s Syndicate 1221**

The Company s Lloyd s Operations included in the consolidated financial statements represents its participation in Syndicate 1221. Syndicate 1221 s stamp capacity is £195 million ($296 million) for the 2013 underwriting year compared to £184 million ($300 million) for the 2012 underwriting year. Stamp capacity is a measure of the amount of premiums a Lloyd s syndicate is authorized to write based on a business plan approved by the Council of Lloyd s. Syndicate 1221 s stamp capacity is expressed net of commission (as is standard at Lloyd s). The Syndicate 1221 premiums recorded in the Company s financial statements are gross of commission. The Company controlled 100% of Syndicate 1221 s stamp capacity for the 2013 and 2012 underwriting years through its wholly-owned Lloyd s corporate member.

The Company provides letters of credit and posts cash to Lloyd s to support its participation in Syndicate 1221 s stamp capacity. As of June 30, 2013, the Company had provided letters of credit of $142.6 million and has $0.8 million of cash collateral posted. If Syndicate 1221 increases its stamp capacity and the Company participates in the additional stamp capacity, or if Lloyd s changes the capital requirements, the Company may be required to supply additional collateral acceptable to Lloyd s. If the Company is unwilling or unable to provide additional acceptable collateral, the Company will be required to reduce its participation in the stamp capacity of Syndicate 1221. The letters of credit are provided through a credit facility with a consortium of banks which provides the Company with the ability to have letters of credit issued to support Syndicate 1221 s stamp capacity at Lloyd s for the 2013 and 2014 underwriting years, as well as open prior years. If any letters of credit remain outstanding under the facility after December 31, 2014, we would be required to post additional collateral to secure the remaining letters of credit. If the credit facility is not renewed prior to December 31, 2014, the Company will need to find internal and/or external sources to provide either letters of credit or other collateral in order to continue to participate in Syndicate 1221. The credit facility is collateralized by all of the common stock of Navigators Insurance Company. Refer to Note 11, *Credit Facility*, for additional information.

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**Note 7. Income Taxes**

The Company is subject to the tax laws and regulations of the United States ( U.S. ) and the foreign countries in which it operates. The Company files a consolidated U.S. Federal tax return, which includes all domestic subsidiaries and the U.K. Branch. The income from the foreign operations is designated as either U.S. connected income or non-U.S. connected income. Lloyd s is required to pay U.S. income tax on U.S. connected income written by Lloyd s syndicates. Lloyd s and the U.S. Internal Revenue Service ( IRS ) have entered into an agreement whereby the amount of tax due on U.S. connected income is calculated by Lloyd s and remitted directly to the IRS. These amounts are then charged to the corporate member in proportion to its participation in the relevant syndicates. The Company s corporate member is subject to this agreement and will receive United Kingdom ( U.K. ) tax credits in the U.K. for any U.S. income tax incurred up to the U.K. income tax charged on the U.S. connected income. The non-U.S. connected insurance income would generally constitute taxable income under the Subpart F income section of the U.S. Internal Revenue Code ( Subpart F ) since less than 50% of Syndicate 1221 s premiums are derived within the U.K. and would therefore be subject to U.S. taxation when the Lloyd s year of account closes. Taxes are accrued at a 35% rate on the Company s foreign source insurance income and foreign tax credits, where available, are utilized to offset U.S. tax as permitted. The Company s effective tax rate for Syndicate 1221 taxable income could substantially exceed 35% to the extent the Company is unable to offset U.S. taxes paid under Subpart F tax regulations with U.K. tax credits on future underwriting year distributions. U.S. taxes are not accrued on the earnings of the Company s foreign agencies as these earnings are not includable as Subpart F income in the current year. These earnings were subject to taxes under U.K. tax regulations at a 26% rate through March 31, 2012. A finance bill was enacted in the U.K. that reduced the U.K. corporate tax rate from 26% to 24% effective April 2012 and from 24% to 23% effective April 2013. The effect of such tax rate change was not material.

The Company has not provided for U.S. income taxes on approximately $17.2 million of undistributed earnings of its non-U.S. subsidiaries since it is intended that those earnings will be reinvested indefinitely in those subsidiaries. If a future determination is made that those earnings no longer are intended to be reinvested indefinitely in those subsidiaries, U.S. income taxes of approximately $1.8 million, assuming all foreign tax credits are realized, would be included in the tax provision at that time and would be payable if those earnings were distributed to the Company.

Unrecognized tax benefits are differences between tax positions taken in the tax returns and benefits recognized in the financial statements. The Company has no unrecognized tax benefits as of June 30, 2013 and 2012. The Company did not incur any interest or penalties related to unrecognized tax benefits for the three and six months ended June 30, 2013 and 2012. The Company currently is under examination by the Internal Revenue Service for taxable years 2010 and 2011, and generally is subject to U.S. Federal, state or local, or foreign tax examinations by tax authorities for 2009 and subsequent years.

The Company recorded income tax expense of $6.3 million and $12.9 million for the three and six months ended June 30, 2013 compared to $6.2 million and $9.5 million for the same period in 2012, resulting in an effective tax rate of 31.1% and 31.7% for the three and six months ended June 30, 2013 and 29.5% and 29.4% for the comparable period in 2012.

The Company had state and local deferred tax assets amounting to potential future tax benefits of $0.5 million as of both June 30, 2013 and December 31, 2012, respectively. Included in the deferred tax assets are state and local net operating loss carry-forwards of $0.2 million for both June 30, 2013 and December 31, 2012. A valuation allowance was established for the full amount of these potential future tax benefits due to the uncertainty associated with their realization. The Company s state and local tax carry-forwards as of June 30, 2013 expire from 2023 to 2031.

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**Note 8. Senior Notes due May 1, 2016**

On April 17, 2006, we completed a public debt offering of $125 million principal amount of 7% senior unsecured notes (the Senior Notes ) and received net proceeds of $123.5 million. The principal amount of the Senior Notes is payable in a single installment on May 1, 2016. In April 2009, the Company repurchased $10.0 million aggregate principal amount of the Senior Notes from an unaffiliated note holder on the open market for $7.0 million, which generated a $3.0 million pre-tax gain that was reflected in Other income. The Senior Notes liability as of June 30, 2013 was $114.5 million. The unamortized discount at June 30, 2013 was $0.5 million. The aggregate principal amount of the Senior Notes that will be repaid on May 1, 2016, as a result of these transactions, is $115.0 million.

The fair value of the Senior Notes was $125.8 million and $123.2 million as of June 30, 2013 and December 31, 2012, respectively. The fair value was determined using quoted prices for similar instruments in active markets and is classified as Level 2 within the fair value hierarchy as defined by the accounting guidance for fair value measurements.

Interest is payable on the Senior Notes each May 1 and November 1. The effective interest rate related to the Senior Notes, based on the proceeds net of discount and all issuance costs, approximates 7.17%. Interest expense on the Senior Notes for the three and six months ended each of June 30, 2013 and 2012 was approximately $2.1 million and $4.1 million, respectively.

The Senior Notes, the Company s only senior unsecured obligation, will rank equally with any future senior unsecured indebtedness. The Company may redeem the Senior Notes at any time and from time to time, in whole or in part, at a make-whole redemption price. The terms of the Senior Notes contain various restrictive business and financial covenants typical for debt obligations of this type, including limitations on mergers, liens and dispositions of the common stock of certain subsidiaries. As of June 30, 2013, the Company was in compliance with all such covenants.

**Note 9. Commitments and Contingencies**

In the ordinary course of conducting business, the Company s subsidiaries are involved in various legal proceedings, either indirectly as insurers for parties or directly as defendants. Most of these proceedings consist of claims litigation involving the Company s subsidiaries as either (a) liability insurers defending or providing indemnity for third party claims brought against insureds or (b) insurers defending first party coverage claims brought against them. The Company accounts for such activity through the establishment of unpaid loss and loss adjustment reserves. The Company s management believes that the ultimate liability, if any, with respect to such ordinary-course claims litigation, after consideration of provisions made for potential losses and cost of defense, will not be material to the Company s consolidated financial condition, results of operations, or cash flows.

The Company s subsidiaries are also from time to time involved with other legal actions, some of which assert claims for substantial amounts. These actions include claims asserting extra contractual obligations, such as claims involving allegations of bad faith in the handling of claims or the underwriting of policies. In general, the Company believes it has valid defenses to these cases. The Company s management expects that the ultimate liability, if any, with respect to future extra-contractual matters will not be material to its consolidated financial position. Nonetheless, given the large or indeterminate amounts sought in certain of these matters, and the inherent unpredictability of litigation, an adverse outcome in such matters could, from time to time, have a material adverse outcome on the Company s consolidated results of operations or cash flows in a particular fiscal quarter or year.

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**Note 10. Investments**

The following tables set forth the Company s cash and investments as of June 30, 2013 and December 31, 2012. The table below includes other-than-temporarily impaired ( OTTI ) securities recognized within other comprehensive income ( OCI ).

| In thousands | June 30, 2013 Fair Value | Gross Unrealized Gains | Gross Unrealized (Losses) | Cost or Amortized Cost |
|---|---|---|---|---|
| Fixed maturities: | | | | |
| U.S. Treasury bonds, agency bonds and foreign government bonds | $ 464,167 | $ 3,538 | $ (7,492) | $ 468,121 |
| States, municipalities and political subdivisions | 452,084 | 10,281 | (13,114) | 454,917 |
| Mortgage-backed and asset-backed securities: | | | | |
| Agency mortgage-backed securities | 320,150 | 7,782 | (4,645) | 317,013 |
| Residential mortgage obligations | 37,335 | 1,196 | (221) | 36,360 |
| Asset-backed securities | 75,311 | 747 | (113) | 74,677 |
| Commercial mortgage-backed securities | 173,388 | 8,731 | (514) | 165,171 |
| Subtotal | $ 606,184 | $ 18,456 | $ (5,493) | $ 593,221 |
| Corporate bonds | 485,371 | 16,285 | (3,162) | 472,248 |
| Total fixed maturities | $ 2,007,806 | $ 48,560 | $ (29,261) | $ 1,988,507 |
| Equity securities common stocks | 138,549 | 25,238 | (1,910) | 115,221 |
| Short-term investments | 124,726 | | | 124,726 |
| Cash | 101,960 | | | 101,960 |
| Total | $ 2,373,041 | $ 73,798 | $ (31,171) | $ 2,330,414 |

| In thousands | December 31, 2012 Fair Value | Gross Unrealized Gains | Gross Unrealized (Losses) | Cost or Amortized Cost |
|---|---|---|---|---|
| Fixed maturities: | | | | |
| U.S. Treasury bonds, agency bonds and foreign government bonds | $ 649,692 | $ 8,654 | $ (36) | $ 641,074 |
| States, municipalities and political subdivisions | 322,947 | 18,712 | (380) | 304,615 |
| Mortgage-backed and asset-backed securities: | | | | |
| Agency mortgage-backed securities | 384,445 | 13,652 | (204) | 370,997 |
| Residential mortgage obligations | 38,692 | 1,053 | (549) | 38,188 |
| Asset-backed securities | 50,382 | 1,133 | (49) | 49,298 |
| Commercial mortgage-backed securities | 204,821 | 17,996 | (18) | 186,843 |
| Subtotal | $ 678,340 | $ 33,834 | $ (820) | $ 645,326 |
| Corporate bonds | 470,854 | 27,129 | (25) | 443,750 |
| Total fixed maturities | $ 2,121,833 | $ 88,329 | $ (1,261) | $ 2,034,765 |
| Equity securities common stocks | 101,297 | 16,919 | (626) | 85,004 |
| Short-term investments | 153,788 | | | 153,788 |
| Cash | 45,336 | | | 45,336 |
| Total | $ 2,422,254 | $ 105,248 | $ (1,887) | $ 2,318,893 |

As of June 30, 2013 and December 31, 2012, debt securities for which non-credit OTTI was previously recognized and included in other comprehensive income are now in an unrealized gains position of $0.5 million and $20 thousand, respectively.

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The fair value of the Company s investment portfolio may fluctuate significantly in response to various factors such as changes in interest rates, investment quality ratings, equity prices, foreign exchange rates and credit spreads. The Company does not have the intent to sell nor is it more likely than not that it will have to sell debt securities in unrealized loss positions that are not other-than-temporarily impaired before recovery. For structured securities, default probability and severity assumptions differ based on property type, vintage and the stress of the collateral. We do not intend to sell any of these securities and it is more likely than not that we will not be required to sell these securities before the recovery of the amortized cost basis. For equity securities, the Company also considers its intent to hold securities as part of the process of evaluating whether a decline in fair value represents an other-than-temporary decline in value. The Company may realize investment losses to the extent its liquidity needs require the disposition of fixed maturity securities in unfavorable interest rate, liquidity or credit spread environments. Significant changes in the factors the Company considers when evaluating investments for impairment losses could result in a significant change in impairment losses reported in the consolidated financial statements.

The contractual maturity dates for fixed maturity securities categorized by the number of years until maturity as of June 30, 2013 are shown in the following table:

| | June 30, 2013 | |
|---|---|---|
| **In thousands** | **Fair Value** | **Amortized Cost** |
| Due in one year or less | $ 117,677 | $ 116,999 |
| Due after one year through five years | 576,742 | 566,164 |
| Due after five years through ten years | 462,171 | 461,911 |
| Due after ten years | 245,032 | 250,212 |
| Mortgage- and asset-backed securities | 606,184 | 593,221 |
| Total | $ 2,007,806 | $ 1,988,507 |

Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties. Due to the periodic repayment of principal, the mortgage-backed and asset-backed securities are estimated to have an effective maturity of approximately 4.6 years.

The following table shows the amount and percentage of the Company s fixed maturities as of June 30, 2013 by S&P credit rating or, if an S&P rating is not available, the equivalent Moody s Investor Services ( Moody s ) rating. The table includes fixed maturities at fair value, and the total rating is the weighted average quality rating.

| | | June 30, 2013 | |
|---|---|---|---|
| **In thousands** | **Rating** | **Fair Value** | **Percent of Total** |
| Rating description: | | | |
| Extremely strong | AAA | $ 293,952 | 15% |
| Very strong | AA | 1,088,098 | 53% |
| Strong | A | 454,692 | 23% |
| Adequate | BBB | 152,317 | 8% |
| Speculative | BB & Below | 15,073 | 1% |
| Not rated | NR | 3,674 | 0% |
| Total | AA | $ 2,007,806 | 100% |

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The following table summarizes all securities in a gross unrealized loss position as of June 30, 2013 and December 31, 2012, showing the aggregate fair value and gross unrealized loss by the length of time those securities had continuously been in a gross unrealized loss position as well as the relevant number of securities.

| In thousands, except # of securities | June 30, 2013 Number of Securities | Fair Value | Gross Unrealized Loss | December 31, 2012 Number of Securities | Fair Value | Gross Unrealized Loss |
|---|---|---|---|---|---|---|
| Fixed maturities: | | | | | | |
| U.S. Treasury bonds, agency bonds, and foreign government bonds | | | | | | |
| 0-6 months | 60 | $ 278,158 | $ 7,492 | 8 | $ 23,760 | $ 22 |
| 7-12 months | | | | 3 | 14,118 | 11 |
| > 12 months | | | | 1 | 4,652 | 3 |
| Subtotal | 60 | $ 278,158 | $ 7,492 | 12 | $ 42,530 | $ 36 |
| States, municipalities and political subdivisions | | | | | | |
| 0-6 months | 110 | $ 223,186 | $ 11,556 | 10 | $ 21,299 | $ 325 |
| 7-12 months | 7 | 17,168 | 1,546 | | | |
| > 12 months | 3 | 1,970 | 12 | 4 | 2,908 | 55 |
| Subtotal | 120 | $ 242,324 | $ 13,114 | 14 | $ 24,207 | $ 380 |
| Agency mortgage-backed securities | | | | | | |
| 0-6 months | 89 | $ 104,138 | $ 3,096 | 10 | $ 62,516 | $ 174 |
| 7-12 months | 9 | 24,070 | 1,431 | 2 | 1,671 | 30 |
| > 12 months | 2 | 1,559 | 118 | | | |
| Subtotal | 100 | $ 129,767 | $ 4,645 | 12 | $ 64,187 | $ 204 |
| Residential mortgage obligations | | | | | | |
| 0-6 months | 12 | $ 2,953 | $ 47 | 6 | $ 1,825 | $ 22 |
| 7-12 months | | | | | | |
| > 12 months | 17 | 3,140 | 174 | 35 | 7,252 | 527 |
| Subtotal | 29 | $ 6,093 | $ 221 | 41 | $ 9,077 | $ 549 |
| Asset-backed securities | | | | | | |
| 0-6 months | 4 | $ 16,905 | $ 29 | | $ | $ |
| 7-12 months | | | | | | |
| > 12 months | 1 | 1,634 | 84 | 2 | 2,369 | 49 |
| Subtotal | 5 | $ 18,539 | $ 113 | 2 | $ 2,369 | $ 49 |
| Commercial mortgage-backed securities | | | | | | |
| 0-6 months | 5 | $ 15,143 | $ 488 | 7 | $ 2,639 | $ 7 |
| 7-12 months | 2 | 651 | 10 | | | |
| > 12 months | 3 | 559 | 16 | 5 | 845 | 11 |
| Subtotal | 10 | $ 16,353 | $ 514 | 12 | $ 3,484 | $ 18 |
| Corporate bonds | | | | | | |
| 0-6 months | 43 | $ 121,470 | $ 3,162 | 2 | $ 3,528 | $ 6 |
| 7-12 months | | | | | | |
| > 12 months | | | | 4 | 6,689 | 19 |
| Subtotal | 43 | $ 121,470 | $ 3,162 | 6 | $ 10,217 | $ 25 |
| Total fixed maturities | 367 | $ 812,704 | $ 29,261 | 99 | $ 156,071 | $ 1,261 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Equity securities common stocks | | | | | | |
| 0-6 months | 6 | $ 33,817 | $ 1,910 | 13 | $ 23,345 | $ 522 |
| 7-12 months | | | | 1 | 1,943 | 104 |
| > 12 months | | | | | | |
| Total equity securities | 6 | $ 33,817 | $ 1,910 | 14 | $ 25,288 | $ 626 |

As of June 30, 2013 and December 31, 2012, the largest single unrealized loss by a non-government backed issuer in the investment portfolio was $1.4 million and $0.2 million, respectively.

The Company analyzes the unrealized losses quarterly to determine if any are other-than-temporary. The above unrealized losses have been determined to be temporary based on our policies.

For debt securities, when assessing whether the amortized cost basis of the security will be recovered, the Company compares the present value of cash flows expected to be collected in relation to the current book value. Any shortfalls of the present value of the cash flows expected to be collected to the amortized cost basis is considered the credit loss portion of OTTI losses and is recognized in earnings. All non-credit losses are recognized as changes in OTTI losses within OCI.

To determine whether the unrealized loss on structured securities is other-than-temporary, the Company analyzes the projections provided by its investment managers with respect to an expected principal loss under a range of scenarios and utilizes the most likely outcomes. The analysis relies on actual collateral performance measures such as default rate, prepayment rate and loss severity. These assumptions are applied throughout the remaining term of the deal, incorporating the transaction structure and priority of payments, to generate loss adjusted cash flows. Results of the analysis will indicate whether the security is expected ultimately to incur a loss or whether there is a material impact on yield due to either a projected loss or a change in cash flow timing. A break even default rate is also calculated. A comparison of the break even default rate to the actual default rate provides an indication of the level of cushion or coverage to the first dollar principal loss. The analysis applies the stated assumptions throughout the remaining term of the transaction to forecast cash flows, which are then applied through the transaction structure to determine whether there is a loss to the security. For securities in which a tranche loss is present, and the net present value of loss adjusted cash flows is less than book value, impairment is recognized. The output data also includes a number of additional metrics such as average life remaining, original and current credit support, over 60 day delinquency and security rating.

The significant inputs used to measure the amount of credit loss recognized in earnings were actual delinquency rates, default probability assumptions, severity assumptions and prepayment assumptions. Projected losses are a function of both loss severity and probability of default. Default probability and severity assumptions differ based on property type, vintage and the stress of the collateral. The Company does not intend to sell any of these securities and it is more likely than not that it will not be required to sell these securities before the recovery of the amortized cost basis.

For equity securities, in general, the Company focuses its attention on those securities with a fair value less than 80% of their cost for six or more consecutive months. If warranted as the result of conditions relating to a particular security, the Company will focus on a significant decline in fair value regardless of the time period involved. Factors considered in evaluating potential impairment include, but are not limited to, the current fair value as compared to cost of the security, the length of time the investment has been below cost and by how much the investment is below cost. If an equity security is deemed to be other-than-temporarily impaired, the cost is written down to fair value with the loss recognized in earnings.

For equity securities, the Company also considers its intent to hold securities as part of the process of evaluating whether a decline in fair value represents an other-than-temporary decline in value. For fixed maturity securities, the Company considers its intent to sell a security and whether it is more likely than not that the Company will be required to sell a security before the anticipated recovery as part of the process of evaluating whether a security s unrealized loss represents an other-than-temporary decline. The Company s ability to hold such securities is supported by sufficient cash flow from its operations and from maturities within its investment portfolio in order to meet its claims payment and other disbursement obligations arising from its underwriting operations without selling such investments. With respect to securities where the decline in value is determined to be temporary and the security s value is not written down, a subsequent decision may be made to sell that security and realize a loss. Subsequent decisions on security sales are made within the context of overall risk monitoring, changing information and market conditions.

As of June 30, 2013, there were no investments with a fair value that was less than 80% of amortized cost.

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The table below summarizes the Company s activity related to OTTI losses for the periods indicated:

| | Three Months Ended June 30, | | | | Six Months Ended June 30, | | | |
|---|---|---|---|---|---|---|---|---|
| | 2013 | | 2012 | | 2013 | | 2012 | |
| **In thousands, except # of securities** | **Number of Securities** | **Amount** | **Number of Securities** | **Amount** | **Number of Securities** | **Amount** | **Number of Securities** | **Amount** |
| Total OTTI losses: | | | | | | | | |
| Corporate and other bonds | | $ | | $ | | $ | | $ |
| Commercial mortgage-backed securities | | | | | | | | |
| Residential mortgage-backed securities | | | | | | | 1 | 54 |
| Asset-backed securities | | | | | | | | |
| Equities | | | 2 | 496 | 2 | 42 | 3 | 639 |
| Total | | $ | 2 | $ 496 | 2 | $ 42 | 4 | $ 693 |
| Less: Portion of loss in accumulated other comprehensive income (loss): | | | | | | | | |
| Corporate and other bonds | | $ | | $ | | $ | | $ |
| Commercial mortgage-backed securities | | | | | | | | |
| Residential mortgage-backed securities | | | | | | | | 43 |
| Asset-backed securities | | | | | | | | |
| Equities | | | | | | | | |
| Total | | $ | | $ | | $ | | $ 43 |
| Impairment losses recognized in earnings: | | | | | | | | |
| Corporate and other bonds | | $ | | $ | | $ | | $ |
| Commercial mortgage-backed securities | | | | | | | | |
| Residential mortgage-backed securities | | | | | | | | 11 |
| Asset-backed securities | | | | | | | | |
| Equities | | | | 496 | | 42 | | 639 |
| Total | | $ | | $ 496 | | $ 42 | | $ 650 |

The following table summarizes the cumulative amounts related to the Company s credit loss portion of the OTTI losses on debt securities for the three and six months ended June 30, 2013 and 2012. The Company does not intend to sell and it is more likely than not that it will not be required to sell the securities prior to recovery of the amortized cost basis and for which the non-credit loss portion is included in OCI.

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| **In thousands** | **2013** | **2012** | **2013** | **2012** |
| Beginning balance | $ 3,332 | $ 3,322 | $ 3,332 | $ 3,321 |
| Additions for credit loss impairments recognized in the current period on securities not previously impaired | | | | |
| Additions for credit loss impairments recognized in the current period on securities previously impaired | | | | 11 |
| Reductions for credit loss impairments previously recognized on securities sold during the period | | | | |
| Ending balance | $ 3,332 | $ 3,332 | $ 3,332 | $ 3,332 |

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The contractual maturity dates for fixed maturity securities categorized by the number of years until maturity, with a gross unrealized loss as of June 30, 2013 is presented in the following table:

| | June 30, 2013 | | | |
|---|---|---|---|---|
| | Gross Unrealized Losses | | Fair Value | |
| In thousands | Amount | Percent of Total | Amount | Percent of Total |
| Due in one year or less | $ 12 | 0% | $ 11,813 | 1% |
| Due after one year through five years | 2,442 | 8% | 192,689 | 24% |
| Due after five years through ten years | 11,394 | 39% | 267,617 | 33% |
| Due after ten years | 9,920 | 34% | 169,833 | 21% |
| Mortgage- and asset-backed securities | 5,493 | 19% | 170,752 | 21% |
| Total | $ 29,261 | 100% | $ 812,704 | 100% |

The Company s net investment income was derived from the following sources:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| In thousands | 2013 | 2012 | 2013 | 2012 |
| Fixed maturities | $ 13,578 | $ 15,006 | $ 26,743 | $ 30,416 |
| Equity securities | 1,257 | 994 | 2,288 | 1,941 |
| Short-term investments | 198 | 701 | 388 | 1,014 |
| Total investment income | $ 15,033 | $ 16,701 | $ 29,419 | $ 33,371 |
| Investment expenses | (787) | (924) | (1,516) | (6,336) |
| Net investment income | $ 14,246 | $ 15,777 | $ 27,903 | $ 27,035 |

Interest expense for the six months ended June 30, 2012 included $4.5 million of interest expense related to a total $9.2 million settlement of a dispute with Equitas over foregone interest on amounts that were due on certain reinsurance contracts.

The portfolio duration was 4.0 years and 3.9 years for the six months ended June 30, 2013 and 2012, respectively.

The change in net unrealized gains and losses, inclusive of the change in the non credit portion of other-than-temporary impairment losses, consisted of:

| | Six Months Ended June 30, | |
|---|---|---|
| In thousands | 2013 | 2012 |
| Fixed maturities | $ (67,769) | $ 17,439 |
| Equity securities | 7,035 | 6,910 |
| Gross unrealized gains (losses) | $ (60,734) | $ 24,349 |
| Deferred income tax | (21,264) | 7,796 |
| Change in net unrealized gains (losses), net | $ (39,470) | $ 16,553 |

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Realized gains and losses, excluding net OTTI losses recognized in earnings, for the periods indicated were as follows:

| In thousands | Three Months Ended June 30, 2013 | Three Months Ended June 30, 2012 | Six Months Ended June 30, 2013 | Six Months Ended June 30, 2012 |
|---|---|---|---|---|
| Fixed maturities: | | | | |
| Gains | $ 1,730 | $ 4,717 | $ 4,936 | $ 7,858 |
| Losses | (73) | (231) | (383) | (1,530) |
| Fixed maturities, net | $ 1,657 | $ 4,486 | $ 4,553 | $ 6,328 |
| Equity securities: | | | | |
| Gains | $ 1,815 | $ 204 | $ 3,733 | $ 204 |
| Losses | (127) | (473) | (127) | (473) |
| Equity securities, net | $ 1,688 | $ (269) | $ 3,606 | $ (269) |
| Net realized gains (losses) | $ 3,345 | $ 4,217 | $ 8,159 | $ 6,059 |

Net realized gains and losses are generated as part of the normal ongoing management of our investment portfolio. Net realized gains of $3.3 million and $8.2 million for the three and six months ended June 30, 2013 are primarily due to the sale of commercial mortgage-backed securities, municipal bonds and equity securities. Net realized gains of $4.2 million and $6.1 million for the three and six months ended June 30, 2012 were due to the sale of corporate bonds and Treasury bonds.

The following tables present, for each of the fair value hierarchy levels as defined by the accounting guidance for fair value measurements, the Company s fixed maturities and equity securities by asset class that are measured at fair value on a recurring basis as of June 30, 2013 and December 31, 2012:

| | June 30, 2013 | | | |
|---|---|---|---|---|
| In thousands | Level 1 | Level 2 | Level 3 | Total |
| Fixed maturities: | | | | |
| U.S. Treasury bonds, agency bonds and foreign government bonds | $ 276,111 | $ 188,056 | $ | $ 464,167 |
| States, municipalities and political subdivisions | | 452,084 | | 452,084 |
| Mortgage-backed and asset-backed securities: | | | | |
| Agency mortgage-backed securities | | 320,150 | | 320,150 |
| Residential mortgage obligations | | 37,335 | | 37,335 |
| Asset-backed securities | | 75,311 | | 75,311 |
| Commercial mortgage-backed securities | | 173,388 | | 173,388 |
| Subtotal | $ | $ 606,184 | $ | $ 606,184 |
| Corporate bonds | | 485,371 | | 485,371 |
| Total fixed maturities | $ 276,111 | $ 1,731,695 | $ | $ 2,007,806 |
| Equity securities common stocks | 138,549 | | | 138,549 |
| Total | $ 414,660 | $ 1,731,695 | $ | $ 2,146,355 |

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| In thousands | December 31, 2012 Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Fixed maturities: | | | | |
| U.S. Treasury bonds, agency bonds and foreign government bonds | $ 414,502 | $ 235,190 | $ | $ 649,692 |
| States, municipalities and political subdivisions | | 322,947 | | 322,947 |
| Mortgage-backed and asset-backed securities: | | | | |
| Agency mortgage-backed securities | | 384,445 | | 384,445 |
| Residential mortgage obligations | | 38,692 | | 38,692 |
| Asset-backed securities | | 50,382 | | 50,382 |
| Commercial mortgage-backed securities | | 204,821 | | 204,821 |
| Subtotal | $ | $ 678,340 | $ | $ 678,340 |
| Corporate bonds | | 470,854 | | 470,854 |
| Total fixed maturities | $ 414,502 | $ 1,707,331 | $ | $ 2,121,833 |
| Equity securities common stocks | 101,297 | | | 101,297 |
| Total | $ 515,799 | $ 1,707,331 | $ | $ 2,223,130 |

The fair value of financial instruments is determined based on the following fair value hierarchy:

Level 1 Quoted prices for identical instruments in active markets. Examples are listed equity and fixed income securities traded on an exchange. U.S. Treasury securities are reported as level 1 and are valued based on unadjusted quoted prices for identical assets in active markets that the Company can access.

Level 2 Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets. Examples are asset-backed and mortgage-backed securities that are similar to other asset-backed or mortgage-backed securities observed in the market. U.S. government agency securities are reported as level 2 and are valued using yields and spreads that are observable in active markets.

Level 3 Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable. An example would be a private placement with minimal liquidity.

The Company did not have any significant transfers between Level 1 and 2 as of June 30, 2013 and December 31, 2012.

As of June 30, 2013 and 2012, the Company did not have any Level 3 assets.

As of June 30, 2013 and December 31, 2012, the Company did not have a concentration of greater than 5% of invested assets in a single non-U.S. government-backed issuer.

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**Note 11. Credit Facility**

On November 22, 2012, we entered into a $165 million credit facility agreement with ING Bank N.V., London Branch, individually and as Administrative Agent, and a syndicate of lenders. The new credit facility amended and restated a $165 million letter of credit facility entered into by the parties on March 28, 2011. The credit facility, which is denominated in U.S. dollars, is utilized to fund our participation in Syndicate 1221 through letters of credit for the 2013 and 2014 underwriting years, as well as open prior years. The letters of credit issued under the facility are denominated in British pounds and their aggregate face amount will fluctuate based on exchange rates. If any letters of credit remain outstanding under the facility after December 31, 2014, we would be required to post additional collateral to secure the remaining letters of credit. As of June 30, 2013, letters of credit with an aggregate face amount of $142.6 million were outstanding under the credit facility and we have $0.8 million of cash collateral posted.

This credit facility contains customary covenants for facilities of this type, including restrictions on indebtedness and liens, limitations on mergers, dividends and the sale of assets, and requirements as to maintaining certain consolidated tangible net worth, statutory surplus and other financial ratios. The credit facility also provides for customary events of default, including failure to pay principal, interest or fees when due, failure to comply with covenants, any representation or warranty made by the Company being false in any material respect, default under certain other indebtedness, certain insolvency or receivership events affecting the Company and its subsidiaries, the occurrence of certain material judgments, or a change in control of the Company. The letter of credit facility is secured by a pledge of the stock of certain insurance subsidiaries of the Company. To the extent the aggregate face amount issued under the credit facility exceeds the commitment amount, the Company is required to post collateral with the lead bank of the consortium. The Company was in compliance with all covenants under the credit facility as of June 30, 2013.

The applicable margin and applicable fee rate payable under the credit facility are based on a tiered schedule that is based on the Company s then-current ratings issued by S&P and Moody s with respect to the Company s Senior Notes without third-party credit enhancement, and the amount of the Company s own collateral utilized to fund its participation in Syndicate 1221.

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*Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations*

**NOTE ON FORWARD-LOOKING STATEMENTS**

Some of the statements in this Quarterly Report on Form 10-Q for The Navigators Group, Inc. and its subsidiaries ( the Company , we , us , and our ) are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact included in or incorporated by reference in this Quarterly Report are forward-looking statements. Whenever used in this report, the words estimate, expect, believe or similar expressions or their negative are intended to identify such forward-looking statements. Forward-looking statements are derived from information that we currently have and assumptions that we make. We cannot assure that anticipated results will be achieved, since actual results may differ materially because of both known and unknown risks and uncertainties which we face. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Factors that could cause actual results to differ materially from our forward-looking statements include, but are not limited to, the factors discussed in the Risk Factors section of our 2012 Annual Report on Form 10-K as well as:

- continued volatility in the financial markets and the current recession;
- risks arising from the concentration of our business in marine and energy, general liability and professional liability insurance, including the risk that market conditions for these lines could change adversely or that we could experience large losses in these lines;
- cyclicality in the property and casualty insurance business generally, and the marine insurance business specifically;
- risks that we face in entering new markets and diversifying the products and services that we offer, including risks arising from the development of our new specialty lines or our ability to manage effectively the rapid growth in our lines of business;
- changing legal, social and economic trends and inherent uncertainties in the loss estimation process, which could adversely impact the adequacy of loss reserves and the allowance for reinsurance recoverables;
- risks inherent in the preparation of our financial statements, which require us to make many estimates and judgments;
- our ability to continue to obtain reinsurance covering our exposures at appropriate prices and/or in sufficient amounts;
- the counterparty credit risk of our reinsurers, including risks associated with the collection of reinsurance recoverable amounts from our reinsurers, who may not pay losses in a timely fashion, or at all;
- the effects of competition from other insurers;
- unexpected turnover of our professional staff and our ability to attract and retain qualified employees;
- increases in interest rates during periods in which we must sell fixed-income securities to satisfy liquidity needs may result in realized investment losses;

our investment portfolio is exposed to market-wide risks and fluctuations, as well as to risks inherent in particular types of securities;

exposure to significant capital market risks related to changes in interest rates, credit spreads, equity prices and foreign exchange rates which may adversely affect our results of operations, financial condition or cash flows;

capital may not be available in the future, or may not be available on favorable terms;

our ability to maintain or improve our insurance company ratings, as downgrades could significantly adversely affect us, including reducing our competitive position in the industry, or causing clients to choose an insurer with a certain rating level to use higher-rated insurers;

risks associated with continued or increased premium levies by Lloyd s of London ( Lloyd s) for the Lloyd s Central Fund and cash calls for trust fund deposits, or a significant downgrade of Lloyd s rating by the A.M. Best Company ( A.M. Best );

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- changes in the laws, rules and regulations that apply to our insurance companies;

- the effect of the European Union Directive on Solvency II on how we manage our business, capital requirements and costs associated with conducting business, including the impact of the delay in the implementation of Solvency II;

- the inability of our subsidiaries to pay dividends to us in sufficient amounts, which would harm our ability to meet our obligations;

- weather-related events and other catastrophes (including man-made catastrophes) impacting our insureds and/or reinsurers;

- volatility in the market price of our common stock;

- exposure to recent uncertainties with regard to European sovereign debt holdings;

- the determination of the impairments taken on our investments is subjective and could materially impact our financial position or results of operations;

- if we experience difficulties with our information technology and telecommunications systems and/or data security, our ability to conduct our business might be adversely affected;

- compliance by our Marine business with the legal and regulatory requirements to which they are subject is evolving and unpredictable. In addition, compliance with new sanctions and embargo laws could have a material adverse effect on our business; and

- other risks that we identify in current and future filings with the Securities and Exchange Commission ( SEC ).

In light of these risks, uncertainties and assumptions, any forward-looking events discussed in this Form 10-Q may not occur. You are cautioned not to place undue reliance on any forward-looking statements, which speak only as of their respective dates.

**OVERVIEW**

*The discussion and analysis of our financial condition and results of operations contained herein should be read in conjunction with our consolidated financial statements and accompanying notes which appear elsewhere in this Form 10-Q. It contains forward-looking statements that involve risks and uncertainties. Please refer to Note on Forward-Looking Statements for more information. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those discussed below and elsewhere in this Form 10-Q.*

We are an international insurance company focusing on specialty products within the overall property and casualty insurance market. Our largest product line and most long-standing area of specialization is ocean marine insurance. We have also developed other specialty insurance lines such as commercial primary and excess liability as well as specialty niches in professional liability, and have expanded our specialty reinsurance business since launching Navigators Re in the fourth quarter of 2010.

We conduct operations through our Insurance Companies and our Lloyd s Operations segments. The Insurance Companies segment consists of Navigators Insurance Company, which includes a United Kingdom Branch (the U.K. Branch ), and Navigators Specialty Insurance Company, which underwrites specialty and professional liability insurance on an excess and surplus lines basis. All of the insurance business written by Navigators Specialty Insurance Company is fully reinsured by Navigators Insurance Company pursuant to a 100% quota share reinsurance agreement. The insurance and reinsurance business written by our Insurance Companies is underwritten through our wholly-owned underwriting management Companies, Navigators Management Company, Inc. ( NMC ) and Navigators Management (UK) Ltd. ( NMUK ).

Our Lloyd s Operations segment includes Navigators Underwriting Agency Ltd. ( NUAL ), a Lloyd s of London ( Lloyd s ) underwriting agency which manages Lloyd s Syndicate 1221 ( Syndicate 1221 ). Our Lloyd s Operations primarily underwrite marine and related lines of business along with offshore energy, professional liability insurance and construction coverages for onshore energy business at Lloyd s through Syndicate 1221. We controlled 100% of Syndicate 1221 s stamp capacity for the 2013 and 2012 underwriting years through our wholly-owned subsidiary, Navigators Corporate Underwriters Ltd. ( NCUL ), which is referred to as a corporate name in the Lloyd s market. We have also established underwriting agencies in Antwerp, Belgium, Stockholm, Sweden, and Copenhagen, Denmark, which underwrite risks pursuant to binding authorities with NUAL into Syndicate 1221. We have also established a presence in Brazil and China through contractual arrangements with local affiliates of Lloyd s.

***Catastrophe Risk Management***

Our Insurance Companies and Lloyd s Operations have exposure to losses caused by natural and man-made catastrophic events. The frequency and severity of catastrophes are unpredictable. The extent of covered losses from a catastrophe is a function of both the total amount of insured exposure in an area affected by the event and the severity of the event. We continually assess our concentration of underwriting exposures in catastrophe exposed areas globally and manage this exposure through individual risk selection and through the purchase of reinsurance. We also use modeling and concentration management tools that allow us to better monitor and control our accumulations of potential losses from catastrophe events. Despite these efforts, there remains uncertainty about the characteristics, timing and extent of insured losses given the unpredictable nature of catastrophes. The occurrence of one or more catastrophic events could have a material adverse effect on our results of operations, financial condition and/or liquidity.

We have significant natural catastrophe exposures throughout the world. We estimate that our largest exposure to loss from a single natural catastrophe event comes from a potential earthquake on the west coast of the United States. As of June 30, 2013, we estimate that our probable maximum pre-tax gross and net loss exposure from such an earthquake event would be approximately $100 million and $40 million, respectively, including the cost of reinsurance reinstatement premiums ( RRPs ).

Like all catastrophe exposure estimates, the foregoing estimate of our probable maximum loss is inherently uncertain. This estimate is highly dependent upon numerous assumptions and subjective underwriting judgments. Examples of significant assumptions and judgments related to such an estimate include the intensity, depth and location of the earthquake, the various types of the insured risks exposed to the event at the time the event occurs and the estimated costs or damages incurred for each insured risk. The composition of our portfolio also makes such estimates challenging due to the non-static nature of the exposures covered under our policies in lines of business such as cargo and hull. There can be no assurances that the gross and net loss amounts that we could incur in such an event or in any natural catastrophe event would not be materially higher than the estimates discussed above given the significant uncertainties with respect to such an estimate. Moreover, our portfolio of insured risks changes dynamically over time and there can be no assurance that our probable maximum loss will not change materially over time.

The occurrence of large loss events could reduce the reinsurance coverage that is available to us and could weaken the financial condition of our reinsurers, which could have a material adverse effect on our results of operations. Although the reinsurance agreements make the reinsurers liable to us to the extent the risk is transferred or ceded to the reinsurer, ceded reinsurance arrangements do not eliminate our obligation to pay claims to our policyholders as we are required to pay the losses if a reinsurer fails to meet its obligations under the reinsurance agreement. Accordingly, we bear credit risk with respect to our reinsurers. Specifically, our reinsurers may not pay claims made by us on a timely basis, or they may not pay some or all of these claims. Either of these events would increase our costs and could have a material adverse effect on our business.

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## CRITICAL ACCOUNTING ESTIMATES

The Company s Annual Report on Form 10-K for the year ended December 31, 2012 discloses our critical accounting estimates (refer to Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Estimates). Certain of these estimates are critical to the portrayal of our financial condition and results since they require management to establish estimates based on complex and subjective judgments, including those related to our estimates for losses and loss adjustment expenses ( LAE ) (including losses that have occurred but were not reported to us by the financial reporting date), reinsurance recoverables, written and unearned premium, the recoverability of deferred tax assets, the impairment of investment securities and accounting for Lloyd s results. For additional information regarding our critical accounting estimates, refer to our Annual Report on Form 10-K for the year ended December 31, 2012.

## RECENT ACCOUNTING PRONOUNCEMENTS

Refer to Note 2, *Recent Accounting Pronouncements*, in the Notes to Interim Consolidated Financial Statements included herein for a discussion about accounting standards recently adopted by the Company, as well as recent accounting developments relating to standards not yet adopted by the Company.

## RESULTS OF OPERATIONS

The following is a discussion and analysis of our consolidated and segment results of operations for the three and six months ended June 30, 2013 and 2012. Our financial results are presented on the basis of U.S. GAAP. However, in presenting our financial results, we discuss our performance with reference to operating earnings, book value per share, underwriting profit or loss, and the combined ratio, all of which are non-GAAP financial measures of performance and/or underwriting profitability. Operating earnings is calculated as net income less after-tax net realized gains (losses) and net other-than-temporary impairment ( OTTI ) losses recognized in earnings. Book value per share is calculated by dividing stockholders equity by the number of outstanding shares at any period end. Underwriting profit or loss is calculated from net earned premiums, less the sum of net losses and LAE, commission expenses, other operating expenses and other income (expense). The combined ratio is derived by dividing the sum of net losses and LAE, commission expenses, other operating expenses and other income (expense) by net earned premiums. A combined ratio of less than 100% indicates an underwriting profit and greater than 100% indicates an underwriting loss. We consider such measures, which may be defined differently by other companies, to be important in the understanding of our overall results of operations by highlighting the underlying profitability of our insurance business.

***Summary of Consolidated Results***

The following table presents a summary of our consolidated financial results for the three and six months ended June 30, 2013 and 2012:

| | Three Months Ended June 30, | | Six Months Ended June 30, | | Percentage Change | |
|---|---|---|---|---|---|---|
| **In thousands, except for per share amounts** | **2013** | **2012** | **2013** | **2012** | **QTD** | **YTD** |
| Gross written premiums | $ 332,128 | $ 322,987 | $ 725,350 | $ 666,136 | 2.8% | 8.9% |
| Net written premiums | 198,469 | 190,252 | 467,921 | 433,297 | 4.3% | 8.0% |
| Total revenues | 222,490 | 215,902 | 443,865 | 412,878 | 3.1% | 7.5% |
| Total expenses | 202,269 | 194,778 | 403,091 | 380,569 | 3.8% | 5.9% |
| Pre-tax income (loss) | $ 20,221 | $ 21,124 | $ 40,774 | $ 32,309 | -4.3% | 26.2% |
| Provision (benefit) for income taxes | 6,284 | 6,225 | 12,927 | 9,506 | 0.9% | 36.0% |
| Net income (loss) | $ 13,937 | $ 14,899 | $ 27,847 | $ 22,803 | -6.5% | 22.1% |
| Net income (loss) per common share: | | | | | | |
| Basic | $ 0.99 | $ 1.06 | $ 1.97 | $ 1.63 | | |
| Diluted | $ 0.97 | $ 1.05 | $ 1.93 | $ 1.60 | | |

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Net income for the three months ended June 30, 2013 was $13.9 million or $0.97 per diluted share compared to $14.9 million or $1.05 per diluted share for the three months ended June 30, 2012. Operating earnings for the three months ended June 30, 2013 were $11.8 million or $0.82 per diluted share compared to $12.5 million or $0.88 per diluted share for the comparable period in 2012. In comparison to net income, operating earnings excluded after-tax net realized gains of $2.2 million for the three months ended June 30, 2013. For the three months ended June 30, 2012, operating earnings excluded $2.7 million of net realized gains and after-tax other-than-temporary impairment losses of $0.3 million. The decrease in our operating earnings was largely attributable to a decrease in net investment income on account of lower investment yields.

Net income for the six months ended June 30, 2013 was $27.8 million or $1.93 per diluted share compared to $22.8 million or $1.60 per diluted share for the six months ended June 30, 2012. Operating earnings for the six months ended June 30, 2013 were $22.6 million or $1.56 per diluted share compared to $19.3 million or $1.35 per diluted share for the comparable period in 2012. In comparison to net income, operating earnings excluded after-tax net realized gains of $5.3 million and after-tax other-than-temporary impairment losses of $0.03 million for the six months ended June 30, 2013. For the six months ended June 30, 2012, operating earnings excluded $3.9 million of net realized gains and after-tax other-than-temporary impairment losses of $0.4 million. The increase in our operating earnings was largely attributable to stronger underwriting results.

Our book value per share as of June 30, 2013 was $61.83, decreasing from $62.61 as of December 31, 2012. The decrease in book value per share primarily resulted from unrealized losses in our investment portfolio across all fixed income classes due to an increase in interest rates during the quarter. Our consolidated stockholders equity decreased 0.6% to $874.0 million as of June 30, 2013 compared to $879.5 million as of December 31, 2012.

Cash flow provided by operations was $48.5 million for the six months ended June 30, 2013 compared to $15.0 million for the comparable period in 2012. The increase in cash flow from operations was due to improved collection on premium receivables, partially offset by the timing of payments to our reinsurers in connection with the increased use of proportional reinsurance to support our offshore energy business in 2013.

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The following table presents our consolidated underwriting results and provides a reconciliation of our underwriting profit or loss to GAAP net income or net loss for the three and six months ended June 30, 2013 and 2012:

| In thousands | Three Months Ended June 30, 2013 | Three Months Ended June 30, 2012 | Six Months Ended June 30, 2013 | Six Months Ended June 30, 2012 | Percentage Change QTD | Percentage Change YTD |
|---|---|---|---|---|---|---|
| Gross written premiums | $ 332,128 | $ 322,987 | $ 725,350 | $ 666,136 | 2.8% | 8.9% |
| Net written premiums | 198,469 | 190,252 | 467,921 | 433,297 | 4.3% | 8.0% |
| Net earned premiums | 205,814 | 196,017 | 408,142 | 379,136 | 5.0% | 7.7% |
| Net losses and loss adjustment expenses | (131,148) | (123,407) | (262,490) | (241,392) | 6.3% | 8.7% |
| Commission expenses | (28,391) | (29,503) | (54,946) | (58,953) | -3.8% | -6.8% |
| Other operating expenses | (40,678) | (39,819) | (81,552) | (76,126) | 2.2% | 7.1% |
| Other income (expenses) | (915) | 387 | (297) | 1,298 | NM | NM |
| Underwriting profit (loss) | $ 4,682 | $ 3,675 | $ 8,857 | $ 3,963 | 27.4% | 123.5% |
| Net investment income | 14,246 | 15,777 | 27,903 | 27,035 | -9.7% | 3.2% |
| Net other-than-temporary impairment losses recognized in earnings | | (496) | (42) | (650) | NM | -93.5% |
| Net realized gains (losses) | 3,345 | 4,217 | 8,159 | 6,059 | -20.7% | 34.7% |
| Interest expense | (2,052) | (2,049) | (4,103) | (4,098) | 0.1% | 0.1% |
| Income (loss) before income taxes | $ 20,221 | $ 21,124 | $ 40,774 | $ 32,309 | -4.3% | 26.2% |
| Income tax expense (benefit) | 6,284 | 6,225 | 12,927 | 9,506 | 0.9% | 36.0% |
| Net income (loss) | $ 13,937 | $ 14,899 | $ 27,847 | $ 22,803 | -6.5% | 22.1% |
| Losses and loss adjustment expenses ratio | 63.7% | 63.0% | 64.3% | 63.7% | | |
| Commission expense ratio | 13.8% | 15.1% | 13.5% | 15.5% | | |
| Other operating expense ratio (1) | 20.2% | 20.0% | 20.0% | 19.8% | | |
| Combined ratio | 97.7% | 98.1% | 97.8% | 99.0% | | |

(1) - Includes Other operating expenses & Other income (expense)
NM - Percentage change not meaningful

The combined ratio for the three months ended June 30, 2013 was 97.7% compared to 98.1% for the same period in 2012. Our pre-tax underwriting profit increased $1.0 million to $4.7 million for the three months ended June 30, 2013 compared to $3.7 million for the same period in 2012.

Our pre-tax underwriting results for the three months ended June 30, 2013 included $4.5 million of underwriting profit from our Lloyd s Operations due to continued favorable loss emergence for underwriting years ( UYs ) 2011 and prior. Our pre-tax underwriting results also included a slight underwriting profit from our Insurance Companies, inclusive of $2.0 million of underwriting profit from our Excess Casualty and Primary Casualty businesses due in part to strong production attributable to the expansion of those underwriting teams and the dislocation of certain competitors, mostly offset by a net underwriting loss of $1.9 million from our Management Liability ( D&O ) and Errors & Omissions ( E&O ) business driven by net prior period reserve deficiencies from UYs 2010 and prior.

Our underwriting results for the three months ended June 30, 2012 include $3.0 million of RRPs related to significant large losses from our marine business, as well as net prior period reserve redundancies of $6.0 million from our Lloyd s Operations.

The combined ratio for the six months ended June 30, 2013 was 97.8% compared to 99.0% for the same period in 2012. Our pre-tax underwriting profit increased $4.9 million to $8.9 million for the six months ended June 30, 2013 compared to $4.0 million for the same period in 2012.

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Our pre-tax underwriting results for the six months ended June 30, 2013 included $8.5 million of underwriting profit from our Lloyd s Operations due to continued favorable loss emergence for UYs 2011 and prior. Our pre-tax underwriting results also included a slight underwriting profit from our Insurance Companies, inclusive of $6.4 million of underwriting profit from our Excess Casualty and Primary Casualty businesses due in part to strong production attributable to the expansion of those underwriting teams and the dislocation of certain competitors, mostly offset by a net underwriting loss of $5.5 million from our D&O business driven by net prior period reserve deficiencies from UYs 2010 and prior.

Our underwriting results for the first six months of 2012 reflect net losses of $11.3 million inclusive of $10.0 million of reinsurance reinstatement premiums, related to several large losses from our marine business, including the grounding of the cruise ship Costa Concordia off the coast of Italy. The results also include net prior period reserve redundancies of $12.2 million primarily driven by our Lloyd s Operations.

***Revenues***

**Gross Written Premiums**

The following tables set forth our gross written premiums, net written premiums and net earned premiums by segment and line of business for the three and six months ended June 30, 2013 and 2012:

| | Three Months Ended June 30, | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 2013 | | | | 2012 | | | |
| In thousands | Gross Written Premiums | % | Net Written Premiums | Net Earned Premiums | Gross Written Premiums | % | Net Written Premiums | Net Earned Premiums |
| Insurance Companies: | | | | | | | | |
| Marine | $ 43,077 | 13% | $ 27,366 | $ 31,798 | $ 49,896 | 15% | $ 31,786 | $ 35,535 |
| Property Casualty | 152,095 | 46% | 90,711 | 99,477 | 130,627 | 41% | 76,842 | 82,175 |
| Professional Liability | 33,393 | 10% | 25,303 | 25,272 | 33,541 | 10% | 25,437 | 23,867 |
| Insurance Companies Total | $ 228,565 | 69% | $ 143,380 | $ 156,547 | $ 214,064 | 66% | $ 134,065 | $ 141,577 |
| Lloyd s Operations: | | | | | | | | |
| Marine | $ 45,893 | 14% | $ 34,060 | $ 34,623 | $ 47,037 | 15% | $ 33,492 | $ 34,272 |
| Property Casualty | 41,217 | 12% | 12,181 | 8,562 | 48,978 | 15% | 15,705 | 15,272 |
| Professional Liability | 16,453 | 5% | 8,848 | 6,082 | 12,908 | 4% | 6,990 | 4,896 |
| Lloyd s Operations Total | $ 103,563 | 31% | $ 55,089 | $ 49,267 | $ 108,923 | 34% | $ 56,187 | $ 54,440 |
| Total | $ 332,128 | 100% | $ 198,469 | $ 205,814 | $ 322,987 | 100% | $ 190,252 | $ 196,017 |

| | Six Months Ended June 30, | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 2013 | | | | 2012 | | | |
| In thousands | Gross Written Premiums | % | Net Written Premiums | Net Earned Premiums | Gross Written Premiums | % | Net Written Premiums | Net Earned Premiums |
| Insurance Companies: | | | | | | | | |
| Marine | $ 93,924 | 13% | $ 68,507 | $ 68,523 | $ 111,761 | 17% | $ 74,651 | $ 70,810 |
| Property Casualty | 371,059 | 51% | 240,662 | 192,195 | 286,546 | 43% | 191,374 | 156,543 |
| Professional Liability | 65,210 | 9% | 50,530 | 50,160 | 64,095 | 10% | 49,290 | 45,772 |
| Insurance Companies Total | $ 530,193 | 73% | $ 359,699 | $ 310,878 | $ 462,402 | 70% | $ 315,315 | $ 273,125 |
| Lloyd s Operations: | | | | | | | | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Marine | $ 99,537 | 14% | $ 73,618 | $ 68,668 | $ 108,812 | 16% | $ 81,550 | $ 67,536 |
| Property Casualty | 66,275 | 9% | 19,493 | 16,441 | 73,274 | 11% | 25,060 | 29,774 |
| Professional Liability | 29,345 | 4% | 15,111 | 12,155 | 21,648 | 3% | 11,372 | 8,701 |
| Lloyd s Operations Total | $ 195,157 | 27% | $ 108,222 | $ 97,264 | $ 203,734 | 30% | $ 117,982 | $ 106,011 |
| Total | $ 725,350 | 100% | $ 467,921 | $ 408,142 | $ 666,136 | 100% | $ 433,297 | $ 379,136 |

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Gross written premiums increased $9.1 million, or 2.8%, to $332.1 million for the three months ended June 30, 2013 compared to $323.0 million for the same period in 2012. The increase in gross written premiums is primarily attributed to growth within our Insurance Companies Property Casualty business, specifically from our Excess Casualty and Primary Casualty divisions as a result of strong production attributable to an expansion of our underwriting teams and continued dislocation among certain competitors, partially offset by a decrease in our Assumed Reinsurance division attributable to the timing of policy renewals on our Accident and Health ( A&H ) business relative to the quarter. The increase in gross written premiums was further offset by a decrease in our Marine business in connection with the re-underwriting of our Inland Marine division.

Gross written premiums increased $59.3 million, or 8.9%, to $725.4 million for the six months ended June 30, 2013 compared to $666.1 million for the same period in 2012. The increase in gross written premiums is primarily attributed to growth within our Insurance Companies Property Casualty business, specifically from our Excess Casualty and Primary Casualty divisions as a result of strong production attributable to an expansion of our underwriting teams and continued dislocation among certain competitors, as well as continued growth from our Assumed Reinsurance division, partially offset by a decrease in our Marine business in connection with the re-underwriting of our Inland Marine division.

Average renewal premium rates for our Insurance Companies segment for the three months ended June 30, 2013 increased as compared to the same period in 2012 across substantially all of our businesses within each segment. Our Insurance Companies Marine business has realized a 5.0% and 15.2% increase in rates for the Marine Liability and Inland Marine divisions, respectively. Within our Insurance Companies Property Casualty business we have realized a 4.6% increase in rates for the Excess Casualty division and a 3.5% increase in the Primary Casualty division, partially offset by a 2.1% decrease from our Energy & Engineering division. Our Insurance Companies Professional Liability business has experienced an overall increase in its renewal rates of 2.8%, consisting of 2.5% and 2.9% for the D&O and E&O divisions, respectively. For the three months ended June 30, 2013, average renewal premium rates for our Lloyd s Operations segment include increases for Lloyd s Marine and Lloyd s Property Casualty of 4.0% and 2.0%, partially offset by a decrease for Lloyd s Professional Liability of 0.5%.

Average renewal premium rates for our Insurance Companies segment for the six months ended June 30, 2013 increased as compared to the same period in 2012 across substantially all of our businesses within each segment. Our Insurance Companies Marine business has realized a 4.9% and 8.0% increase in rates for the Marine Liability and Inland Marine divisions, respectively. Within our Insurance Companies Property Casualty business we have realized a 3.3% increase in rates for the Excess Casualty division and a 3.4% increase in the Primary Casualty division, partially offset by a 1.6% decrease from our Energy & Engineering division. Our Insurance Companies Professional Liability business has experienced an overall increase in its renewal rates of 4.4%, consisting of 6.9% and 3.4% for the D&O and E&O divisions, respectively. For the six months ended June 30, 2013, average renewal premium rates for our Lloyd s Operations segment include increases for Lloyd s Marine and Lloyd s Property Casualty of approximately 4.6% and 1.9%, respectively. Our Lloyd s Professional Liability business experienced an average decrease of 1.9%.

The average premium rate increases or decreases as noted above for the Marine, Property Casualty and Professional Liability businesses are calculated primarily by comparing premium amounts on policies that have renewed. The premiums are adjusted for changes in exposures and sometimes represent an aggregation of several lines of business. The rate change calculations provide an indicated pricing trend and are not meant to be a precise analysis of the numerous factors that affect premium rates or the adequacy of such rates to cover all underwriting costs and generate an underwriting profit. The calculation can also be affected quarter by quarter depending on the particular policies and the number of policies that renew during that period. Due to market conditions, these rate changes may or may not apply to new business that generally would be more competitively priced compared to renewal business. The calculation does not reflect the rate on business that we are unwilling or unable to renew due to loss experience or competition.

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**Ceded Written Premiums**

In the ordinary course of business, we reinsure certain insurance risks with unaffiliated insurance companies for the purpose of limiting our maximum loss exposure, protecting against catastrophic losses and maintaining desired ratios of net premiums written to statutory surplus. The relationship of ceded to gross written premium varies based upon the types of business written and whether the business is written by the Insurance Companies or the Lloyd s Operations.

Our reinsurance program includes contracts for proportional reinsurance, per risk and whole account excess-of-loss reinsurance for both property and casualty risks and property catastrophe excess-of-loss reinsurance. In recent years we have increased our utilization of excess-of-loss reinsurance for marine, property and certain casualty risks. Our excess-of-loss reinsurance contracts generally provide for a specific amount of coverage in excess of an attachment point and sometimes provides for reinstatement of the coverage to the extent the limit has been exhausted for payment of additional reinsurance premium (referred to as RRPs). The number of reinsurance reinstatements available varies by contract.

We record an estimate of the expected RRPs for losses ceded to excess-of-loss agreements where this feature applies.

For the three and six months ended June 30, 2013, we incurred $4.3 million and $5.0 million in RRPs primarily driven by large losses from our Marine business. For the three and six months ended June 30, 2012, we incurred $5.0 million and $16.4 million in RRPs, respectively, primarily attributable to large losses from our Marine business, including the grounding of the cruise ship Costa Concordia off the coast of Italy.

The following table sets forth our ceded written premiums by segment and major line of business for the three and six months ended June 30, 2013 and 2012:

| | Three Months Ended June 30, | | | | Six Months Ended June 30, | | | |
|---|---|---|---|---|---|---|---|---|
| | 2013 | | 2012 | | 2013 | | 2012 | |
| In thousands | Ceded Written Premiums | % of Gross Written Premiums | Ceded Written Premiums | % of Gross Written Premiums | Ceded Written Premiums | % of Gross Written Premiums | Ceded Written Premiums | % of Gross Written Premiums |
| Insurance Companies: | | | | | | | | |
| Marine | $ 15,711 | 36% | $ 18,110 | 36% | $ 25,417 | 27% | $ 37,110 | 33% |
| Property Casualty | 61,384 | 40% | 53,785 | 41% | 130,397 | 35% | 95,172 | 33% |
| Professional Liability | 8,090 | 24% | 8,104 | 24% | 14,680 | 23% | 14,805 | 23% |
| Total Insurance Companies | $ 85,185 | 37% | $ 79,999 | 37% | $ 170,494 | 32% | $ 147,087 | 32% |
| Lloyd s Operations: | | | | | | | | |
| Marine | $ 11,833 | 26% | $ 13,545 | 29% | $ 25,919 | 26% | $ 27,262 | 25% |
| Property Casualty | 29,036 | 70% | 33,273 | 68% | 46,782 | 71% | 48,214 | 66% |
| Professional Liability | 7,605 | 46% | 5,918 | 46% | 14,234 | 49% | 10,276 | 47% |
| Total Lloyd s Operations | $ 48,474 | 47% | $ 52,736 | 48% | $ 86,935 | 45% | $ 85,752 | 42% |
| Total | $ 133,659 | 40% | $ 132,735 | 41% | $ 257,429 | 35% | $ 232,839 | 35% |

Overall, the decrease in the percentage of total ceded written premiums to total gross written premiums for the three months ended June 30, 2013 compared to the same period in 2012 was primarily due to changes in the mix of our Lloyd s Marine business driven by a decrease in classes subject to proportional reinsurance, such as energy liability and war, partially offset by an increase in percentage for the Lloyd s Property Casualty business driven by the increased use of proportional reinsurance to support our offshore energy business in 2013.

Overall, the percentage of total ceded written premiums to total gross written premiums for the six months ended June 30, 2013 and 2012 has remained constant at 35%. The decrease in percentage for Insurance Companies Marine is driven by RRPs recorded in 2012 in connection with several large losses, including Costa Concordia as explained above. The increase in the percentage for Insurance Companies Property Casualty is driven by the significant growth of our Excess Casualty business, where our retention is lower, partially offset by the continued growth of our Assumed Reinsurance business where our retentions are higher. The increase in the Property Casualty business for the Lloyd s Operations is driven by increased use of proportional reinsurance to support our offshore energy business for 2013.

**Net Written Premiums**

Net written premiums increased 4.3% for the three months ended June 30, 2013 compared to the same period in 2012. The increase is due to the mix of our Insurance Companies Property Casualty business and is specifically driven by the growth of our Excess Casualty and Primary Casualty business as well as more RRPs recorded in 2012 in connection with several losses from our Marine businesses. The aforementioned increases are partially offset by a decrease in our Energy & Engineering business in connection with the increased use of proportional reinsurance to support our offshore energy lines for 2013, and a decrease in our Marine business in connection with the re-underwriting of our Inland Marine division.

Net written premiums increased 8.0% for the six months ended June 30, 2013 compared to the same period in 2012. The increase is due to the mix of our Insurance Companies Property Casualty business and is specifically driven by the growth of our Excess Casualty and Primary Casualty business, the continued growth of our Assumed Reinsurance business, and as well more RRPs recorded in 2012 in connection with several losses from our Marine businesses. The aforementioned increases are partially offset by a decrease in our Energy & Engineering business in connection with the increased use of proportional reinsurance to support our offshore energy lines for 2013, and a decrease in our Marine business in connection with the re-underwriting of our Inland Marine division.

**Net Earned Premiums**

Net earned premiums increased 5.0% and 7.7% for the three and six months ended June 30, 2013 compared to the same periods in 2012, driven by earnings from the continued growth of our Insurance Companies Excess Casualty, Primary Casualty, and our Assumed Reinsurance business, which includes the A&H lines that are recognized in earnings over a longer exposure period than our other lines of business. In addition, the increases are also attributable to the RRPs recorded in 2012, and are partially offset by a decrease from our Energy & Engineering business, as described above.

**Net Investment Income**

Our net investment income was derived from the following sources:

| | Three Months Ended June 30, | | Six Months Ended June 30, | | Percentage Change | |
|---|---|---|---|---|---|---|
| **In thousands** | **2013** | **2012** | **2013** | **2012** | **QTD** | **YTD** |
| Fixed maturities | $ 13,578 | $ 15,006 | $ 26,743 | $ 30,416 | -9.5% | -12.1% |
| Equity securities | 1,257 | 994 | 2,288 | 1,941 | 26.5% | 17.9% |
| Short-term investments | 198 | 701 | 388 | 1,014 | -71.8% | -61.7% |
| Total investment income | $ 15,033 | $ 16,701 | $ 29,419 | $ 33,371 | -10.0% | -11.8% |
| Investment expenses | (787) | (924) | (1,516) | (6,336) | -14.8% | -76.1% |
| Net investment income | $ 14,246 | $ 15,777 | $ 27,903 | $ 27,035 | -9.7% | 3.2% |

The decrease in total investment income before investment expenses was 10.0% and 11.8% for the three and six months ended June 30, 2013 compared to the same periods in 2012, primarily due to lower investment yields. The annualized pre-tax investment yield, excluding net realized gains and losses and net other-than-temporary impairment ( OTTI ) losses recognized in earnings, was 2.4% for the three and six months ended June 30, 2013 compared to 2.8% and 2.4% for the same periods in 2012, respectively.

The 2.4% average yield for the six months ended June 30, 2012 included $4.5 million of interest expense related to a total $9.2 million settlement of a dispute with Equitas over foregone interest on amounts that were due on certain reinsurance contracts. In the dispute Equitas alleged that we failed to make timely payments to them under certain reinsurance agreements in connection with subrogation recoveries received by us with respect to several catastrophe losses that occurred in the in the late 1980 s and early 1990 s. Excluding the impact of the aforementioned accrued interest expense, the average yield for the six months ended June 30, 2012 would have been 2.8%.

The portfolio duration was 4.0 years and 3.9 years for the six months ended June 30, 2013 and 2012, respectively.

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**Net Other-Than-Temporary Impairment Losses Recognized In Earnings**

Our net OTTI losses recognized in earnings for the periods indicated were as follows:

| In thousands | Three Months Ended June 30, 2013 | Three Months Ended June 30, 2012 | Six Months Ended June 30, 2013 | Six Months Ended June 30, 2012 | Percentage Change QTD | Percentage Change YTD |
|---|---|---|---|---|---|---|
| Fixed maturities | $ | $ | $ | $ 11 | NM | NM |
| Equity securities | | 496 | 42 | 639 | NM | -93.4% |
| OTTI recognized in earnings | $ | $ 496 | $ 42 | $ 650 | NM | -93.5% |

NM - Percentage change not meaningful

Net OTTI losses of $0.5 million for the three months ended June 30, 2012 consisted of two equity securities.

Net OTTI losses of $0.7 million for the six months ended June 30, 2012 consisted of one non-agency mortgage-backed security and three equity securities.

**Net Realized Gains and Losses**

Our realized gains and losses for the periods indicated were as follows:

| In thousands | Three Months Ended June 30, 2013 | Three Months Ended June 30, 2012 | Six Months Ended June 30, 2013 | Six Months Ended June 30, 2012 | Percentage Change QTD | Percentage Change YTD |
|---|---|---|---|---|---|---|
| Fixed maturities: | | | | | | |
| Gains | $ 1,730 | $ 4,717 | $ 4,936 | $ 7,858 | -63.3% | -37.2% |
| Losses | (73) | (231) | (383) | (1,530) | -68.4% | -75.0% |
| Fixed maturities, net | $ 1,657 | $ 4,486 | $ 4,553 | $ 6,328 | -63.1% | -28.0% |
| Equity securities: | | | | | | |
| Gains | $ 1,815 | $ 204 | $ 3,733 | $ 204 | NM | NM |
| Losses | (127) | (473) | (127) | (473) | -73.2% | -73.2% |
| Equity securities, net | $ 1,688 | $ (269) | $ 3,606 | $ (269) | NM | NM |
| Net realized gains (losses) | $ 3,345 | $ 4,217 | $ 8,159 | $ 6,059 | -20.7% | 34.7% |

NM - Percentage change not meaningful

Net realized gains and losses are generated as part of the normal ongoing management of our investment portfolio. Net realized gains of $3.3 million and $8.2 million for the three and six months ended June 30, 2013 are due to the sale of municipal bonds, commercial mortgage-backed securities and equity securities. Net realized gains of $4.2 million and $6.1 million for the three and six months ended June 30, 2012 were due to the sale of corporate bonds and Treasury bonds.

**Other Income/Expense**

Total other expense for the three and six months ended June 30, 2013 was $0.9 million and $0.3 million compared to other income of $0.4 million and $1.3 million for the three and six months ended June 30, 2012, respectively. Other income consists of foreign exchange gains and losses from our Lloyd s Operations, commission income and inspection fees related to our specialty insurance business.

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*Expenses*

**Net Losses and Loss Adjustment Expenses**

The ratio of net losses and LAE to net earned premiums ( loss ratios ) for the three and six months ended June 30, 2013 and 2012 is presented in the following table:

| Net Loss and LAE Ratio | Three Months Ended June 30, 2013 | Three Months Ended June 30, 2012 | Six Months Ended June 30, 2013 | Six Months Ended June 30, 2012 |
|---|---|---|---|---|
| Net Loss and LAE Payments | 62.3% | 61.7% | 58.5% | 63.1% |
| Change in reserves | 0.4% | 4.0% | 4.3% | 3.8% |
| Subtotal current year loss ratio | 62.7% | 65.7% | 62.8% | 66.9% |
| Prior year deficiencies (redundancies) | 1.0% | -2.7% | 1.5% | -3.2% |
| Net loss and LAE ratio | 63.7% | 63.0% | 64.3% | 63.7% |

The changes in current accident year loss ratios, as noted above, are driven by mix of business and loss trends.

The segment and line of business breakdown of the net loss and LAE ratios for the three and six months ended June 30, 2013 and 2012 are as follows:

| In thousands | Three Months Ended June 30, 2013 | Three Months Ended June 30, 2012 | Six Months Ended June 30, 2013 | Six Months Ended June 30, 2012 |
|---|---|---|---|---|
| Insurance Companies: | | | | |
| Marine | 54.4% | 85.2% | 59.4% | 82.0% |
| Property Casualty | 71.1% | 60.5% | 68.7% | 62.5% |
| Professional Liability | 73.7% | 83.8% | 81.7% | 77.0% |
| Insurance Companies | 68.1% | 70.6% | 68.7% | 70.0% |
| Lloyd s Operations: | | | | |
| Marine | 52.6% | 37.1% | 54.0% | 50.8% |
| Property Casualty | 79.4% | 50.6% | 45.9% | 39.5% |
| Professional Liability | -8.8% | 60.3% | 34.9% | 47.7% |
| Lloyd s Operations | 49.7% | 43.0% | 50.2% | 47.4% |
| Net loss and LAE ratio | 63.7% | 63.0% | 64.3% | 63.7% |

The changes in the net loss and LAE ratios by segment and line of business, as noted above, are primarily related to prior year reserve deficiencies and or redundancies, as described below.

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**Prior Year Reserve Deficiencies/Redundancies**

The relevant factors that may have a significant impact on the establishment and adjustment of losses and LAE reserves can vary by line of business and from period to period. As part of our regular review of prior reserves, management, in consultation with our actuaries, may determine, based on their judgments that certain assumptions made in the reserving process in prior year periods may need to be revised to reflect various factors, typically including the availability of additional information. Based on their reserve analyses, management may make corresponding reserve adjustments.

The segment and line of business breakdowns of prior period net reserve deficiencies (redundancies) for the three and six months ended June 30, 2013 and 2012 is as follows:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| **In thousands** | **2013** | **2012** | **2013** | **2012** |
| Insurance Companies: | | | | |
| Marine | $ (2,469) | $ (94) | $ (1,276) | $ (588) |
| Property Casualty | 7,311 | (2,951) | 7,155 | (6,280) |
| Professional Liability | 2,905 | 3,671 | 9,598 | 4,778 |
| Insurance Companies | $ 7,747 | $ 626 | $ 15,477 | $ (2,090) |
| Lloyd s Operations: | | | | |
| Marine | $ (1,352) | $ (4,026) | $ (2,979) | $ (3,970) |
| Property Casualty | 361 | (1,272) | (1,669) | (4,010) |
| Professional Liability | (4,843) | (700) | (4,833) | (2,168) |
| Lloyd s Operations | $ (5,834) | $ (5,998) | $ (9,481) | $ (10,148) |
| Total deficiencies (redundancies) | $ 1,913 | $ (5,372) | $ 5,996 | $ (12,238) |

The following is a discussion of relevant factors related to the $1.9 million prior period net reserve deficiencies recorded for the three months ended June 30, 2013:

The Insurance Companies recorded $7.7 million of net prior period reserve deficiencies primarily driven by our Property Casualty business. Within the Property Casualty business we reported prior period reserve deficiencies of $4.8 million from our Assumed Reinsurance business mostly related to several large losses from our A&H business, $1.4 million from our Primary Casualty business in connection with increased loss activity across all product lines, and $1.1 million in losses from commercial auto and liquor liability lines which are in run-off. In addition, we reported prior period reserve deficiencies of $2.9 million from our Professional Liability business, which included $1.9 million of reserve deficiencies directly related to our D&O division in connection with specific large losses from our public directors and officers liability lines for UYs 2010 and prior, as well as $1.0 million of reserve deficiencies from our E&O division also related to specific large losses from our small lawyers lines from UYs 2011 and prior. The aforementioned strengthening was partially offset by $2.5 million of prior period reserve redundancies from our Marine business related to favorable emergence from our Cargo and Marine Liability lines from UYs 2008 and prior.

Our Lloyd s Operations recorded $5.8 million of net prior period reserve redundancies primarily driven by our Lloyd s Professional Liability business. Within our Lloyd s Professional Liability business we reported prior period reserve redundancies of $5.8 million in connection with continued favorable emergence from our Lloyd s D&O business, partially offset by $1.0 million of strengthening on our Lloyd s E&O business. In addition, our Lloyd s Operations recorded $1.4 million of prior period reserve redundancies from our Lloyd s Marine business and is related to the favorable settlement of specific claims from our marine liability lines for UYs 2012 and prior.

The following is a discussion of relevant factors related to the $5.4 million prior period net reserve redundancies recorded for the three months ended June 30, 2012:

The Insurance Companies recorded $0.6 million of net prior period reserve deficiency. The net reserve deficiency includes adverse development from our Professional Liability business related to our lawyers and accountants products, partially offset by favorable development from our Property Casualty business related to our Primary Casualty and NavTech divisions.

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Our Lloyd s Operations recorded $6.0 million of net prior period reserve redundancies driven by the Marine and Property Casualty businesses.

The following is a discussion of relevant factors related to the $6.0 million prior period net reserve deficiencies for the six months ended June 30, 2013:

The Insurance Companies recorded $15.5 million of net prior period reserve deficiencies, primarily driven by our Professional Liability and Property Casualty businesses. Within the Professional Liability business, we reported prior period net reserve deficiencies of $5.6 million from the D&O division related to specific large claims from our public and private sectors directors and officers liability lines for UYs 2010 and prior. In addition, we reported prior period net reserve deficiencies of $4.0 million from the E&O division related to specific large claims from our insurance agents, miscellaneous professional liability, and small lawyers lines from UYs 2011 and prior. Within the Property Casualty business we reported prior period reserve deficiencies of $7.4 million from our NavRe division mostly related to several large losses from our A&H business and $2.2 million in losses from commercial auto and liquor liability lines which are in run-off, partially offset by $2.6 million of prior period redundancies from our Energy & Engineering business related to favorable emergence from our Offshore Energy lines for UYs 2011 and prior. The aforementioned net strengthening was partially offset by $1.3 million of net prior period reserve redundancies from our Marine business primarily related to $3.1 million of favorable emergence from our Cargo and Marine Liability lines from UYs 2008 and prior, partially offset by $1.8 million of prior period reserve deficiencies from our Inland Marine business across all product lines.

Our Lloyd s Operations recorded $9.5 million of net prior period reserve redundancies across all businesses. Within our Lloyd s Professional Liability business we reported prior period reserve redundancies of $5.4 million in connection with continued favorable emergence from our Lloyd s D&O business, partially offset by $0.6 million of strengthening on our Lloyd s E&O business. Within the Lloyd s Marine business we reported prior period reserve redundancies of $3.0 million related to the favorable settlement of specific claims from our Ocean Marine liability lines from UYs 2012 and prior. In addition, our Lloyd s Property Casualty business also reported net prior period reserve redundancies of $1.6 million from the Energy & Engineering division due in part to the favorable settlement of two claims from our onshore lines from UY 2011

The following is a discussion of relevant factors related to the $12.2 million prior period net reserve redundancies recorded for the six months ended June 30, 2012:

The Insurance Companies recorded $2.1 million of net prior period reserve redundancies driven by net favorable development from our Property Casualty business related to our Primary Casualty and NavTech divisions, partially offset by adverse development from our Professional Liability business across multiple products within our D&O and E&O divisions.

Our Lloyd s Operations recorded $10.1 million of net prior period reserve redundancies across all businesses and divisions.

**Commission Expenses**

Commission expenses paid to brokers and agents are generally based on a percentage of gross written premiums and are partially offset by ceding commissions we may receive on ceded written premiums. Commissions are generally deferred and recorded as deferred policy acquisition costs to the extent that they relate to unearned premium. The percentage of commission expenses to net earned premiums ( commission expense ratio ) for the three and six months ended June 30, 2013 were 13.8% and 13.5%, respectively, compared to 15.1% and 15.5% for the comparable periods during 2012. The decrease in the commission expense ratio for the three and six months ended June 30, 2013 when compared to the same periods in 2012 is attributed to changes in the mix of business, mostly driven by an increase in the ceding commission on the new quota share program for our offshore energy business, and to a lesser extent RRPs recorded in 2012 in connection with loss events from our Marine business.

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**Other Operating Expenses**

Other operating expenses were $40.7 million and $81.6 million for the three and six months ended June 30, 2013 compared to $39.8 million and $76.1 million for the same periods in 2012. The increase in operating expenses is primarily due to an increase in overall headcount due to continued investments in new underwriting teams and related support staff, closely aligned with business growth.

**Interest Expense**

Interest expense relates to our Senior Notes due May 1, 2016. Interest on these Senior Notes is due each May 1 and November 1 and the effective interest rate, based on the proceeds net of discount and all issuance costs, is approximately 7.17%. Interest expense for both the three and six months ended June 30, 2013 and 2012 was approximately $2.1 million and $4.1 million.

**Income Taxes**

We recorded income tax expense of $6.3 million and $12.9 million for the three and six months ended June 30, 2013 compared to $6.2 million and $9.5 million for the comparable periods in 2012, resulting in effective tax rates of 31.1% and 31.7% for the three and six months ended June 30, 2013 compared to 29.5% and 29.4% for the same periods in 2012. The effective tax rate on net investment income was 27.6% and 28.0% for the three and six months ended June 30, 2013 compared to 28.2% and 26.9% for the same periods during 2012.

As of June 30, 2013, the net deferred federal, foreign, state and local tax assets were $25.9 million compared to $3.2 million as of December 31, 2012 with the change primarily due to the increase in unrealized losses on investments and the increase in the deferred tax asset for unearned premium reserve, in line with the growth of our business.

We had net state and local deferred tax assets amounting to potential future tax benefits of $0.5 million as of both June 30, 2013 and December 31, 2012, respectively. Included in the deferred tax assets are state and local net operating loss carry-forwards of $0.2 million as of both June 30, 2013 and December 31, 2012. A valuation allowance was established for the full amount of these potential future tax benefits due to uncertainty associated with their realization. Our state and local tax carry-forwards as of June 30, 2013 expire from 2023 to 2031.

The Company has not provided for U.S. income taxes on approximately $17.2 million of undistributed earnings of its non-U.S. subsidiaries since it is intended that those earnings will be reinvested indefinitely in those subsidiaries. If a future determination is made that those earnings no longer are intended to be reinvested indefinitely in those subsidiaries, U.S. income taxes of approximately $1.8 million, assuming all foreign tax credits are realized, would be included in the tax provision at that time and would be payable if those earnings were distributed to the Company.

***Segment Information***

We classify our business into two underwriting segments consisting of the Insurance Companies and the Lloyd s Operations, which are separately managed, and a Corporate segment. Segment data for each of the two underwriting segments include allocations of the operating expenses of the wholly-owned underwriting management companies and The Navigators Group, Inc. s (the Parent Company s ) operating expenses and related income tax amounts. The Corporate segment consists of the Parent Company s investment income, interest expense and the related tax effect.

We evaluate the performance of each segment based on its underwriting and GAAP results. The underwriting results of the Insurance Companies and the Lloyd s Operations are measured by taking into account net earned premium, net loss and LAE, commission expenses, other operating expenses and other income (expense). Each segment also maintains its own investments, on which it earns income and realizes capital gains or losses. Our underwriting performance is evaluated separately from the performance of our investment portfolios.

Following are the financial results of our two underwriting segments.

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**Insurance Companies**

The Insurance Companies consist of Navigators Insurance Company, including its U.K. Branch, and its wholly-owned subsidiary, Navigators Specialty. They are primarily engaged in underwriting marine insurance and related lines of business, specialty insurance lines of business, including contractors general liability insurance, commercial umbrella and primary and excess casualty businesses, specialty assumed reinsurance business, and professional liability insurance. Navigators Specialty underwrites specialty and professional liability insurance on an excess and surplus lines basis. Navigators Specialty is 100% reinsured by Navigators Insurance Company.

The following table sets forth the results of operations for the Insurance Companies for the three and six months ended June 30, 2013 and 2012:

| | Three Months Ended June 30, | | Six Months Ended June 30, | | Percentage Change | |
|---|---|---|---|---|---|---|
| **In thousands** | **2013** | **2012** | **2013** | **2012** | **QTD** | **YTD** |
| Gross written premiums | $ 228,565 | $ 214,064 | $ 530,193 | $ 462,402 | 6.8% | 14.7% |
| Net written premiums | 143,380 | 134,065 | 359,699 | 315,315 | 6.9% | 14.1% |
| Net earned premiums | 156,547 | 141,577 | 310,878 | 273,125 | 10.6% | 13.8% |
| Net losses and loss adjustment expenses | (106,668) | (100,003) | (213,653) | (191,180) | 6.7% | 11.8% |
| Commission expenses | (20,573) | (21,117) | (39,090) | (40,418) | -2.6% | -3.3% |
| Other operating expenses | (29,829) | (28,914) | (59,172) | (54,259) | 3.2% | 9.1% |
| Other income (expense) | 689 | 879 | 1,348 | 2,521 | -21.6% | -46.5% |
| Underwriting profit (loss) | $ 166 | $ (7,578) | $ 311 | $ (10,211) | NM | NM |
| Net investment income | 12,515 | 13,286 | 24,466 | 22,221 | -5.8% | 10.1% |
| Net realized gains (losses) | 3,099 | 2,325 | 7,891 | 4,200 | 33.3% | 87.9% |
| Income (loss) before income taxes | $ 15,780 | $ 8,033 | $ 32,668 | $ 16,210 | 96.4% | 101.5% |
| Income tax expense (benefit) | 4,785 | 2,101 | 10,199 | 3,980 | 127.7% | NM |
| Net income (loss) | $ 10,995 | $ 5,932 | $ 22,469 | $ 12,230 | 85.4% | 83.7% |
| Losses and loss adjustment expenses ratio | 68.1% | 70.6% | 68.7% | 70.0% | | |
| Commission expense ratio | 13.1% | 14.9% | 12.6% | 14.8% | | |
| Other operating expense ratio (1) | 18.7% | 19.9% | 18.6% | 18.9% | | |
| Combined ratio | 99.9% | 105.4% | 99.9% | 103.7% | | |

(1) - Includes Other operating expenses & Other income (expense)
NM - Percentage change not meaningful

Our Insurance Companies reported net income of $11.0 million for the three months ended June 30, 2013 compared to $5.9 million for the same period in 2012. The increase in net income for the three months ended June 30, 2013 as compared to the same period in 2012 was largely related to an improvement in underwriting results.

Our Insurance Companies combined ratio for the three months ended June 30, 2013 was 99.9% compared to 105.4% for the same period in 2012. Our Insurance Companies pre-tax underwriting results increased by $7.8 million to a $0.2 million pre-tax underwriting profit for the three months ended June 30, 2013 compared to an underwriting loss of $7.6 million for the same period in 2012.

Our Insurance Companies pre-tax underwriting results for the three months ended June 30, 2013 included $2.0 million of underwriting profit from our Excess Casualty and Primary Casualty businesses due in part to strong production attributable to the expansion of those underwriting teams and the continued dislocation of certain competitors, mostly offset by a net underwriting loss of $1.9 million from our D&O and E&O businesses driven by net prior period reserve deficiencies from UYs 2010 and prior.

Our Insurance Companies underwriting results for the three months ended June 30, 2012 includes $3.9 million of RRPs related to several large losses from our Marine business.

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Our Insurance Companies reported net income of $22.5 million for the six months ended June 30, 2013 compared to $12.2 million for the same period in 2012. The increase in net income for the six months ended June 30, 2013 as compared to the same period in 2012 was largely related to an improvement in underwriting results.

Our Insurance Companies combined ratio for the six months ended June 30, 2013 was 99.9% compared to 103.7% for the same period in 2012. Our Insurance Companies pre-tax underwriting results increased by $10.5 million to a $0.3 million pre-tax underwriting profit for the six months ended June 30, 2013 compared to an underwriting loss of $10.2 million for the same period in 2012.

Our Insurance Companies pre-tax underwriting results for the six months ended June 30, 2013 included $6.4 million of underwriting profit from our Excess Casualty and Primary Casualty businesses due in part to strong production attributable to the expansion of those underwriting teams and the continued dislocation of certain competitors, mostly offset by an underwriting loss of $5.5 million from our D&O business driven by net prior period reserve deficiencies from UYs 2010 and prior.

Our Insurance Companies underwriting results for the six months ended June 30, 2012 reflected net losses of $9.6 million related to several large losses from our marine business, including the grounding of the cruise ship Costa Concordia off the coast of Italy.

*Insurance Companies Gross Written Premiums*

*Marine Premiums.* The gross written premiums for our Marine business for the three and six months ended June 30, 2013 and 2012 consisted of the following:

| | **Three Months Ended June 30,** | | **Six Months Ended June 30,** | | **Percentage Change** | |
|---|---|---|---|---|---|---|
| **In thousands** | **2013** | **2012** | **2013** | **2012** | **QTD** | **YTD** |
| Marine Liability | $ 16,951 | $ 16,562 | $ 31,756 | $ 34,805 | 2.3% | -8.8% |
| Craft/Fishing Vessels | 7,176 | 6,000 | 17,956 | 14,244 | 19.6% | 26.1% |
| Cargo | 3,553 | 4,988 | 11,973 | 13,446 | -28.8% | -11.0% |
| Protection & Indemnity | 4,097 | 3,838 | 10,248 | 10,454 | 6.7% | -2.0% |
| Inland Marine | 4,503 | 9,404 | 9,384 | 21,242 | -52.1% | -55.8% |
| Bluewater Hull | 3,155 | 4,701 | 5,755 | 8,260 | -32.9% | -30.3% |
| Other Marine | 3,642 | 4,403 | 6,852 | 9,310 | -17.3% | -26.4% |
| Total Marine | $ 43,077 | $ 49,896 | $ 93,924 | $ 111,761 | -13.7% | -16.0% |

The Insurance Companies Marine gross written premiums for the three and six months ended June 30, 2013 decreased 13.7% and 16.0% compared to the same periods during 2012 primarily due to the re-underwriting of our Inland Marine business, as well as a reduction in the Bluewater Hull business due to lower than anticipated new business production resulting from a stricter underwriting approach on certain accounts and vessel types. In addition, the decrease in Cargo was related to non renewed business that did not meet the current underwriting criteria.

The Insurance Companies Marine business achieved a 5.0% and 4.9% increase on renewal rates for the three and six months ended June 30, 2013, respectively. The increase in renewal rates on Inland Marine business was 15.2% and 8.0% for the three and six months ended June 30, 2013.

*Property Casualty Premiums.* The gross written premiums for our Property Casualty business for the three and six months ended June 30, 2013 and 2012 consisted of the following:

| In thousands | Three Months Ended June 30, 2013 | Three Months Ended June 30, 2012 | Six Months Ended June 30, 2013 | Six Months Ended June 30, 2012 | Percentage Change QTD | Percentage Change YTD |
|---|---|---|---|---|---|---|
| Excess Casualty | $ 64,306 | $ 51,425 | $ 134,588 | $ 89,079 | 25.0% | 51.1% |
| Assumed Reinsurance | 15,436 | 20,375 | 107,572 | 93,796 | -24.2% | 14.7% |
| Primary Casualty | 35,034 | 26,225 | 61,469 | 50,115 | 33.6% | 22.7% |
| Energy & Engineering | 21,828 | 20,192 | 41,892 | 33,393 | 8.1% | 25.5% |
| Environmental Liability | 7,539 | 6,310 | 13,075 | 11,520 | 19.5% | 13.5% |
| Other Property & Casualty | 7,952 | 6,100 | 12,463 | 8,643 | 30.4% | 44.2% |
| Total Property Casualty | $ 152,095 | $ 130,627 | $ 371,059 | $ 286,546 | 16.4% | 29.5% |

The Insurance Companies Property Casualty gross written premiums for the three months ended June 30, 2013 increased 16.4% compared to the same period in 2012, driven by growth from our Excess Casualty and Primary Casualty divisions as a result of strong production attributable to an expansion of our underwriting teams and continued dislocation among certain competitors, partially offset a decrease in our Assumed Reinsurance business attributable to the timing of policy renewals on our A&H business relative to the quarter.

The Insurance Companies Property Casualty gross written premiums for the six months ended June 30, 2013 increased 29.5% compared to the same period in 2012, driven by growth from our Excess Casualty and Primary Casualty divisions as a result of strong production attributable to an expansion of our underwriting teams and continued dislocation among certain competitors, as well as continued growth from our Assumed Reinsurance business.

For the three months ended June 30, 2013, our Insurance Companies Property Casualty business realized a 4.6% increase in rates for the Excess Casualty division and a 3.5% increase in the Primary Casualty division, partially offset by a 2.1% decrease from our Energy & Engineering division.

For the six months ended June 30, 2013, our Insurance Companies Property Casualty business realized a 3.3% increase in rates for the Excess Casualty division and a 3.4% increase in the Primary Casualty division, partially offset by a 1.6% decrease from our Energy & Engineering division.

*Professional Liability Premiums*. The gross written premiums for the Professional Liability business for the three and six months ended June 30, 2013 and 2012 consisted of the following:

| In thousands | Three Months Ended June 30, 2013 | Three Months Ended June 30, 2012 | Six Months Ended June 30, 2013 | Six Months Ended June 30, 2012 | Percentage Change QTD | Percentage Change YTD |
|---|---|---|---|---|---|---|
| Errors & Omissions | $ 21,474 | $ 22,229 | $ 44,127 | $ 44,161 | -3.4% | -0.1% |
| Management Liability | 11,919 | 11,312 | 21,083 | 19,934 | 5.4% | 5.8% |
| Total Professional Liability | $ 33,393 | $ 33,541 | $ 65,210 | $ 64,095 | -0.4% | 1.7% |

For the three months ended June 30, 2013, our Insurance Companies Professional Liability business has experienced an overall increase in its renewal rates of 2.8%, consisting of 2.5% and 2.9% for the D&O and E&O divisions, respectively.

For the six months ended June 30, 2013, our Insurance Companies Professional Liability business has experienced an overall increase in its renewal rates of 4.4%, consisting of 6.9% and 3.4% for the D&O and E&O divisions, respectively.

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*Insurance Companies Commission Expenses*

The commission expense ratios for the three and six months ended June 30, 2013, were 13.1% and 12.6%, respectively, compared to 14.9% and 14.8% for the same periods in 2012. The decrease in the commission expense ratio is attributable to changes in the mix of business, mostly driven by an increase in the ceding commission received on the new quota share program for our offshore energy business. The decrease for the six months ended June 30, 2013 in comparison to 2012 is further attributable to more RRPs recorded in 2012 in connection with several losses from our Marine business.

*Insurance Companies Other Operating Expenses*

Insurance Companies other operating expenses were $29.8 million and $59.2 million for the three and six months ended June 30, 2013 compared to $28.9 million and $54.3 million for the same periods in 2012. The increase in operating expenses is due to an increase in overall headcount due to continued investments in new underwriting teams and related support staff, closely aligned with business growth.

**Lloyd s Operations**

Our Lloyd s Operations primarily underwrite marine and related lines of business along with offshore energy, construction coverages for onshore energy business and professional liability insurance at Lloyd s through Syndicate 1221. Our Lloyd s Operations segment includes NUAL, a Lloyd s underwriting agency which manages Syndicate 1221.

The following table sets forth the results of operations for the Lloyd s Operations for the three and six months ended June 30, 2013 and 2012:

| | Three Months Ended June 30, | | Six Months Ended June 30, | | Percentage Change | |
|---|---|---|---|---|---|---|
| **In thousands** | **2013** | **2012** | **2013** | **2012** | **QTD** | **YTD** |
| Gross written premiums | $ 103,563 | $ 108,923 | $ 195,157 | $ 203,734 | -4.9% | -4.2% |
| Net written premiums | 55,089 | 56,187 | 108,222 | 117,982 | -2.0% | -8.3% |
| Net earned premiums | 49,267 | 54,440 | 97,264 | 106,011 | -9.5% | -8.3% |
| Net losses and loss adjustment expenses | (24,480) | (23,404) | (48,837) | (50,212) | 4.6% | -2.7% |
| Commission expenses | (8,335) | (8,938) | (16,956) | (19,824) | -6.7% | -14.5% |
| Other operating expenses | (10,849) | (10,905) | (22,380) | (21,867) | -0.5% | 2.3% |
| Other income (expense) | (1,087) | 60 | (545) | 66 | NM | NM |
| Underwriting profit (loss) | $ 4,516 | $ 11,253 | $ 8,546 | $ 14,174 | -59.9% | -39.7% |
| Net investment income | 1,728 | 2,454 | 3,430 | 4,737 | -29.6% | -27.6% |
| Net realized gains (losses) | 242 | 1,396 | 222 | 1,209 | -82.7% | -81.6% |
| Income (loss) before income taxes | $ 6,486 | $ 15,103 | $ 12,198 | $ 20,120 | -57.1% | -39.4% |
| Income tax expense (benefit) | 2,206 | 5,207 | 4,242 | 6,933 | -57.6% | -38.8% |
| Net income (loss) | $ 4,280 | $ 9,896 | $ 7,956 | $ 13,187 | -56.7% | -39.7% |
| Losses and loss adjustment expenses ratio | 49.7% | 43.0% | 50.2% | 47.4% | | |
| Commission expense ratio | 16.9% | 16.4% | 17.4% | 18.7% | | |
| Other operating expense ratio (1) | 24.2% | 19.9% | 23.6% | 20.5% | | |
| Combined ratio | 90.8% | 79.3% | 91.2% | 86.6% | | |

(1) - Includes Other operating expenses & Other income (expense)
NM - Percentage change not meaningful.

Our Lloyd s Operations reported net income of $4.3 million for the three months ended June 30, 2013 compared to $9.9 million for the same period in 2012. The decrease in net income for the three months ended June 30, 2013 as compared to the same period in 2012 was largely attributable to a reduction in underwriting profit, and to a lesser extent, a reduction in net investment income due to lower investment yields.

Our Lloyd s Operations combined ratio for the three months ended June 30, 2013 was 90.8% compared to 79.3% for the same period in 2012. Our Lloyd s Operations pre-tax underwriting profit decreased $6.8 million to $4.5 million for the three months ended June 30, 2013 compared to $11.3 million for the same period in 2012.

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Our Lloyd s Operations pre-tax underwriting profit for the three months ended June 30, 2013 included $5.8 million of net prior period reserve redundancies in connection with continued favorable emergence from our Lloyd s D&O business and to a lesser extent the favorable settlement of specific claims from our Lloyd s Marine business, partially offset by a $1.2 million foreign exchange loss on the remeasurement of certain deposits required by Lloyd s.

Our Lloyd s Operations pre-tax underwriting profit for the three months ended June 30, 2012 included net prior period reserve redundancies of $6.0 million from our Lloyd s Property Casualty and Lloyd s Marine businesses.

Our Lloyd s Operations reported net income of $8.0 million for the six months ended June 30, 2013 compared to $13.2 million for the same period in 2012. The decreases in net income for the six months ended June 30, 2013 as compared to the same period in 2012 was largely attributable to a reduction in underwriting profit, and to a lesser extent, a reduction in net investment income due to lower investment yields.

Our Lloyd s Operations combined ratio for the six months ended June 30, 2013 was 91.2% compared to 86.6% for the same period in 2012. Our Lloyd s Operations pre-tax underwriting profit decreased $5.7 million to $8.5 million for the three months ended June 30, 2013 compared to $14.2 million for the same period in 2012.

Our Lloyd s Operations pre-tax underwriting profit for the six months ended June 30, 2013 included $9.5 million of net prior period reserve redundancies in connection with continued favorable emergence from our Lloyd s D&O business and the favorable settlement of specific claims from our Lloyd s Marine business, partially offset by a $1.2 million foreign exchange loss on the remeasurement of certain deposits required by Lloyd s.

Our Lloyd s Operations pre-tax underwriting profit for the six months ended June 30, 2012 included net prior period reserve redundancies of $10.1 million as a result of favorable emergence from all businesses.

*Lloyd s Operations Gross Written Premiums*

We have controlled 100% of Syndicate 1221 s stamp capacity since 2006. Stamp capacity is a measure of the amount of premium a Lloyd s syndicate is authorized to write based on a business plan approved by the Council of Lloyd s. Syndicate 1221 s stamp capacity is £195 million ($296 million) in 2013 compared to £184 million ($300 million) in 2012.

*Marine Premiums.* The gross written premiums for our Marine business for the three and six months ended June 30, 2013 and 2012 consisted of the following:

| | **Three Months Ended June 30,** | | **Six Months Ended June 30,** | | **Percentage Change** | |
|---|---|---|---|---|---|---|
| **In thousands** | **2013** | **2012** | **2013** | **2012** | **QTD** | **YTD** |
| Marine Liability | $ 8,842 | $ 9,875 | $ 26,657 | $ 28,819 | -10.5% | -7.5% |
| Cargo | 13,720 | 11,740 | 23,724 | 25,419 | 16.9% | -6.7% |
| Specie | 4,876 | 5,265 | 11,331 | 11,561 | -7.4% | -2.0% |
| Marine Excess-of-Loss Reinsurance | 4,826 | 4,066 | 10,564 | 11,139 | 18.7% | -5.2% |
| Energy Liability | 4,301 | 5,826 | 10,157 | 11,927 | -26.2% | -14.8% |
| Transport | 6,088 | 6,046 | 9,979 | 9,934 | 0.7% | 0.5% |
| War | 1,482 | 2,687 | 3,964 | 5,973 | -44.8% | -33.6% |
| Bluewater Hull | 1,758 | 1,532 | 3,161 | 4,040 | 14.8% | -21.8% |
| Total Marine | $ 45,893 | $ 47,037 | $ 99,537 | $ 108,812 | -2.4% | -8.5% |

The Lloyd s Operations Marine gross written premiums decreased 2.4% and 8.5% for the three and six months ended June 30, 2013 compared to the same periods in 2012. The decrease is driven by reduction in renewals on War, Marine Liability and Energy Liability in connection with, and partially offset by an increase in average renewal rates of 4.0% and 4.6% for the three and six months ended June 30, 2013.

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*Property Casualty Premiums.* The gross written premiums for our Property Casualty business for the three and six months ended June 30, 2013 and 2012 consisted of the following:

| In thousands | Three Months Ended June 30, 2013 | 2012 | Six Months Ended June 30, 2013 | 2012 | Percentage Change QTD | YTD |
|---|---|---|---|---|---|---|
| Energy & Engineering: | | | | | | |
| Offshore Energy | $ 15,266 | $ 20,411 | $ 28,534 | $ 31,731 | -25.2% | -10.1% |
| Onshore Energy | 11,485 | 14,694 | 16,754 | 18,920 | -21.8% | -11.4% |
| Engineering and Construction | 9,665 | 12,402 | 14,673 | 20,597 | -22.1% | -28.8% |
| U.S. Direct and Facultative Property | 3,846 | | 5,374 | | NM | NM |
| Energy & Engineering | $ 40,262 | $ 47,507 | $ 65,335 | $ 71,248 | -15.2% | -8.3% |
| Other Property Casualty | 955 | 1,471 | 940 | 2,026 | -35.1% | -53.6% |
| Total Property Casualty | $ 41,217 | $ 48,978 | $ 66,275 | $ 73,274 | -15.8% | -9.6% |

NM - Percentage change not meanigful

The Lloyd s Operations Property Casualty gross written premiums decreased 15.8% and 9.6% for the three and six months ended June 30, 2013 compared to the same periods in 2012. The decreases are primarily due to reductions in new business growth across all lines, partially offset by new business from our U.S. direct and facultative property lines that we began writing in 2013.

The Lloyd s Operations Property Casualty business achieved a 2.0% and 1.9% increase on renewal rates for the three and six months ended June 30, 2013.

*Professional Liability Premiums.* The gross written premiums for the Professional Liability business for the three and six months ended June 30, 2013 and 2012 consisted of the following:

| In thousands | Three Months Ended June 30, 2013 | 2012 | Six Months Ended June 30, 2013 | 2012 | Percentage Change QTD | YTD |
|---|---|---|---|---|---|---|
| Management Liability | $ 11,257 | $ 9,309 | $ 21,498 | $ 15,739 | 20.9% | 36.6% |
| Errors & Omissions | 5,196 | 3,599 | 7,847 | 5,909 | 44.4% | 32.8% |
| Total Professional Liability | $ 16,453 | $ 12,908 | $ 29,345 | $ 21,648 | 27.5% | 35.6% |

The Lloyd s Operations Professional Liability gross written premiums increased 27.5% and 35.6% for the three and six months ended June 30, 2013 compared to the same periods in 2012, as a result of new business growth, partially offset by decreases in renewal rates of 0.5% and 1.9% for the three and six months ended, respectively.

***Capital Resources***

We monitor our capital adequacy to support our business on a regular basis. The future capital requirements of our business will depend on many factors, including our ability to write new business successfully and to establish premium rates and reserves at levels sufficient to cover losses. Our ability to underwrite is largely dependent upon the quality of our claims paying and financial strength ratings as evaluated by independent rating agencies. In particular, we require (1) sufficient capital to maintain our financial strength ratings, as issued by various ratings agencies, at a level considered necessary by management to enable our Insurance Companies to compete, (2) sufficient capital to enable our Insurance Companies to meet the capital adequacy tests performed by statutory agencies in the United States and the United Kingdom and

(3) letters of credit and other forms of collateral that are necessary to support the business plan of our Lloyd s Operations.

Our capital resources consist of funds deployed or available to be deployed to support our business operations. As of June 30, 2013 and December 31, 2012, our capital resources were as follows:

| In thousands | June 30, 2013 | December 31, 2012 |
| --- | --- | --- |
| Senior Notes | $ 114,502 | $ 114,424 |
| Stockholders equity | 873,952 | 879,485 |
| Total capitalization | $ 988,454 | $ 993,909 |
| Ratio of debt to total capitalization | 11.6% | 11.5% |

As part of our capital management program, we may seek to raise additional capital or may seek to return capital to our stockholders through share repurchases, cash dividends or other methods (or a combination of such methods). Any such determination will be at the discretion of the Parent Company s Board of Directors and will be dependent upon our profits, financial requirements and other factors, including legal restrictions, rating agency requirements, credit facility limitations and such other factors as our Board of Directors deems relevant.

In July 2012, we filed a universal shelf registration statement with the SEC. This registration statement, which expires in July 2015, allows for the future possible offer and sale by the Company of up to $500 million in the aggregate of various types of securities including common stock, preferred stock, debt securities, depositary shares, warrants, units or stock purchase contracts and stock purchase units. The shelf registration statement enables us to efficiently access the public equity or debt markets in order to meet future capital needs, if necessary. This report is not an offer to sell or the solicitation of an offer to buy nor shall there be any sale of these securities in any state in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of such state.

We primarily rely upon dividends from our subsidiaries to meet our Parent Company s obligations. Since the issuance of the senior debt in April 2006, the Parent Company s cash obligations primarily consist of semi-annual interest payments on the senior debt, which are currently $4.0 million. Going forward, the interest payments may be made from funds currently at the Parent Company or dividends from its subsidiaries.

Navigators Insurance Company may pay dividends to the Parent Company out of its statutory earned surplus pursuant to statutory restrictions imposed under the New York insurance law. As of June 30, 2013, the maximum amount available for the payment of dividends by Navigators Insurance Company in 2013 without prior regulatory approval is $70.7 million. During the preceding 12 month period Navigators Insurance Company declared and paid $5.0 million in dividends to the Parent Company, none of which were declared and paid in the second quarter of 2013.

Navigators Corporate Underwriters Ltd. ( NCUL ) may pay dividends to the Parent Company up to the extent of available profits that have been distributed from Syndicate 1221 and as of June 30, 2013 that amount was $8.0 million (£5.3 million).

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Condensed Parent Company balance sheets as of June 30, 2013 (unaudited) and December 31, 2012 are shown in the table below:

| In thousands | June 30, 2013 | December 31, 2012 |
|---|---|---|
| Cash and investments | $ 9,758 | $ 15,026 |
| Investments in subsidiaries | 948,621 | 955,024 |
| Goodwill and other intangible assets | 2,533 | 2,534 |
| Other assets | 29,405 | 23,219 |
| Total assets | $ 990,317 | $ 995,803 |
| Senior Notes | $ 114,502 | $ 114,424 |
| Accounts payable and other liabilities | 521 | 552 |
| Accrued interest payable | 1,342 | 1,342 |
| Total liabilities | $ 116,365 | $ 116,318 |
| Stockholders equity | $ 873,952 | $ 879,485 |
| Total liabilities and stockholders equity | $ 990,317 | $ 995,803 |

On November 22, 2012, we entered into a $165 million credit facility agreement with ING Bank N.V., London Branch, individually and as Administrative Agent, and a syndicate of lenders. The new credit facility amended and restated a $165 million letter of credit facility entered into by the parties on March 28, 2011. The credit facility, which is denominated in U.S. dollars, is utilized to fund our participation in Syndicate 1221 through letters of credit for the 2013 and 2014 underwriting years, as well as open prior years. The letters of credit issued under the facility are denominated in British pounds and their aggregate face amount will fluctuate based on exchange rates. If any letters of credit remain outstanding under the facility after December 31, 2014, we would be required to post additional collateral to secure the remaining letters of credit. As of June 30, 2013, letters of credit with an aggregate face amount of $142.6 million were outstanding under the credit facility and we have $0.8 million of cash collateral posted.

This credit facility contains customary covenants for facilities of this type, including restrictions on indebtedness and liens, limitations on mergers, dividends and the sale of assets, and requirements as to maintaining certain consolidated tangible net worth, statutory surplus and other financial ratios. The credit facility also provides for customary events of default, including failure to pay principal, interest or fees when due, failure to comply with covenants, any representation or warranty made by the Company being false in any material respect, default under certain other indebtedness, certain insolvency or receivership events affecting the Company and its subsidiaries, the occurrence of certain material judgments, or a change in control of the Company. The letter of credit facility is secured by a pledge of the stock of certain insurance subsidiaries of the Company. To the extent the aggregate face amount issued under the credit facility exceeds the commitment amount, we are required to post collateral with the lead bank of the consortium. We were in compliance with all covenants under the credit facility as of June 30, 2013.

The applicable margin and applicable fee rate payable under the credit facility are based on a tiered schedule that is based on the Company s then-current ratings issued by S&P and Moody s with respect to the Company s Senior Notes without third-party credit enhancement, and the amount of the Company s own collateral utilized to fund its participation in Syndicate 1221.

Time lags do occur in the normal course of business between the time gross loss reserves are paid by the Company and the time such gross paid losses are billed and collected from reinsurers. Reinsurance recoverable amounts related to gross loss reserves as of June 30, 2013 are anticipated to be billed and collected over the next several years as the gross loss reserves are paid by the Company.

Generally, for pro rata or quota share reinsurers, we issue quarterly settlement statements for premiums less commissions and paid loss activity, which are expected to be settled within 30-45 days. We have the ability to issue cash calls requiring such reinsurers to pay losses whenever paid loss activity for a claim ceded to a particular reinsurance treaty exceeds a predetermined amount (generally $0.5 million to $1.0 million) as set forth in the pro rata treaty. For the Insurance Companies, cash calls must generally be paid within 30 calendar days. There is generally no specific settlement period for the Lloyd s Operations cash call provisions, but such billings have historically on average been paid within 45 calendar days.

Generally, for excess-of-loss reinsurers we pay quarterly deposit premiums based on the estimated subject premiums over the contract period (usually one year) that are subsequently adjusted based on actual premiums determined after the expiration of the applicable reinsurance treaty. Paid losses subject to excess-of-loss recoveries are generally billed as they occur and are usually settled by reinsurers within 30 calendar days for the Insurance Companies and 30 business days for the Lloyd s Operations.

We sometimes withhold funds from reinsurers and may apply ceded loss billings against such funds in accordance with the applicable reinsurance agreements.

***Liquidity***

**Consolidated Cash Flows**

Cash flow provided by operations was $48.5 million for the six months ended June 30, 2013 compared to $15.0 million for the comparable period in 2012. The increase in cash flow from operations was due to improved collection on premium receivables partially offset by the timing of payments to our reinsurers in connection with the increased use of proportional reinsurance to support our offshore energy business in 2013.

Net cash provided by investing activities was $6.6 million for the six months ended June 30, 2013 compared to net cash used in investing activities of $97.0 million for the same period in 2012. The increase in cash provided by investing activities is driven by the on-going management of our investment portfolio.

Net cash provided by financing activities was $1.5 million for the six months ended June 30, 2013 compared to $0.4 million for the comparable period in 2012. The increase in cash provided by financing activities relates to the exercise of employee stock options.

We believe that the cash flow generated by the operating activities of our subsidiaries will provide sufficient funds for us to meet our liquidity needs over the next twelve months. Beyond the next twelve months, cash flow available to us may be influenced by a variety of factors, including general economic conditions and conditions in the insurance and reinsurance markets, as well as fluctuations from year to year in claims experience.

We believe that we have adequately managed our cash flow requirements related to reinsurance recoveries from their positive cash flows and the use of available short-term funds when applicable. However, there can be no assurances that we will be able to continue to adequately manage such recoveries in the future or that collection disputes or reinsurer insolvencies will not arise that could materially increase the collection time lags or result in recoverable write-offs causing additional incurred losses and liquidity constraints to the Company. The payment of gross claims and related collections from reinsurers with respect to large losses could significantly impact our liquidity needs. However, we expect to collect our paid reinsurance recoverables generally under the terms described above.

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**Investments**

As of June 30, 2013, the weighted average rating of our fixed maturity investments was AA by S&P and Aa by Moody s. The entire fixed maturity investment portfolio, except for investments with a fair value of $18.7 million, consists of investment grade bonds. As of June 30, 2013, our portfolio had a duration of 4.0 years. Management periodically projects cash flow of the investment portfolio and other sources in order to maintain the appropriate levels of liquidity in an effort to ensure our ability to satisfy claims. As of June 30, 2013 and December 31, 2012, all fixed maturity securities and equity securities held by us were classified as available-for-sale.

The following tables set forth the Company s cash and investments as of June 30, 2013 and December 31, 2012. The tables below include OTTI securities recognized within OCI.

| | June 30, 2013 | | | |
|---|---|---|---|---|
| In thousands | Fair Value | Gross Unrealized Gains | Gross Unrealized (Losses) | Cost or Amortized Cost |
| Fixed maturities: | | | | |
| U.S. Treasury bonds, agency bonds and foreign government bonds | $ 464,167 | $ 3,538 | $ (7,492) | $ 468,121 |
| States, municipalities and political subdivisions | 452,084 | 10,281 | (13,114) | 454,917 |
| Mortgage-backed and asset-backed securities: | | | | |
| Agency mortgage-backed securities | 320,150 | 7,782 | (4,645) | 317,013 |
| Residential mortgage obligations | 37,335 | 1,196 | (221) | 36,360 |
| Asset-backed securities | 75,311 | 747 | (113) | 74,677 |
| Commercial mortgage-backed securities | 173,388 | 8,731 | (514) | 165,171 |
| Subtotal | $ 606,184 | $ 18,456 | $ (5,493) | $ 593,221 |
| Corporate bonds | 485,371 | 16,285 | (3,162) | 472,248 |
| Total fixed maturities | $ 2,007,806 | $ 48,560 | $ (29,261) | $ 1,988,507 |
| Equity securities common stocks | 138,549 | 25,238 | (1,910) | 115,221 |
| Short-term investments | 124,726 | | | 124,726 |
| Cash | 101,960 | | | 101,960 |
| Total | $ 2,373,041 | $ 73,798 | $ (31,171) | $ 2,330,414 |

| | December 31, 2012 | | | |
|---|---|---|---|---|
| In thousands | Fair Value | Gross Unrealized Gains | Gross Unrealized (Losses) | Cost or Amortized Cost |
| Fixed maturities: | | | | |
| U.S. Treasury bonds, agency bonds and foreign government bonds | $ 649,692 | $ 8,654 | $ (36) | $ 641,074 |
| States, municipalities and political subdivisions | 322,947 | 18,712 | (380) | 304,615 |
| Mortgage-backed and asset-backed securities: | | | | |
| Agency mortgage-backed securities | 384,445 | 13,652 | (204) | 370,997 |
| Residential mortgage obligations | 38,692 | 1,053 | (549) | 38,188 |
| Asset-backed securities | 50,382 | 1,133 | (49) | 49,298 |
| Commercial mortgage-backed securities | 204,821 | 17,996 | (18) | 186,843 |
| Subtotal | $ 678,340 | $ 33,834 | $ (820) | $ 645,326 |
| Corporate bonds | 470,854 | 27,129 | (25) | 443,750 |
| Total fixed maturities | $ 2,121,833 | $ 88,329 | $ (1,261) | $ 2,034,765 |
| Equity securities common stocks | 101,297 | 16,919 | (626) | 85,004 |

| | | | | |
|---|---|---|---|---|
| Short-term investments | 153,788 | | | 153,788 |
| Cash | 45,336 | | | 45,336 |
| Total | $ 2,422,254 | $ 105,248 | $ (1,887) | $ 2,318,893 |

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As of June 30, 2013 and December 31, 2012, debt securities for which non-credit OTTI was previously recognized and included in other comprehensive income are now in an unrealized gains position of $0.5 million and $20 thousand, respectively.

The fair value of our investment portfolio may fluctuate significantly in response to various factors such as changes in interest rates, investment quality ratings, equity prices, foreign exchange rates and credit spreads. We do not have the intent to sell nor is it more likely than not that we will have to sell debt securities in unrealized loss positions that are not other-than-temporarily impaired before recovery. For structured securities, default probability and severity assumptions differ based on property type, vintage and the stress of the collateral. We do not intend to sell any of these securities and it is more likely than not that we will not be required to sell these securities before the recovery of the amortized cost basis. For equity securities, the Company also considers its intent to hold securities as part of the process of evaluating whether a decline in fair value represents an other-than-temporary decline in value. We may realize investment losses to the extent our liquidity needs require the disposition of fixed maturity securities in unfavorable interest rate, liquidity or credit spread environments. Significant changes in the factors we consider when evaluating investments for impairment losses could result in a significant change in impairment losses reported in the consolidated financial statements.

Invested assets increased from the prior comparable periods in 2012 primarily due to cash flow from operations. The annualized pre-tax investment yields, excluding net realized gains and losses and net OTTI losses recognized in earnings, were 2.4% for the three and six months ended June 30, 2013 compared to 2.8% and 2.4% for the three and six months ended June 30, 2012.

The tax equivalent yields for the three and six months ended June 30, 2013 on a consolidated basis were 2.5% and 2.6%, respectively, compared to 3.0% and 2.6% for the same periods during 2012. The portfolio duration was 4.0 years and 3.9 years for the six months ended June 30, 2013 and 2012, respectively. Since the beginning of 2013, the tax-exempt portion of our investment portfolio has increased by $118.1 million to approximately 19.8% of the fixed maturities investment portfolio as of June 30, 2013 compared to approximately 13.2% as of December 31, 2012.

We are a specialty insurance company and periods of moderate economic recession or inflation tend not to have a significant direct effect on our underwriting operations. They do, however, impact our investment portfolio. A decrease in interest rates will tend to decrease our yield and have a positive effect on the fair value of our invested assets. An increase in interest rates will tend to increase our yield and have a negative effect on the fair value of our invested assets.

The contractual maturity dates for fixed maturity securities categorized by the number of years until maturity as of June 30, 2013 are shown in the following table:

| | June 30, 2013 | |
|---|---|---|
| **In thousands** | **Fair Value** | **Amortized Cost** |
| Due in one year or less | $ 117,677 | $ 116,999 |
| Due after one year through five years | 576,742 | 566,164 |
| Due after five years through ten years | 462,171 | 461,911 |
| Due after ten years | 245,032 | 250,212 |
| Mortgage- and asset-backed securities | 606,184 | 593,221 |
| Total | $ 2,007,806 | $ 1,988,507 |

Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties. Due to the periodic repayment of principal, the aggregate amount of mortgage-backed and asset-backed securities is estimated to have an effective maturity of approximately 4.6 years.

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The following table sets forth the amount and percentage of our fixed maturities as of June 30, 2013 by S&P credit rating or, if an S&P rating is not available, the equivalent Moody s rating. The table includes fixed maturities at fair value, and the total rating is the weighted average quality rating.

| In thousands | Rating | June 30, 2013 Fair Value | Percent of Total |
|---|---|---|---|
| Rating description: | | | |
| Extremely strong | AAA | $ 293,952 | 15% |
| Very strong | AA | 1,088,098 | 53% |
| Strong | A | 454,692 | 23% |
| Adequate | BBB | 152,317 | 8% |
| Speculative | BB & Below | 15,073 | 1% |
| Not rated | NR | 3,674 | 0% |
| Total | AA | $ 2,007,806 | 100% |

The following table sets forth our U.S. Treasury bonds, agency bonds, and foreign government bonds as of June 30, 2013 and December 31, 2012:

| | June 30, 2013 | | | |
|---|---|---|---|---|
| In thousands | Fair Value | Gross Unrealized Gains | Gross Unrealized (Losses) | Amortized Cost |
| U.S. Treasury bonds | $ 412,503 | $ 2,298 | $ (7,247) | $ 417,452 |
| Agency bonds | 48,378 | 1,240 | (179) | 47,317 |
| Foreign government bonds | 3,286 | | (66) | 3,352 |
| **Total** | $ 464,167 | $ 3,538 | $ (7,492) | $ 468,121 |

| | December 31, 2012 | | | |
|---|---|---|---|---|
| In thousands | Fair Value | Gross Unrealized Gains | Gross Unrealized (Losses) | Amortized Cost |
| U.S. Treasury bonds | $ 414,503 | $ 4,441 | $ (10) | $ 410,072 |
| Agency bonds | 155,465 | 3,331 | (11) | 152,145 |
| Foreign government bonds | 79,724 | 882 | (15) | 78,857 |
| **Total** | $ 649,692 | $ 8,654 | $ (36) | $ 641,074 |

The following table sets forth the composition of the investments categorized as states, municipalities and political subdivisions in our portfolio by generally equivalent S&P and Moody s ratings (not all securities in our portfolio are rated by both S&P and Moody s) as of June 30, 2013. The securities that are not rated in the table below are primarily state bonds.

| In thousands | | June 30, 2013 | | |
|---|---|---|---|---|
| Equivalent S&P Rating | Equivalent Moody s Rating | Fair Value | Amortized Cost | Net Unrealized Gain (Loss) |
| AAA/AA/A | Aaa/Aa/A | $ 427,035 | $ 430,039 | $ (3,004) |

| | | | | |
|---|---|---|---|---|
| BBB | Baa | 21,375 | 21,299 | 76 |
| BB | Ba | | | |
| B | B | | | |
| CCC or lower | Caa or lower | | | |
| NR | NR | 3,674 | 3,579 | 95 |
| Total | | $ 452,084 | $ 454,917 | $ (2,833) |

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The following table sets forth the municipal bond holdings by sectors as of June 30, 2013 and December 31, 2012:

| In thousands | June 30, 2013 Fair Value | June 30, 2013 Percent of Total | December 31, 2012 Fair Value | December 31, 2012 Percent of Total |
|---|---|---|---|---|
| Municipal Sector: | | | | |
| General obligation | $ 117,154 | 26% | $ 73,642 | 23% |
| Prerefunded | 23,478 | 5% | 22,692 | 7% |
| Revenue | 256,914 | 57% | 183,096 | 57% |
| Taxable | 54,538 | 12% | 43,517 | 13% |
| Total | $ 452,084 | 100% | $ 322,947 | 100% |

We own $106.5 million of municipal securities which are credit enhanced by various financial guarantors. As of June 30, 2013, the average underlying credit rating for these securities is A+. There has been no material adverse impact to our investment portfolio or results of operations as a result of downgrades of the credit ratings for several of the financial guarantors.

We analyze our mortgage-backed and asset-backed securities by credit quality of the underlying collateral distinguishing between the securities issued by the Federal National Mortgage Association ( FNMA ), the Federal Home Loan Mortgage Corporation ( FHLMC ) and the Government National Mortgage Association ( GNMA ) which are Federal government sponsored entities, and the non-FNMA and non-FHLMC securities broken out by prime, Alternative A-paper ( Alt-A ) and subprime collateral. The securities issued by FNMA and FHLMC are the obligations of each respective entity. Legislation has provided for guarantees by the U.S. Government of up to $100 billion each for FNMA and FHLMC.

Prime collateral consists of mortgages or other collateral from the most creditworthy borrowers. Alt-A collateral consists of mortgages or other collateral from borrowers which have a risk potential that is greater than prime but less than subprime. The subprime collateral consists of mortgages or other collateral from borrowers with low credit ratings. Such subprime and Alt-A categories are as defined by S&P.

The following table sets forth our agency mortgage-backed securities and residential mortgage-backed securities ( RMBS ) by those issued by GNMA, FNMA, and FHLMC, and the quality category (prime, Alt-A and subprime) for all other such investments as of June 30, 2013:

| In thousands | June 30, 2013 Fair Value | Gross Unrealized Gains | Gross Unrealized Losses | Amortized Cost |
|---|---|---|---|---|
| Agency mortgage-backed securities: | | | | |
| GNMA | $ 120,673 | $ 2,892 | $ (2,759) | $ 120,540 |
| FNMA | 154,398 | 4,115 | (1,634) | 151,917 |
| FHLMC | 45,079 | 775 | (252) | 44,556 |
| Total agency mortgage-backed securities | $ 320,150 | $ 7,782 | $ (4,645) | $ 317,013 |
| Residential mortgage-backed securities: | | | | |
| Prime | $ 11,872 | $ 423 | $ (183) | $ 11,632 |
| Alt-A | 2,111 | 110 | (38) | 2,039 |
| Subprime | 630 | 27 | | 603 |
| Non-U.S. RMBS | 22,722 | 636 | | 22,086 |
| Total residential mortgage-backed securities | $ 37,335 | $ 1,196 | $ (221) | $ 36,360 |

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The following table sets forth the composition of the investments categorized as RMBS in our portfolio by generally equivalent S&P and Moody s ratings (not all securities in our portfolio are rated by both S&P and Moody s) as of June 30, 2013:

| In thousands | | June 30, 2013 | | |
|---|---|---|---|---|
| Equivalent S&P Rating | Equivalent Moody s Rating | Fair Value | Amortized Cost | Net Unrealized Gain (Loss) |
| AAA/AA/A | Aaa/Aa/A | $ 23,632 | $ 22,944 | $ 688 |
| BBB | Baa | 2,155 | 2,195 | (40) |
| BB | Ba | 1,566 | 1,624 | (58) |
| B | B | 2,345 | 2,324 | 21 |
| CCC or lower | Caa or lower | 7,637 | 7,273 | 364 |
| NR | NR | | | |
| Total | | $ 37,335 | $ 36,360 | $ 975 |

Details of the collateral of our asset-backed securities portfolio as of June 30, 2013 are presented below:

| In thousands | AAA | AA | A | BBB | BB | CCC | Fair Value | Amortized Cost | Unrealized Gain (Loss) |
|---|---|---|---|---|---|---|---|---|---|
| Auto loans | $ 9,763 | $ 3,522 | $ 8,974 | $ | $ | $ | $ 22,259 | $ 22,140 | $ 119 |
| Credit cards | 13,792 | | | | | | 13,792 | 13,465 | 327 |
| Collateralized Debt Obligations | 18,000 | | | | | | 18,000 | 18,000 | |
| Time Share | | | 13,097 | | | | 13,097 | 12,870 | 227 |
| Student Loans | 4,803 | 2,987 | | | | | 7,790 | 7,833 | (43) |
| Miscellaneous | 373 | | | | | | 373 | 369 | 4 |
| Total | $ 46,731 | $ 6,509 | $ 22,071 | $ | $ | $ | $ 75,311 | $ 74,677 | $ 634 |

The following table sets forth the composition of the investments categorized as commercial mortgage-backed securities in our portfolio by generally equivalent S&P and Moody s ratings (not all securities in our portfolio are rated by both S&P and Moody s) as of June 30, 2013:

| In thousands | | June 30, 2013 | | |
|---|---|---|---|---|
| Equivalent S&P Rating | Equivalent Moody s Rating | Fair Value | Amortized Cost | Net Unrealized Gain (Loss) |
| AAA/AA/A | Aaa/Aa/A | $ 173,388 | $ 165,171 | $ 8,217 |
| BBB | Baa | | | |
| BB | Ba | | | |
| B | B | | | |
| CCC or lower | Caa or lower | | | |
| NR | NR | | | |
| Total | | $ 173,388 | $ 165,171 | $ 8,217 |

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The following table sets forth the composition of the investments categorized as corporate bonds in our portfolio by generally equivalent S&P and Moody s ratings (not all securities in our portfolio are rated by both S&P and Moody s) as of June 30, 2013:

| In thousands Equivalent S&P Rating | Equivalent Moody s Rating | June 30, 2013 Fair Value | Amortized Cost | Net Unrealized Gain (Loss) |
|---|---|---|---|---|
| AAA/AA/A | Aaa/Aa/A | $ 353,059 | $ 343,373 | $ 9,686 |
| BBB | Baa | 128,787 | 125,475 | 3,312 |
| BB | Ba | 3,525 | 3,400 | 125 |
| B | B | | | |
| CCC or lower | Caa or lower | | | |
| NR | NR | | | |
| Total | | $ 485,371 | $ 472,248 | $ 13,123 |

The company holds non-sovereign European securities of $67.7 million at fair value and $67.4 million at amortized cost, primarily in the investment portfolio. This represents 3.2% of our total fixed income and equity portfolio. Our largest exposure is in France with a total of $31.8 million followed by the Netherlands with a total of $22.1 million. We have no direct material exposure to Greece, Portugal, Italy or Spain as of June 30, 2013.

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The following table summarizes all securities in a gross unrealized loss position as of June 30, 2013 and December 31, 2012, showing the aggregate fair value and gross unrealized loss by the length of time those securities had continuously been in a gross unrealized loss position as well as the number of securities:

| | June 30, 2013 | | | December 31, 2012 | | |
|---|---|---|---|---|---|---|
| In thousands, except # of securities | Number of Securities | Fair Value | Gross Unrealized Loss | Number of Securities | Fair Value | Gross Unrealized Loss |
| Fixed maturities: | | | | | | |
| U.S. Treasury bonds, agency bonds, and foreign government bonds | | | | | | |
| 0-6 months | 60 | $ 278,158 | $ 7,492 | 8 | $ 23,760 | $ 22 |
| 7-12 months | | | | 3 | 14,118 | 11 |
| > 12 months | | | | 1 | 4,652 | 3 |
| Subtotal | 60 | $ 278,158 | $ 7,492 | 12 | $ 42,530 | $ 36 |
| States, municipalities and political subdivisions | | | | | | |
| 0-6 months | 110 | $ 223,186 | $ 11,556 | 10 | $ 21,299 | $ 325 |
| 7-12 months | 7 | 17,168 | 1,546 | | | |
| > 12 months | 3 | 1,970 | 12 | 4 | 2,908 | 55 |
| Subtotal | 120 | $ 242,324 | $ 13,114 | 14 | $ 24,207 | $ 380 |
| Agency mortgage-backed securities | | | | | | |
| 0-6 months | 89 | $ 104,138 | $ 3,096 | 10 | $ 62,516 | $ 174 |
| 7-12 months | 9 | 24,070 | 1,431 | 2 | 1,671 | 30 |
| > 12 months | 2 | 1,559 | 118 | | | |
| Subtotal | 100 | $ 129,767 | $ 4,645 | 12 | $ 64,187 | $ 204 |
| Residential mortgage obligations | | | | | | |
| 0-6 months | 12 | $ 2,953 | $ 47 | 6 | $ 1,825 | $ 22 |
| 7-12 months | | | | | | |
| > 12 months | 17 | 3,140 | 174 | 35 | 7,252 | 527 |
| Subtotal | 29 | $ 6,093 | $ 221 | 41 | $ 9,077 | $ 549 |
| Asset-backed securities | | | | | | |
| 0-6 months | 4 | $ 16,905 | $ 29 | | $ | $ |
| 7-12 months | | | | | | |
| > 12 months | 1 | 1,634 | 84 | 2 | 2,369 | 49 |
| Subtotal | 5 | $ 18,539 | $ 113 | 2 | $ 2,369 | $ 49 |
| Commercial mortgage-backed securities | | | | | | |
| 0-6 months | 5 | $ 15,143 | $ 488 | 7 | $ 2,639 | $ 7 |
| 7-12 months | 2 | 651 | 10 | | | |
| > 12 months | 3 | 559 | 16 | 5 | 845 | 11 |
| Subtotal | 10 | $ 16,353 | $ 514 | 12 | $ 3,484 | $ 18 |
| Corporate bonds | | | | | | |
| 0-6 months | 43 | $ 121,470 | $ 3,162 | 2 | $ 3,528 | $ 6 |
| 7-12 months | | | | | | |
| > 12 months | | | | 4 | 6,689 | 19 |
| Subtotal | 43 | $ 121,470 | $ 3,162 | 6 | $ 10,217 | $ 25 |
| Total fixed maturities | 367 | $ 812,704 | $ 29,261 | 99 | $ 156,071 | $ 1,261 |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Equity securities common stocks | | | | | | | | | | |
| 0-6 months | 6 | $ | 33,817 | $ | 1,910 | 13 | $ | 23,345 | $ | 522 |
| 7-12 months | | | | | | 1 | | 1,943 | | 104 |
| > 12 months | | | | | | | | | | |
| Total equity securities | 6 | $ | 33,817 | $ | 1,910 | 14 | $ | 25,288 | $ | 626 |

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We analyze the unrealized losses quarterly to determine if any are other-than-temporary. The above unrealized losses have been determined to be temporary based on our policies.

In the above table the gross unrealized loss for the greater than 12 months category consists primarily of residential mortgage-backed securities. Residential mortgage-backed securities are a type of fixed income security in which residential mortgage loans are sold into a trust or special purpose vehicle, thereby securitizing the cash flows of the mortgage loans.

To determine whether the unrealized loss on structured securities is other-than-temporary, we analyze the projections provided by our investment managers with respect to an expected principal loss under a range of scenarios and utilize the most likely outcomes. The analysis relies on actual collateral performance measures such as default rate, prepayment rate and loss severity. These assumptions are applied throughout the remaining term of the deal, incorporating the transaction structure and priority of payments, to generate loss adjusted cash flows. Results of the analysis will indicate whether the security is expected ultimately to incur a loss or whether there is a material impact on yield due to either a projected loss or a change in cash flow timing. A break even default rate is also calculated. A comparison of the break even default rate to the actual default rate provides an indication of the level of cushion or coverage to the first dollar principal loss. The analysis applies the stated assumptions throughout the remaining term of the transaction to forecast cash flows, which are then applied through the transaction structure to determine whether there is a loss to the security. For securities in which a tranche loss is present, and the net present value of loss adjusted cash flows is less than book value, an impairment is recognized. The output data also includes a number of additional metrics such as average life remaining, original and current credit support, over 60 day delinquency and security rating.

Prepayment assumptions associated with the mortgage-backed and asset-backed securities are reviewed on a periodic basis. When changes in prepayment assumptions are deemed necessary as the result of actual prepayments differing from anticipated prepayments, securities are revalued based upon the new prepayment assumptions utilizing the retrospective accounting method.

As of June 30, 2013 and December 31, 2012, the largest single unrealized loss by issuer in the investment portfolio was $1.4 million and $0.2 million.

The following table sets forth the composition of the investments categorized as fixed maturity securities in our investment portfolio with gross unrealized losses by generally equivalent S&P and Moody s ratings (not all of the securities are rated by S&P and Moody s) as of June 30, 2013:

| In thousands | | June 30, 2013 | | | |
|---|---|---|---|---|---|
| | | Gross Unrealized Loss | | Fair Value | |
| Equivalent S&P Rating | Equivalent Moody s Rating | Amount | Percent of Total | Amount | Percent of Total |
| AAA/AA/A | Aaa/Aa/A | $ 27,918 | 95% | $ 764,310 | 94% |
| BBB | Baa | 1,178 | 5% | 43,854 | 6% |
| BB | Ba | 69 | 0% | 1,318 | 0% |
| B | B | 29 | 0% | 1,574 | 0% |
| CCC or lower | Caa or lower | 67 | 0% | 1,648 | 0% |
| NR | NR | | 0% | | 0% |
| Total | | $ 29,261 | 100% | $ 812,704 | 100% |

As of June 30, 2013, the gross unrealized losses in the table above were related to fixed maturity securities that are rated investment grade, which is defined as a security having an S&P rating of BBB or higher, or a Moody s rating of Baa3 or higher, except for $0.2 million which is rated below investment grade or not rated. Unrealized losses on investment grade securities principally relate to changes in interest rates or changes in sector-related credit spreads since the securities were acquired.

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The contractual maturity for fixed maturity securities categorized by the number of years until maturity, with a gross unrealized loss as of June 30, 2013 is presented in the following table:

| | June 30, 2013 | | | |
|---|---|---|---|---|
| | Gross Unrealized Losses | | Fair Value | |
| In thousands | Amount | Percent of Total | Amount | Percent of Total |
| Due in one year or less | $ 12 | 0% | $ 11,813 | 1% |
| Due after one year through five years | 2,442 | 8% | 192,689 | 24% |
| Due after five years through ten years | 11,394 | 39% | 267,617 | 33% |
| Due after ten years | 9,920 | 34% | 169,833 | 21% |
| Mortgage- and asset-backed securities | 5,493 | 19% | 170,752 | 21% |
| Total | $ 29,261 | 100% | $ 812,704 | 100% |

As of June 30, 2013, there were no investments with a fair value that was less than 80% of amortized cost.

The table below summarizes our activity related to OTTI losses for the periods indicated:

| | Three Months Ended June 30, | | | | Six Months Ended June 30, | | | |
|---|---|---|---|---|---|---|---|---|
| | 2013 | | 2012 | | 2013 | | 2012 | |
| In thousands, except # of securities | Number of Securities | Amount | Number of Securities | Amount | Number of Securities | Amount | Number of Securities | Amount |
| Total OTTI losses: | | | | | | | | |
| Corporate and other bonds | | $ | | $ | | $ | | $ |
| Commercial mortgage-backed securities | | | | | | | | |
| Residential mortgage-backed securities | | | | | | | 1 | 54 |
| Asset-backed securities | | | | | | | | |
| Equities | | | 2 | 496 | 2 | 42 | 3 | 639 |
| Total | | $ | 2 | $ 496 | 2 | $ 42 | 4 | $ 693 |
| Less: Portion of loss in accumulated other comprehensive income (loss): | | | | | | | | |
| Corporate and other bonds | | $ | | $ | | $ | | $ |
| Commercial mortgage-backed securities | | | | | | | | |
| Residential mortgage-backed securities | | | | | | | | 43 |
| Asset-backed securities | | | | | | | | |
| Equities | | | | | | | | |
| Total | | $ | | $ | | $ | | $ 43 |
| Impairment losses recognized in earnings: | | | | | | | | |
| Corporate and other bonds | | $ | | $ | | $ | | $ |
| Commercial mortgage-backed securities | | | | | | | | |
| Residential mortgage-backed securities | | | | | | | | 11 |
| Asset-backed securities | | | | | | | | |
| Equities | | | | 496 | | 42 | | 639 |
| Total | | $ | | $ 496 | | $ 42 | | $ 650 |

During the three months ended June 30, 2012, we recognized OTTI losses of $0.5 million related to two equity securities. During the six months ended June 30, 2012, we recognized OTTI losses of $0.7 million related to one non-agency mortgage-backed security and three equity securities.

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***Item 3. Quantitative and Qualitative Disclosures about Market Risk***

The following updates our disclosure regarding foreign currency exchange rate risk as previously stated in the Company s 2012 Annual Report on Form 10-K.

***Foreign Currency Exchange Rate Risk***

Our Lloyd s Operations are exposed to foreign currency exchange rate risk primarily related to foreign-denominated cash, cash equivalents and marketable securities ( foreign funds ), premiums receivable, reinsurance recoverables on paid and unpaid losses and loss adjustment expenses as well as reserves for losses and loss adjustment expenses. The principal currencies creating foreign currency exchange risk for the Lloyd s Operations are the British pound, the Euro and the Canadian dollar. The Lloyd s Operations manages its foreign currency exchange rate risk primarily through asset-liability matching.

Based on the primary foreign-denominated balances within the Lloyd s Operations as of June 30, 2013, an assumed 5%, 10% and 15% negative currency movement would result in changes as follows:

| | | June 30, 2013 | | |
|---|---|---|---|---|
| | | Negative Currency Movement of | | |
| **In millions** | **USD Equivalent** | **5%** | **10%** | **15%** |
| Cash, cash equivalents and marketable securities at fair value | $ 95.5 | $ (4.8) | $ (9.6) | $ (14.3) |
| Premiums receivable | $ 34.7 | $ (1.7) | $ (3.5) | $ (5.2) |
| Reinsurance recoverables on paid, unpaid losses and LAE | $ 41.8 | $ (2.1) | $ (4.2) | $ (6.3) |
| Reserves for losses and loss adjustment expenses | $ 125.1 | $ 6.3 | $ 12.5 | $ 18.8 |

***Item 4. Controls and Procedures***

(a) The Chief Executive Officer and Chief Financial Officer of the Company have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act )), as of the end of the period covered by this quarterly report. Based on such evaluation, such officers have concluded that as of the end of such period the Company s disclosure controls and procedures are effective in identifying, on a timely basis, material information required to be disclosed in our reports filed or submitted under the Exchange Act.

(b) There have been no changes during our second fiscal quarter in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

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**PART II OTHER INFORMATION**

***Item 1. Legal Proceedings***

In the ordinary course of conducting business, our subsidiaries are involved in various legal proceedings, either indirectly as insurers for parties or directly as defendants. Most of the these proceedings consist of claims litigation involving our subsidiaries as either (a) liability insurers defending or providing indemnity for third party claims brought against insureds or (b) insurers defending first party coverage claims brought against them. We account for such activity through the establishment of unpaid loss and loss adjustment reserves. Our management believes that the ultimate liability, if any, with respect to such ordinary-course claims litigation, after consideration of provisions made for potential losses and cost of defense, will not be material to our consolidated financial condition, results of operations, or cash flows.

Our subsidiaries are also from time to time involved with other legal actions, some of which assert claims for substantial amounts. These actions include claims asserting extra contractual obligations, such as claims involving allegations of bad faith in the handling of claims or the underwriting of policies. In general, we believe we have valid defenses to these cases. Our management expects that the ultimate liability, if any, with respect to such extra-contractual matters will not be material to our consolidated financial position. Nonetheless, given the large or indeterminate amounts sought in certain of these matters, and the inherent unpredictability of litigation, an adverse outcome in such matters could, from time to time, have a material adverse outcome on our consolidated results of operations or cash flows in a particular fiscal quarter or year.

***Item 1A. Risk Factors***

There have been no material changes from the risk factors as previously disclosed in the Company s 2012 Annual Report on Form 10-K.

***Item 2. Unregistered Sales of Equity Securities and Use of Proceeds***

None

***Item 3. Defaults Upon Senior Securities***

None

***Item 4. Mine Safety Disclosures***

Not applicable

***Item 5. Other Information***

None

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***Item 6. Exhibits***

| Exhibit No. | Description of Exhibit | |
|---|---|---|
| 11-1 | Computation of Per Share Earnings | * |
| 31-1 | Certification of CEO per Section 302 of the Sarbanes-Oxley Act | * |
| 31-2 | Certification of CFO per Section 302 of the Sarbanes-Oxley Act | * |
| 32-1 | Certification of CEO per Section 906 of the Sarbanes-Oxley Act<br><br>(This exhibit is intended to be furnished in accordance with Regulation S-K item 601(b)(32)(ii) and shall not be deemed to be filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, or incorporated by reference into any filing under the Securities Act of 1933, except as shall be expressly set forth by specific reference). | * |
| 32-2 | Certification of CFO per Section 906 of the Sarbanes-Oxley Act<br><br>(This exhibit is intended to be furnished in accordance with Regulation S-K item 601(b)(32)(ii) and shall not be deemed to be filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, or incorporated by reference into any filing under the Securities Act of 1933, except as shall be expressly set forth by specific reference). | * |
| 101.INS | XBRL Instance Document | * |
| 101.SCH | XBRL Taxonomy Extension Scheme | * |
| 101.CAL | XBRL Taxonomy Extension Calculation Database | * |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase | * |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase | * |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase | * |

* Included herein

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***Signatures***

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

| | |
|---|---|
| | The Navigators Group, Inc.<br>(Registrant) |
| Date: August 9, 2013 | /s/ Ciro M. DeFalco<br>Ciro M. DeFalco<br>Senior Vice President and Chief Financial Officer |

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