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Sirius International Insurance Corp.

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Sirius International Insurance Corp.

The rating on Sirius International Insurance Corp. reflects its core status as a member of the Bermuda-based White Mountains Re Group Ltd. (WMRe; core operating entities rated A-/Stable/--). The following analysis is based on a review of the company on a stand-alone basis.

Major Rating Factors

Strengths:

- Historically strong operating performance
- Very strong capitalization
- Improving competitive position as a member of the White Mountains Group Ltd.

Weaknesses:

- Marked increase in the company's risk appetite

Holding Company: White Mountains Insurance Group Ltd.
Counterparty Credit Rating <i>Local Currency</i> BBB/Negative/--
Operating Companies Covered By This Report
Financial Strength Rating <i>Local Currency</i> A-/Stable/--

Rationale

The ratings on Stockholm-based reinsurer Sirius International Insurance Corp. (Sirius) reflect its core status as a member of the Bermuda-based White Mountains Re Group Ltd. (WMRe, core operating entities rated A-/Stable/--). As a core entity of WMRe, the ratings and outlook on Sirius would be affected by any change in the ratings or outlook on WMRe. Standard & Poor's Ratings Services considers the company's operations as a significant strength for the ratings on WMRe.

On a stand-alone basis, the key rating factors include Sirius' very strong capitalization, historically strong operating performance, and its improved competitive position as a member of the Bermuda-based White Mountains Insurance Group Ltd. (WTM; BBB/Negative/--). The ratings are constrained, however, by the increase in the company's risk appetite as a member of WMRe.

We consider Sirius to be core to WMRe, reflecting the breadth of the company's financial and operational integration within the group and ultimately within WTM, as illustrated by the demonstrable fungibility of risk within the group. As a member of WTM, the company benefits from intragroup business, which adds further diversification to premium income (both by geography and lines of business) and earnings. For 2008, intragroup business is likely to account for about 45% of the total premium income (46% in 2007). Sirius benefits from groupwide initiatives such as dynamic financial analysis for capital allocation purposes.

Sirius' capitalization is very strong, underpinned by its very strong risk-based capital adequacy according to Standard & Poor's proprietary model. The capital position of the company is expected to remain very strong despite increased investments in equities and affiliates, which together accounted for 24% of total investments at October 2008. The company's very strong capitalization also reflects the capital protection afforded by the regulatory

environment in Sweden.

Sirius' historical operating performance is strong as evidenced by the company's outperformance of its European peers over an extended period. Although the downturn in the financial markets will negatively affect the company, we believe Sirius will be more resilient to these effects than its peers partly due to its consistently strong underwriting performance. For the period ended Sept. 30, 2008, Sirius posted a very strong combined ratio of 86% largely due to a one-off reserve release on prior year, which reduced the ratio by about 12 percentage points. Nevertheless, its post-tax profit reduced significantly to Swedish krona (SEK) 354 million at September 2008, largely because of diminished investment returns resulting from the current economic conditions. Excluding the impact of reserve releases we forecast that the company is likely to post a combined ratio of about 100% at year-end 2008, reflecting the company's losses to the European hailstorms and Hurricane Ike. On an accident-year basis, the company's combined ratio is expected to be in line with its peers.

As a member of WMRe, Sirius' risk appetite has increased more than Standard & Poor's had expected, although not yet to an extent that would threaten the company's very strong capitalization. This was most evident in Sirius' decision to cease purchasing nonproportional retrocession for its peak exposures in 2004, albeit this stance has been substantially reversed. Nevertheless, residual uncertainty about the extent to which WMRe might seek to place risk with Sirius further acts as a drag on the ratings.

Outlook

The stable outlook on Sirius reflects the stable outlook on other core entities of WMRe. As a core subsidiary of WMRe, the ratings on the company will move in tandem with those on the parent.

Subject to normal loss experience we expect Sirius' net combined ratio (excluding the positive impact of reserve releases) to revert to its historical trends, below 95%, over the rating horizon. We expect Sirius to maintain its very strong capitalization.

Sirius is viewed as a rating strength to the group and we expect this to continue over the rating horizon. Negative rating action would be driven by a sustained downturn in operating performance or competitive position or a significant deterioration in risk-based capital adequacy that would most likely arise from capital demands elsewhere in the group.

Corporate Profile: Sirius Leads International Business Of White Mountains Re Group Ltd.

Sirius is a core member of WMRe--WTM's reinsurance division. WMRe is the hub of WMRe's international business, focusing on property, motor, marine, aviation, accident and health, and specialty lines in Europe, the U.S., and Asia.

During 2006, Sirius commuted its pre-existing inwards quota share agreement with affiliate OneBeacon Insurance group (main entities are rated A/Negative/--) and began providing reinsurance capacity, again on a quota share basis, to its affiliates Esurance (not rated)--a direct writer of personal auto insurance in the U.S. This agreement is likely to account for 36% of Sirius' gross premium income in 2008. In addition, Sirius continues to provide quota share capacity to its affiliate White Mountains Reinsurance Company of America (rated A-/Stable, previously

known as Folksam Reinsurance Co.). This is likely to account for 8% of gross premium income in 2008.

Competitive Position: Strong, Enhanced By White Mountains Insurance Group Ltd.

Table 1

Sirius International Insurance Corp./Business Statistics					
	--Year ended Dec. 31--				
(Mil. SEK)	2007	2006	2005	2004	2003
Gross premiums written	6,652.0	7,988	5,570	5,766	6,891
Annual change in gross premiums written (%)	16.7	43.4	(3.4)	(16.3)	4.1
Net premiums written	5,810.0	7,257	4,877	4,781	5,292
Annual change in net premiums written (%)	19.9	48.8	2	(9.7)	6.7
Net premiums earned	6,019.0	5,898	4,988	4,608	5,344
Unearned premiums reserves/net premiums earned (%)	30.0	35.7	19.2	11.6	14.2
Revenue	6,978.0	6,357	5,559	5,009	5,738

SEK--Swedish krone.

Sirius' historically good competitive position has been enhanced as a result of its membership of WTM and WMRe. The company's business profile benefits from intragroup business, which is expected to account for about 45% of total premium income at year-end 2008(42% in 2007), which brings diversity by both geography and lines of business.

Sirius' consolidated group gross premiums written (GPW) reduced by 17%, from the 2006 level, to SEK6.7 billion in 2007, reflecting the reduced premium rates, the depreciation of SEK against the U.S. dollar, and the distortion caused by the intragroup business. For the first half of 2008, Sirius' gross premium income increased to SEK4.1 billion from SEK3.9 billion for the same period in 2007, partly reflecting the growth in its property, accident, and health accounts.

Sirius currently leads and coleads 34% of its portfolio. The company's leadership credentials have improved as a result of its increased underwriting capacity (to \$50 million per event from \$20 million). This has enabled Sirius to take larger lines on existing programs and increased the breadth of risks it is being shown by brokers, particularly in developing markets such as Eastern Europe. In addition, the company has recently established branches in Denmark and Australia to enhance its competitive position.

The focus of Sirius' book is on short- to medium-tail lines where the company seeks opportunistically to reallocate its capital to maximize its risk-adjusted return in any given year. Historically, Sirius' opportunism was born out of its modest leadership credentials. Nevertheless, Sirius' historical competitive position was not unduly adversely affected by its opportunistic approach, owing to the consistency with which it has applied this approach over an extended period and the longevity of the relationships Sirius enjoys with brokers and cedents. Broker-channel business constitutes about 85% of gross premium income (excluding intragroup business) and the remainder consists of business written directly.

Sirius continues to maintain a well-diversified portfolio, both in terms of the classes of business that it writes and its

geographical spread. During 2007, the premium income per branch was as follows: Stockholm (55%), London (17%), Liege (10%), Zurich (7%), Hamburg (7%), and Singapore (4%).

Property will continue to remain the dominant class, and is likely to account for approximately 45%-50% of the expected gross premiums income (excluding intragroup business) at financial year-end 2008 (50% in 2007). This line of business is written from more than 100 countries and more than 50% of the business emanates from Europe. Accident and health and life is likely to account for approximately 25% at year-end 2008 (21% in 2007) and is almost entirely written out of the London branch. Prospectively personal accident and health will also be written from the Australian branch, but the premium income is not expected to be material over the medium term.

Aviation, which is currently written out of the Zurich branch, is likely to provide about 12% of premium income at year-end 2008 (12% in 2007). Sirius' competitive position has been enhanced through the development of a sustainable franchise in the aviation segment. Prospectively, aviation business will also be written via its Danish branch.

Prospective

Despite the pressure on pricing during 2008, the gross premium income is likely to remain stable at year-end 2008 because of the growth in its property, accident, and health accounts.

Further tangible evidence of the enhancements made to Sirius' competitive position under WTM and WMRe's stewardship could positively influence our view of its financial strength on a stand-alone basis.

Sirius, whose tolerance for European property catastrophe risk is almost at its limit (relative to WMRe's risk appetite), is expected to continue to look for ways to further diversify its portfolio, possibly through acquisitions. Although no transformational acquisitions are expected, more opportunistic bolt-on acquisitions of either underwriting teams or blocks of business can be expected given the history of WMRe and WTM.

Management And Corporate Strategy: Experienced Management Team Is A Positive Ratings Factor

Standard & Poor's considers Sirius' management team to be a marginally positive factor for the ratings. The ongoing close involvement of the executive team from WMRe should enable local management to meet the challenges posed by the continuing uplift in Sirius' risk appetite. The management team intends to enhance the level of diversification to improve the balance of its portfolio.

Operational management

Standard & Poor's considers Sirius to have a very capable and experienced management team, focused on profitability and the cautious development of successful business niches. Although responsibility for the day-to-day operations at Sirius will remain with the incumbent management team, the executive team at both WTM and WMRe will continue to provide additional strategic and operational oversight.

Financial management

WMRe has strengthened financial management at Sirius--particularly by encouraging the company's underwriting team to focus on ensuring that each individual treaty is priced at a level that enables the company as a whole to achieve the target rate of return on equity (ROE) that WTM sets for all its operating subsidiaries, a 7% premium

over the risk-free rate.

Enterprise Risk Management: Adequate With Key Strengths In Cycle And M&A Risk Management

Standard & Poor's considers the enterprise risk management (ERM) program of WMRe group and consequently Sirius to be adequate with key strengths in cycle and M&A risk management. The ERM framework at the Sirius level is robust and appears to be consistent with the risk management practices prescribed by the WMRe group. Future upside for WMRe and consequently Sirius' ERM appraisal will be a function of its ability to further enhance its strategic risk management credentials, and agree a more broad-based definition of the board's risk appetite.

The group has experienced outsized catastrophe losses due to hurricanes KRW in 2005 and has significantly improved its controls since then, especially in the property catastrophe area, which is considered to be the top risk for the group. Standard & Poor's does not expect the insurer to experience losses outside of its normal range from traditional risk areas.

Although the group sees itself as an opportunistic investor that judges every acquisition on a stand-alone basis without reference to synergies, it is planning to take advantage of the diverse businesses that it has put together, creating centers of excellence and common platforms for some of the most complex common problems of the group. A chief risk officer (CRO) position has recently been established within the WMRe group, which is headed by Eckard Roth. Mr. Roth is working on strengthening WMRe's groupwide standards for systematic risk management across all risk classes, which includes its most critical risk, property catastrophe.

Management's opportunistic view supports a favorable approach to cycle risk management. In addition, its longstanding performance measurement system focuses on returns on deployed capital, which is aimed at underwriting as to growth. Underwriting rules such as "no data, no deal" are tightly enforced.

Top management holds regular discussions of emerging risks and the effects on underwriting and claims. These discussions also filter into investment thinking. These discussions, and actions taken as a result, are evidence of good emerging risk management.

WMRe has built an economic capital model this year, which will be used throughout the group to determining overall risk positions as part of its strategic risk management initiatives. The model will be implemented in 2009 for both property and casualty lines. The model determines risk tolerances and risk limits tied to overall group risk profile and risk-adjusted returns. The group has demonstrated quickly exiting nonperforming businesses in the past and also seen in the current environment, which demonstrates a management culture that is very responsive to feedback. In addition, management has developed quantitative risk-reward disciplines within its catastrophe exposures, which if extended to the company's business broadly, would constitute a significant advance in its strategic risk management.

Operating Performance: Historically Strong, But Impaired In 2008, Reflecting The Turbulent Financial Market Conditions

Table 2

Sirius International Insurance Corp./Operating Statistics					
	--Year ended Dec. 31--				
(Mil. SEK)	2007	2006	2005	2004	2003
Gross combined ratio (%)	87.0	81	103	90	99
Gross loss ratio (%)	58.3	49	72	56	72
Net combined ratio (%)	88.3	84.1	101.5	96.4	108.2
Net loss ratio (%)	57.7	51	69	58	78
Net expense ratio (%)	30.7	33	32	39	30
Acquisition expense ratio (%)	26.7	29	28	33	24
Administrative expense ratio (%)	4.0	4.2	4.5	5.7	5.9
Reinsurance result	(189.0)	(322)	83	(405)	(498)
Three-year average combined ratio	91.4	94.0	102.0	102.7	110.8
ROR (%)	23.8	22.0	8.9	11.3	(0.8)
Direct yield on invested assets (%)	6.5	3	3.9	2.8	2.7
Yield (incl. realized) (%)	4.3	(0.4)	8.6	0.9	4.8
Total return (incl. smoothed unrealized & realized) (%)	6.9	3.9	5.2	4.2	4.5
ROE--reported equity (%)	7.5	9.2	7.8	10.2	2.9
ROE--adjusted equity (%)	7.5	9.2	7.8	10.2	2.9
Five-year average ROE--reported equity (%)	7.5	6.1	2.8	2.7	3.1

SEK--Swedish krone.

Sirius' historical operating performance has been strong, reflecting the company's focus on cycle management. Over the past three years, the company reported an average net combined ratio of 91.0%. Although the economic downturn will negatively impact the company's earnings, we believe Sirius will be more resilient to these effects than its peers partly due to its historically strong underwriting performance.

Historical

Sirius' stand-alone (excluding Scandinavian Re) historical operating performance has been strong, with the company reporting a strong average net combined ratio of 91.0% and a return on revenue (ROR) of 17.0% over the past five years. The strong underwriting performance reflects the company's procyclical approach to underwriting. Historically, Sirius' operating performance was negatively affected, however, by the persistent deterioration at Scandinavian Re (see table 3). As part of a planned restructuring, Scandinavian Re was sold to a WMRe holding company at Sept. 30, 2007. Hence, Scandinavian Re will no longer be a drag on Sirius' earnings.

Table 3

Impact Of Scandinavian Re On The Operating Performance Of The Sirius International Group														
	2007		2006		2005		2004		2003		Five-year average		Standard deviation	
(%)	Group	Parent	Group	Parent	Group	Parent	Group	Parent	Group	Parent	Group	Parent	Group	Parent
Net combined ratio	88.3	87.7	84.1	80	101.5	99	96.4	92.5	108.2	95.7	111.7	90.98	9.9	7.3
Return on revenue	23.8	23.4	21.7	25.5	8.9	10.1	11.3	14.3	(0.8)	11	18.08	16.86	9.9	7.04

In 2007, the strong earnings momentum was impaired by the low investment returns largely due to low performance of the equity portfolio and losses relating to the sale of two of its foreign subsidiaries to WMRe. For the period ended Sept. 30, 2008, Sirius reported a combined ratio of 86% due to substantial reserve releases (\$80 million) reducing the combined ratio by 12 percentage points. This has offset the negative impact of Hurricane Ike and the European hailstorms, which are currently estimated to cost the company \$25 million and \$22 million, respectively.

Owing to diminished investment returns, the company reported a pretax operating income of only SEK354 million at September 2008, despite the reserve releases. This result has been hindered largely by SEK356 million in unrealized losses, due to the turbulence in the financial markets.

Historically, Sirius' underwriting result has been augmented by the substantial investment income it has been able to earn on its surplus reserves during this time.

Prospective

Subject to normal loss experience, we expect Sirius' net combined ratio (excluding the positive impact of reserve releases) to revert to its historical trends, below 95%, over the rating horizon. We believe that the company will post a net underlying combined ratio (excluding the reserve release during the first half of 2008) of about 100% for the financial year-end 2008. Bottom-line earnings will reduce significantly at year-end 2008 from the 2007 level owing to the current economic downturn as well as catastrophe losses in 2008 to the current date.

In the short-to-medium term, the company's earnings could benefit from WMRe's emphasis on risk-adjusted returns.

Accounting: IFRS Reporting From 2007

From January 2007 Sirius started reporting in accordance with International Financial Reporting Standards (IFRS). The transition to IFRS did not have a material impact on Standard & Poor's assessment of Sirius' capital adequacy or earnings.

In adjusting 2007 amounts reported under Swedish generally accepted accounting principles (GAAP) to total adjusted capital (TAC) the material changes included:

- Goodwill included in the balance sheet, but deducted from TAC (SEK3318 million);
- Deferred tax liability on untaxed reserves added to TAC (SEK2,581 million). This liability is not expected to crystallize and is consequently viewed as loss absorbing capital by Standard & Poor's.

Standard & Poor's believes Sirius' stand-alone performance is the appropriate metric by which to appraise historical operating performance as the reserving strain caused by Scandinavian Re was considered to be a capital, not an earnings, event.

Investments: Strong, But Volatile Reflecting The Current Financial Turmoil

Table 4

Sirius International Insurance Corp./Investment Statistics					
--Year ended Dec. 31--					
(Mil. SEK)	2007	2006	2005	2004	2003
Total investments	14,240	14,870	15,669	14,396	13,879

Table 4

Sirius International Insurance Corp./Investment Statistics (cont.)					
Investment in affiliates (%)	11.6	0.0	13.4	12.3	0
Loans to affiliates (%)	0.0	0.0	0	0.2	0.2
Bonds and other fixed interest securities (%)	53.8	65.7	64	63	75
Equities and other variable interest securities (%)	15.4	7.4	10.6	12.4	15.3
Property (%)	0.1	0.0	0.1	0.1	0.1
Cash and bank deposits (%)	19.1	26.8	11.7	10.1	8.3
Other investments (%)	0.0	0.1	0	2	1.1
Investment analysis					
Total investment return (incl. unrealized and realized) (%)	1.4	1.5	5.5	5.5	6.7
Investment leverage (incl p/h capital) (%)	49.2	14.7	52	54	35
Liquidity					
Insurance & reinsurance receivables/total assets (%)	5.6	5.0	3.9	4.9	28

SEK--Swedish krone.

Sirius' investment portfolio is strong, but volatile, due to the current economic downturn. As at the end of October 2008, Sirius held 68% of its total invested assets in bonds, 9% in equities, 16% in affiliates, and 7% in cash and cash equivalents. Sirius has increased its exposure to equities since the beginning of 2007 and this was partly reversed at the end of October 2008. At the same time, investments in affiliates were increased to utilize surplus capital. At this stage, given the generous level of surplus capital we consider the investment mix to be appropriate for the current ratings. We do not expect significant changes at year-end 2008.

Sirius' affiliate, White Mountains Advisors, sets the investment strategy and administers the investments for all the WTM companies. The company's strategy is to invest technical reserves in low-risk asset classes such as cash and fixed income; and the balance partly in equities to maximize the risk-adjusted return. The company targets a return on investment equivalent to the yield on 10-year Treasuries plus 150 basis points.

Concentration risk

Concentration risk is not considered excessive, with a highly rated fixed-income portfolio and an equity portfolio spread globally. Sirius' largest single investment is White Mountains International, S.a.r.l. (representing 11% of its total investments in 2007).

Credit risk

The quality of the fixed-income portfolio is strong and credit risk is modest. The company's policy is to invest in rated fixed-income securities rated 'BBB+' or higher. At September 2008, 82% of Sirius' fixed-interest portfolio was invested in 'AAA' rated securities, 5% in the 'AA' range, 4% in the 'A' range, with the balance being held in the 'BBB' range.

Market risk

Market risk within the portfolio arising from the equity exposure is acceptable. Sirius has clear limits on amounts to be invested locally and amounts to be invested in an individual security/issuer.

Liquidity: Very Strong Supported By Surplus Capital

Liquidity is very strong, supported by the surplus capital held at Sirius. At financial year-end 2007, the ratio of liquid assets to technical reserves for the company was 180% (170% in 2006).

Capitalization: Capital Adequacy Remains Resilient To Increased Operating Leverage And Equities

Capitalization remains a key strength for the ratings on Sirius despite the marked increase in its operating leverage over the past few years, which has been greater than expected. Standard & Poor's expects Sirius' capitalization to remain supportive of the current ratings.

Capital adequacy

Sirius' capital adequacy level, measured using Standard & Poor's risk-based model will continue to remain very strong overall. During 2007, the company's capital adequacy level deteriorated, although to a still very strong level, because of increased investments in equities and affiliates. The quality of the company's capital is also very strong. Sirius' capital adequacy has generally trended downward since its acquisition by WTM, reflecting its increased risk appetite as a member of WMRe.

Reserves

Sirius (that is, absent Scandinavian Re) has a long-established track record of reporting modest surpluses in respect of reserves held for prior underwriting years. An external review of the sufficiency of the loss reserves held, by Sirius was performed for the financial year ended Dec. 31, 2007. The outcome of this review suggested that the company holds a substantial amount of reserve redundancy equating to \$80 million (10.5% of total net technical reserves at June 2008) largely relating to the property account. During the second half of 2008, Sirius released all of the reserve redundancy. Management believes that Sirius still has about SEK95 million (2% of net technical reserves) of reserve redundancy.

Reinsurance

The extent of the increase in Sirius' operating leverage as a member of WMRe has been greater than expected. Specifically, the company increased its worldwide and European per-event property catastrophe retention. The company intends to increase its retrocession usage when the markets are perceived to be softening and vice versa in hardening markets.

The reinsurance program represents a diverse composition, spread among securely rated reinsurers, with some exposure to unrated companies for which Sirius holds substantial collateral against reinsurance recoverables.

Sirius's aggregate net probable maximum loss (PML) before reinstatement premiums, at a return period of 250 years, is estimated to be about 27% of its forecasted total adjusted capital at year-end 2008. A charge equating to the one-in-250-year PML has been included in our assessment of Sirius' capital adequacy.

Financial Flexibility: Strong, Driven By WTM

Table 5

Sirius International Insurance Corp./Financial Statistics					
	--Year ended Dec. 31--				
(Mil. SEK)	2007	2006	2005	2004	2003
Total adjusted equity	7,838	7,483	7,290	6,632	6,154
Change in adjusted equity (%)	5	3	9.9	7.8	(12.7)
Total capital	7,838	7,483	7,290	6,632	6,154
Reinsurance exposure ratio (%)	14	15	21	17.7	34
Investment leverage (incl. all quasi capital) (%)	49	15	52	54	35
Affiliated investment leverage (%)	21	0	29	27	0.4
Reinsurance					
Reinsurance utilization ratio (%)	13	9	12.4	17.1	23
Reserving					
Net technical reserves/gross technical reserves (%)	84	87	83	87	78
Technical reserves/net premiums written (%)	120	121	180	186	171
Equity + reserves/net premiums written (%)	120	121	180	186	171
Loss reserves/net premiums written (%)	89	92	162	167	159
Net claims reserves/net claims incurred (%)	149	219	229	301	201
Loss reserves/claims paid (three-year average) (%)	168	195	180	198	246

SEK--Swedish krona.

Sirius' financial flexibility is considered strong and is largely influenced by WTM's capital-management strategies. Aside from the parental capital support, the company also uses internal and external reinsurance to manage its capital. Should the need arise, potential sources of financial flexibility are the issuance of hybrid debt or use of insurance-linked securities.

Ratings Detail (As Of December 18, 2008)*

Holding Company: White Mountains Insurance Group Ltd.

Issuer Credit Rating

Local Currency

BBB/Negative/--

Senior Unsecured (1 Issue)

BBB

Operating Companies Covered By This Report

Sirius International Insurance Corp.

Financial Strength Rating

Local Currency

A-/Stable/--

Counterparty Credit Rating

Local Currency

A-/Stable/--

White Mountains Re America

Financial Strength Rating

Local Currency

A-/Stable/--

Issuer Credit Rating

Local Currency

A-/Stable/--

Ratings Detail (As Of December 18, 2008)* (cont.)	
White Mountains Re Bermuda Ltd.	
Financial Strength Rating	
Local Currency	A-/Stable/--
Issuer Credit Rating	A-/Stable/--
White Mountains Re Group Ltd.	
Issuer Credit Rating	
Local Currency	BBB-/Stable/--
Preference Stock (1 Issue)	BB
Senior Unsecured (1 Issue)	BBB-
Domicile	Sweden
*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.	

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