

**Overview**

Management believes that the Company is principally exposed to five types of market related risk: interest rate risk, credit spread risk, foreign currency risk, counterparty credit risk and equity price risk. How these risks relate to the Company, and the process used to manage them, is discussed below.

As discussed previously in this report, the Company's investment philosophy distinguishes between assets that are generally matched against the estimated net reinsurance assets and liabilities (liability funds) and those assets that represent shareholder capital (capital funds). At December 31, 2008, liability funds represented 61% (or \$7.2 billion) of the Company's total invested assets. Liability funds are invested in a way that generally matches them to the corresponding liabilities in both duration and currency composition. This practice seeks to protect the Company against changes in interest rates and foreign exchange rates. Although the focus of this discussion is to identify risk exposures that impact the market value of assets alone, it is important to recognize that the risks discussed herein are significantly mitigated to the extent that the Company's investment strategy allows market forces to influence the economic valuation of assets and liabilities in a way that is generally offsetting.

At December 31, 2008, capital funds represented 39% (or \$4.7 billion) of the Company's total invested assets. These assets represent shareholders' capital and are invested in a diversified portfolio with the objective of maximizing investment return, subject to prudent risk constraints. Capital funds contain most of the asset classes typically viewed as offering a higher risk and higher return profile, such as preferred and common stocks, private equity and bond investments and convertible and high-yield fixed income securities, in addition to investment-grade securities. At December 31, 2008, 80% of the Company's capital funds were invested in investment grade fixed income securities, which was reflective of the Company's current view of available returns for higher risk assets. The Company's investment philosophy is to reduce foreign currency risk on capital funds by investing primarily in U.S. dollar denominated investments. In considering the market risk of capital funds, it is important to recognize the benefits of portfolio diversification. Although these asset classes in isolation may introduce more risk into the portfolio, market forces have a tendency to influence each class in different ways and at different times. Consequently, the aggregate risk introduced by a portfolio of these assets should be less than might be estimated by summing the individual risks.

The Company's investment strategy allows the use of derivative investments, subject to strict limitations. Derivative instruments may be used to hedge market risk, to enhance investment performance, to replicate investment positions or to manage market exposure and duration risks that would be allowed under the Company's investment policy if implemented in other ways. The use of financial leverage, whether achieved through derivatives or margin borrowing, requires approval from the Risk Management and Finance Committee of the Board. The Company also imposes a high standard for the credit quality of counterparties in all derivative transactions and aims to diversify its counterparty credit risk exposure. (See Note 17 to the Consolidated Financial Statements for additional information concerning derivatives.)

The following comments address those areas where the Company believes it has exposure to material market risk in its operations.

### Interest Rate Risk

The Company's fixed income portfolio is exposed to interest rate risk. Fluctuations in interest rates have a direct impact on the market valuation of these securities. The Company manages interest rate risk on liability funds by constructing bond portfolios in which the economic impact of a general interest rate shift is comparable to the impact on the related liabilities. This process involves matching the duration of the investment portfolio to the estimated duration of the liabilities. For loss reserves and policy benefits related to non-life and traditional life business, the estimated duration of the Company's liabilities is based on projected claims payout patterns. For policy benefits related to annuity business, the Company estimates duration based on its commitment to annuitants. The Company believes that this matching process mitigates the overall interest rate risk on an economic basis. The Company manages the exposure to interest rate volatility on capital funds by choosing a duration profile that it believes will optimize the risk-reward relationship.

While this matching of duration insulates the Company from the economic impact of interest rate changes, changes in interest rates do impact the reported U.S. GAAP shareholders' equity of the Company. The Company's liabilities are carried at their nominal value, and are not adjusted for changes in interest rates, with the exception of certain policy benefits for life and annuity contracts and deposit liabilities that are interest rate sensitive; however, the Company's invested assets are carried at fair value, which reflects such changes. As a result, an increase in interest rates will result in a decrease in the fair value of the Company's investments and a corresponding decrease, net of applicable taxes, in the Company's shareholders' equity. A decrease in interest rates would have the opposite effect.

At December 31, 2008, the Company held approximately \$3,014 million of its total invested assets in mortgage/asset-backed securities. These assets are exposed to prepayment risk, the adverse impact of which is more evident in a declining interest rate environment.

At December 31, 2008, the Company estimates that the hypothetical case of an immediate 100 basis points or 200 basis points parallel shift in global bond curves would result in a change in fair value of investments exposed to interest rates and total invested assets and shareholders' equity as follows (in millions of U.S. dollars):

	-200 basis points	% change	-100 basis points	% change	December 31, 2008	+100 basis points	% change	+200 basis points	% change
Fair value of investments exposed to interest rates (including accrued interest)	\$ 11,992	6%	\$ 11,649	3%	\$ 11,306	\$ 10,963	(3)%	\$ 10,620	(6)%
Total invested assets (including accrued interest)	12,580	6	12,237	3	11,894	11,551	(3)	11,208	(6)
Shareholders' equity	4,885	16	4,542	8	4,199	3,856	(8)	3,513	(16)

This change does not take into account any potential mitigating impact from the equity market, taxes or the corresponding change in the economic value of the Company's reinsurance liabilities, which, as noted above, would substantially offset the economic impact on invested assets, although the offset would not be reflected in the Consolidated Balance Sheets.

As discussed above, the Company strives to match the foreign currency exposure in its fixed income portfolio to its multicurrency liabilities. The Company believes that this matching process creates a diversification benefit. Consequently, the exact market value effect of a change in interest rates will depend on which countries experience interest rate changes and the foreign currency mix of the Company's fixed income portfolio at the time of the interest rate changes. See Foreign Currency Risk.

**Quantitative and Qualitative Disclosures about Market Risk**

At December 31, 2007, the Company estimated that the hypothetical case of an immediate 100 basis point adverse parallel shift in global bond curves would result in an approximate 4%, or \$404 million, decrease in the fair value of investments exposed to interest rates, or an approximate 3% and 9% decrease of the total invested assets and shareholders' equity, respectively. Accordingly, the impact of an immediate change in interest rates on the Company's fair value of investments, total invested assets and shareholders' equity has not changed significantly at December 31, 2008 compared to December 31, 2007.

Interest rate movements also affect the economic value of the Company's outstanding debt obligations and preferred securities in the same way that they affect the Company's fixed income investments, and this can result in a liability whose economic value is different from the value reported in the Consolidated Balance Sheets. The Company believes that the economic fair value of its outstanding long-term debt, senior notes, capital efficient notes (CENts) and preferred securities at December 31, 2008 was as follows (in millions of U.S. dollars):

	Carrying Value	Fair Value
Long-term debt	\$ 200	\$ 196
Senior Notes <sup>(1)</sup>	250	237
Capital efficient notes <sup>(2)</sup>	250	95
Series C cumulative preferred shares	290	220
Series D cumulative preferred shares	230	164

<sup>(1)</sup> *PartnerRe Finance A LLC, the issuer of the Senior Notes, does not meet the consolidation requirements of FIN 46(R). Accordingly, the Company shows the related intercompany debt of \$250.0 million in its Consolidated Balance Sheets.*

<sup>(2)</sup> *PartnerRe Finance II, the issuer of the capital efficient notes, does not meet the consolidation requirements of FIN 46(R). Accordingly, the Company shows the related intercompany debt of \$257.6 million in its Consolidated Balance Sheets. The fair value of the capital efficient notes was based on the initial issuance of \$250.0 million from PartnerRe Finance II.*

The fair value of the long-term debt has been calculated as the present value of estimated future cash flows using a discount rate reflective of the current market cost of borrowing under similar terms and conditions. The fair value of the Senior Notes and CENts has been calculated using quoted market prices based on the initial issuance of \$250.0 million from PartnerRe Finance A and \$250.0 million from PartnerRe Finance II, respectively. For the Company's Series C and Series D cumulative preferred shares, fair value is based on quoted market prices, while carrying value is based on the liquidation value of the securities.

The fair value of the Company's Series C and Series D cumulative preferred shares has not changed significantly at December 31, 2008 compared to December 31, 2007. The \$135 million decrease in the fair value of the capital efficient notes from \$230 million at December 31, 2007 to \$95 million at December 31, 2008 reflects increased credit spreads in the current financial environment for this type of debt instrument.

**Credit Spread Risk**

The Company's fixed income portfolio is exposed to credit spread risk. Fluctuations in market credit spreads have a direct impact on the market valuation of these securities. The Company manages credit spread risk by the selection of securities within its fixed income portfolio. Changes in credit spreads directly affect the market value of certain fixed income securities, but do not necessarily result in a change in the future expected cash flows associated with holding individual securities. Other factors, including liquidity, supply and demand, and changing risk preferences of investors, may affect market credit spreads without any change in the underlying credit quality of the security.

**Quantitative and Qualitative Disclosures about Market Risk**

As with interest rates, changes in credit spreads impact the shareholders' equity of the Company as invested assets are carried at fair value, which includes changes in credit spreads. As a result, an increase in credit spreads will result in a decrease in the fair value of the Company's investments and a corresponding decrease, net of applicable taxes, in the Company's shareholders' equity. A decrease in credit spreads would have the opposite effect.

At December 31, 2008, the Company estimates that the hypothetical case of an immediate 100 basis points or 200 basis points parallel shift in global credit spreads would result in a change in fair value of investments exposed to such spreads and total invested assets and shareholders' equity as follows (in millions of U.S. dollars):

	-200 basis points	% change	-100 basis points	% change	December 31, 2008	+100 basis points	% change	+200 basis points	% change
Fair value of investments exposed to interest rates (including accrued interest)	\$ 11,738	4%	\$ 11,522	2%	\$ 11,306	\$ 11,090	(2)%	\$ 10,874	(4)%
Total invested assets (including accrued interest)	12,326	4	12,110	2	11,894	11,678	(2)	11,462	(4)
Shareholders' equity	4,631	10	4,415	5	4,199	3,983	(5)	3,767	(10)

The impacts of changes in credit spreads for all parallel shifts in basis points are lower than the impacts of changes in interest rates, as the change in credit spreads does not impact government fixed income securities. However, the change in credit spreads does assume that mortgage backed securities issued by government sponsored entities are affected, even though these typically exhibit significantly lower spread volatility than corporate fixed income securities. This change also excludes any impact from the equity market, taxes, and the change in the economic value of the Company's reinsurance liabilities, which may offset the economic impact on invested assets, although the offset would not be reflected in the Consolidated Balance Sheets.

The impact of an immediate change in credit spreads on the Company's fair value of investments, total invested assets and shareholders' equity has not changed significantly at December 31, 2008 compared to December 31, 2007.

**Foreign Currency Risk**

Through its multinational reinsurance operations, the Company conducts business in a variety of non-U.S. currencies, with the principal exposures being the euro, British pound, Canadian dollar, Swiss franc and Japanese yen. As the Company's reporting currency is the U.S. dollar, foreign exchange rate fluctuations may materially impact the Company's Consolidated Financial Statements.

The Company is generally able to match its liability funds against its net reinsurance liabilities both by currency and duration to protect the Company against foreign exchange and interest rate risks. However, a natural offset does not exist for all currencies. For the non-U.S. dollar currencies for which the Company deems the net asset or liability exposures to be material, the Company employs a hedging strategy utilizing foreign exchange forward contracts and other derivative financial instruments, as appropriate, to ensure that its liability funds are matched by currency. The Company does not hedge currencies for which its asset or liability exposures are not material or where it is unable or impractical to do so. In such cases, the Company is exposed to foreign currency risk. However, the Company does not believe that the foreign currency risks corresponding to these unhedged positions are material.

For the Company's capital funds, including its net investment in foreign subsidiaries and branches, the Company does not typically employ hedging strategies. However, due to the foreign exchange volatility in the latter part of 2008, the Company did enter into euro and Canadian dollar hedges (see Currency above).

**Quantitative and Qualitative Disclosures about Market Risk**

The table below summarizes the Company's gross and net exposure in its December 31, 2008 Consolidated Balance Sheet to foreign currency as well as the associated foreign currency derivatives the Company has put in place to manage this exposure (in millions of U.S. dollars):

	euro	GBP	CAD	CHF	JPY	Other	Total <sup>(1)</sup>
Invested assets	\$ 2,869	\$ 284	\$ 493	\$ 20	\$ 26	\$ 47	\$ 3,739
Other net liabilities	(2,373)	(193)	(232)	(224)	(49)	(367)	(3,438)
Total foreign currency exposure	496	91	261	(204)	(23)	(320)	301
Total derivative amount	(98)	(82)	(44)	180	58	320	334
Net foreign currency exposure	\$ 398	\$ 9	\$ 217	\$ (24)	\$ 35	\$ —	\$ 635

<sup>(1)</sup> As the U.S. dollar is the Company's reporting currency, there is no currency risk attached to the U.S. dollar and it is excluded from this table. The U.S. dollar accounted for the difference between the Company's total foreign currency exposure in this table and the invested assets and other net liabilities in the Company's Consolidated Balance Sheet.

The above numbers include the Company's investment in PartnerRe Europe, whose functional currency is the euro, and certain of its branches, whose functional currencies are the euro or Canadian dollar, and the foreign exchange forward contracts that the Company entered into during the fourth quarter of 2008 to hedge a portion of its translation exposure in light of the significant volatility in foreign exchange markets.

Assuming all other variables are held constant and disregarding any tax effects, a change in the U.S. dollar of 10% or 20% relative to the other currencies held by the Company would result in a change in the Company's net assets of \$64 million and \$127 million, respectively, inclusive of the effect of the derivative and net investment hedges.

At December 31, 2007, the Company's net foreign currency exposure in its Consolidated Balance Sheet, after the effect of derivatives, was \$844 million. The \$209 million decrease in the Company's net foreign currency exposure compared to December 31, 2007 primarily reflects a reduction in the Company's euro exposure which is the result of entering into the net investment hedge.

**Counterparty Credit Risk**

The Company has exposure to credit risk primarily as a holder of fixed income securities. The Company controls this exposure by emphasizing investment grade credit quality in the fixed income securities it purchases. At December 31, 2008, approximately 62% of the Company's fixed income portfolio was rated AAA (or equivalent rating), 86% was rated A- or better and 3% of the Company's fixed income portfolio was rated below investment-grade. The Company believes this high quality concentration reduces its exposure to credit risk on fixed income investments to an acceptable level. At December 31, 2008, the Company is not exposed to any significant credit concentration risk on its investments, excluding securities issued by the U.S. and other AAA-rated sovereign governments, with the single largest corporate issuer and the top 10 corporate issuers accounting for 3.4% and 24.7% of the Company's total corporate fixed income securities, respectively. The Company keeps cash and cash equivalents in several banks and may keep up to \$500 million, excluding custodial accounts, at any point in time in any one bank.

To a lesser extent, the Company also has credit risk exposure as a party to foreign exchange forward contracts and other derivative contracts. To mitigate this risk, the Company monitors its exposure by counterparty, aims to diversify its counterparty credit risk and ensures that counterparties to these contracts are high credit quality international banks or counterparties. These contracts are generally of short duration (approximately 90 days) and settle on a net basis, which means that the Company is exposed to the movement of one currency against the other, as opposed to the notional amount of the contracts. At

December 31, 2008, the Company's absolute notional value of foreign exchange forward contracts and foreign currency option contracts, including the net investment hedge, was \$1,764 million, while the net value of those contracts was an unrealized loss of \$13 million.

The Company is also exposed to credit risk in its underwriting operations, most notably in the credit/surety line and as part of its principal finance activities. Loss experience in these lines of business is cyclical and is affected by the general economic environment. The Company provides its clients in these lines of business with protection against credit deterioration, defaults or other types of financial non-performance of or by the underlying credits that are the subject of the protection provided and, accordingly, the Company is exposed to the credit risk of those credits. As with all of the Company's business, these risks are subject to rigorous underwriting and pricing standards. In addition, the Company strives to mitigate the risks associated with these credit-sensitive lines of business through the use of risk management techniques such as risk diversification, careful monitoring of risk aggregations and accumulations and, at times, through the use of retrocessional reinsurance protection and the purchase of credit default swaps and total return and interest rate swaps. The Company purchased protection related to its investment portfolio, credit/surety line and principal finance activities primarily in the form of credit default swaps with a notional value of \$296 million and an unrealized gain of \$20 million at December 31, 2008.

At December 31, 2008, the notional value of the Company's total return swaps was \$240 million with an unrealized loss of \$25 million, and the fair value of its interest rate swaps was an unrealized loss of \$12 million. Separately, the Company has also assumed credit risk to replicate investment positions in the form of credit default swaps with a notional value of \$46 million and an unrealized loss of \$16 million at December 31, 2008.

The Company is subject to the credit risk of its cedants in the event of their insolvency or their failure to honor the value of the funds held balances due to the Company for any other reason. However, the Company's credit risk is somewhat mitigated by the fact that the Company generally has the contractual ability to offset any shortfall in the payment of the funds held balances with amounts owed by the Company to cedants for losses payable and other amounts contractually due. Funds held balances for which the Company receives an investment return based upon either the results of a pool of assets held by the cedant or the investment return earned by the cedant on its investment portfolio are exposed to an additional layer of credit risk. The Company is also exposed to some extent to the underlying financial market risk of the pool of assets, inasmuch as the underlying policies may have guaranteed minimum returns.

The Company has exposure to credit risk as it relates to its business written through brokers if any of the Company's brokers is unable to fulfill their contractual obligations with respect to payments to the Company. In addition, in some jurisdictions, if the broker fails to make payments to the insured under the Company's policy, the Company might remain liable to the insured for the deficiency. See Risk Factors in Item 1A of Part I of the Company's report on Form 10-K for detailed information on two brokers that accounted for approximately 42% of the Company's gross premiums written for the year ended December 31, 2008.

The Company has exposure to credit risk as it relates to its reinsurance balances receivable and reinsurance recoverable on paid and unpaid losses. Reinsurance balances receivable from the Company's clients at December 31, 2008 were \$1,720 million, including balances both currently due and accrued. The Company believes that credit risk related to these balances is mitigated by several factors, including but not limited to, credit checks performed as part of the underwriting process and monitoring of aged receivable balances.

In addition, as the vast majority of its reinsurance agreements permit the Company the right to offset reinsurance balances receivable from clients against losses payable to them, the Company believes that the credit risk in this area is substantially reduced. Provisions are made for amounts considered potentially uncollectible and the allowance for uncollectible reinsurance balances receivable was \$6 million at December 31, 2008.

Although the Company does not rely heavily on retrocessional reinsurance, it does require its reinsurers to have adequate financial strength. The Company evaluates the financial condition of its reinsurers and monitors its concentration of credit risk on an ongoing basis. Provisions are made for amounts considered potentially uncollectible. The balance of reinsurance recoverable on paid and unpaid losses was \$154 million, which is net of the allowance provided for uncollectible reinsurance recoverables of \$6 million at December 31, 2008.

The concentrations of the Company's counterparty credit risk exposures have not changed significantly compared to December 31, 2007.

### Equity Price Risk

The Company invests a portion of its capital funds in marketable equity securities (fair market value of \$439 million, excluding fixed income mutual funds of \$74 million) at December 31, 2008. These equity investments are exposed to equity price risk, defined as the potential for loss in market value due to a decline in equity prices. The Company believes that the effects of diversification and the relatively small size of its investments in equities relative to total invested assets mitigate its exposure to equity price risk. The Company estimates that its equity investment portfolio has a beta versus the S&P 500 and MSCI EAFE Indexes of approximately 0.9 on average. Portfolio beta measures the response of a portfolio's performance relative to a market return, where a beta of 1 would be an equivalent return to the index. Given the estimated beta for the Company's equity portfolio, a 10% and 20% movement in the S&P 500 and MSCI EAFE Indexes would result in a change in the fair value of the Company's equity portfolio, total invested assets and shareholders' equity as follows:

	20% decrease	% change	10% decrease	% change	December 31, 2008	10% increase	% change	20% increase	% change
Equities (excluding fixed income mutual funds)	\$ 362	(17)%	\$ 401	(9)%	\$ 439	\$ 477	9%	\$ 516	17%
Total invested assets (excluding accrued interest)	11,648	(1)	11,687	—	11,725	11,763	—	11,802	1
Shareholders' equity	4,122	(2)	4,161	(1)	4,199	4,237	1	4,276	2

This change does not take into account any potential mitigating impact from the fixed income market or taxes.

At December 31, 2007, the Company estimated that a 10% decrease in the S&P 500 Index would result in an approximate 9%, or \$120 million, decrease in the fair value of the Company's equity portfolio, or an approximate 1% and 3% decrease of the total invested assets and shareholders' equity, respectively. Accordingly, the percentage impact of a decrease in equity markets on the Company's equity portfolio has not changed significantly at December 31, 2008 compared to December 31, 2007, however, the absolute impacts on the Company's equity portfolio, total invested assets and shareholders' equity are significantly reduced compared to December 31, 2007, as a result of the decrease in the equity portfolio.