

As is customary in the reinsurance business, life insurance clients continually update, refine, and revise reinsurance information provided to the Company. Such revised information is used by the Company in preparation of its financial statements and the financial effects resulting from the incorporation of revised data are reflected currently.

Our profitability primarily depends on the volume and amount of death claims incurred and our ability to adequately price the risks we assume. While death claims are reasonably predictable over a period of many years, claims become less predictable over shorter periods and are subject to significant fluctuation from quarter to quarter and year to year. Effective July 1, 2003, we increased the maximum amount of coverage that we retain per life from \$4 million to \$6 million. This increase does not affect business written prior to July 1, 2003. Claims in excess of this retention amount are retroceded to retrocessionaires; however, we remain fully liable to the ceding company, our customer, for the entire amount of risk we assume. The increase in our retention limit from \$4 million to \$6 million reduces the amount of premiums we pay to our retrocessionaires, but increases the maximum impact a single death claim can have on our results and therefore may result in additional volatility to our results.

We maintain catastrophe insurance under a program that renews on August 13th of each year. The current program, which began August 13, 2003 and expires August 12, 2004, provides up to \$50 million of coverage per occurrence for events involving 40 or more deaths. Under this program, we retain the first \$50 million in claims, the catastrophe program covers the next \$50 million in claims, and we retain all claims in excess of \$100 million. Acts of terrorism are covered except when arising from the use of nuclear, chemical, or biological weapons. The insurance is provided through seven insurance companies and seven Lloyds Syndicates with no single insurer providing more than \$10 million of coverage.

We are exposed to foreign currency risk on business conducted in foreign currencies to the extent that the exchange rates of the foreign currencies are subject to adverse change over time. Additionally, we are exposed to the economic and political risk associated with our net investment in foreign locations. Our most significant foreign operations are in Canada. The business generated from the Asia Pacific region is primarily denominated in U.S. dollars, Australian dollars, and Japanese yen. Additionally, we reinsure business in other international currencies including the Great British pound and South African rand. We generally do not hedge our net investment or translation exposure since we view our operations as long-term investments and believe the costs of hedging would outweigh the benefits.

Since December 31, 1998, we have formally reported our accident and health division as a discontinued operation. The accident and health business was placed into run-off, and all treaties were

terminated at the earliest possible date. Notice was given to all cedants and retrocessionaires that all treaties were being cancelled at the expiration of their terms. The nature of the underlying risks is such that the claims may take several years to reach the reinsurers involved. Thus, we expect to pay claims over a number of years as the level of business diminishes. We will report a loss to the extent claims and related expenses exceed established reserves. During 2003, the accident and health division reported a net loss of \$5.7 million due to claim payments in excess of established reserves and legal fees. See Note 21 to the Consolidated Financial Statements.

Prior to January 1, 2003, the Company aggregated the results of its five main operational segments into three reportable segments: U.S., Canada and Other International. The Other International reportable segment formerly included operations in Latin America, Asia Pacific, and Europe & South Africa. Effective January 1, 2003, as a result of our declining presence in Argentina and changes in management responsibilities for part of the Latin America region, the Other International reportable segment no longer included Latin America operations. Latin America results relating to the Argentine privatized pension business as well as direct insurance operations in Argentina are now reported in the Corporate and Other segment. The results for all other Latin America business, primarily traditional reinsurance business in Mexico, are reported as part of U.S. operations in the Traditional sub-segment. Additionally, the remaining operations of the Other International reportable segment, Asia Pacific and Europe & South Africa, are now presented as separate reportable segments. Prior-period segment information has been reclassified to conform to this new presentation.

The U.S. operations provide traditional life, asset-intensive, and financial reinsurance primarily to domestic clients. The Canada operations provide insurers with reinsurance of traditional life products as well as reinsurance of critical illness products. Asia Pacific operations provide primarily traditional life reinsurance and, to a lesser extent, financial reinsurance. Europe & South Africa operations include traditional life reinsurance and critical illness business from Europe and South Africa, in addition to other markets we are developing. Our discontinued accident and health business is excluded from continuing operations. We measure segment performance based on profit or loss from operations before income taxes.

Consolidated income from continuing operations increased 38.8% in 2003 to \$178.3 million and increased 222.1% in 2002 to \$128.5 million. Diluted earnings per share from continuing operations were \$3.46 for 2003 compared to \$2.59 for 2002 and \$0.80 for 2001. A majority of our earnings during these years were attributed primarily to traditional reinsurance results in the U.S. and Canada. Mortality experience during 2003 and 2002 was generally within our range of expectations. Additionally, 2003 net income for our U.S. Traditional operations benefited from the Allianz Life transaction by approximately \$6.8 million. We expect that transaction to contribute \$30 to \$40 million to net income