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Questioning Market Leaders For Long Term Investors

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COMPANY INTERVIEW

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Max Capital Group Ltd. (MXGL)



JOE ROBERTS serves as Executive Vice President and Chief Financial Officer of Max Capital Group Ltd. From 2001 until early 2002, Mr. Roberts served as Vice President in Finite Underwriting for Overseas Partners Re Ltd., a Bermuda-based reinsurance company specializing in providing quality reinsurance solutions for its business partners. He worked in public accounting in Bermuda from 1994 through 2001 with KPMG, with a specialization in providing assurance based services to the financial services sector. Mr. Roberts served as Senior Manager with KPMG from 1998. From 1987 to 1994, he worked in public accounting in London, primarily with Moore Stephens. Mr. Roberts is a member of the Institute of Chartered Accountants in England and Wales.

SECTOR – NON-LIFE INSURANCE

(AGU608) TWST: We'd like to begin with a brief historical sketch of Max Capital and a picture of the things you're doing right now.

Mr. Roberts: Our company changed its name recently from Max Re Capital Ltd. to Max Capital Group Ltd. to more accurately reflect the insurance markets in which we do business. We underwrite property and casualty insurance and reinsurance and also write some life reinsurance business. When we started out in 2000, we were a reinsurance company focused on larger transactions and expected to write only a few contracts in each period. Over the intervening years, we have transitioned to a more global and diverse insurance operation that writes a larger number of smaller transactions and we now write a more traditional book of business compared to what many would have called a finite or alternative risk type of business in the early days.

The insurance industry is very cyclical and we have had some significant changes over the six

or seven years we have been in operation. We started as an alternative risk business, taking smaller amounts of underwriting risk compared to a traditional insurance company and coupled that with a slightly more aggressive asset strategy than was typical of our competitors. Following September 11, 2001, the insurance market changed. The opportunities in the traditional property and casualty markets increased, and, as we have always been a company that embraces the concept of flexibility in response to changing market conditions and looks to produce a consistent ROE for our shareholders, we expanded our operations. We developed our traditional reinsurance business in 2002, and entered the traditional insurance business in 2003, and we have expanded those lines over the past five years.

TWST: What else differentiates you from your competition?

Mr. Roberts: Our competition is here in Bermuda, in the United States and globally within the insurance business. In Bermuda, a

number of our competitors focus more on shorter-tail lines, such as property and property catastrophe insurance and reinsurance. We also write these lines, but they form a smaller part of our total book, as we also write a significant volume of casualty business. In fact, casualty business now makes up approximately two-thirds of our business platform and the typically longer tail of that business can be expected to enhance our cash flows, allowing us to utilize a different and, we believe, a potentially more beneficial investment strategy than the strategies used by most of our competitors. By way of explanation, when claims related to a particular class of insurance business are typically paid out during or shortly after the policy period, that business is described as having a “short tail.” Conversely, when claims related to a particular class of insurance business are typically paid out long after the expiration of the policy period, that business is described as having a “long tail.”

“Casualty business now makes up approximately two-thirds of our business platform and the typically longer tail of that business can be expected to enhance our cash flows, allowing us to utilize a different and, we believe, a potentially more beneficial investment strategy than the strategies used by most of our competitors.”

TWST: I understand that there are significant advantages for a company like yours in working from Bermuda.

Mr. Roberts: We are fortunate in Bermuda to have a very good regulatory department in the Bermuda Monetary Authority, which understands the need to develop good practice in a timely manner. It has helped Bermuda to be a jurisdiction that permits companies to set up relatively quickly and

efficiently within a well-regulated environment. Local regulations permit capital to locate here in Bermuda, allowing companies to conduct good business practices across the globe while potentially benefiting from Bermuda’s tax-free environment. As a predominantly long-tail casualty writer, we generate significant investment income over the life of the business written, more so than a short-tail property catastrophe writer, where the duration of business written is shorter. Therefore the investment and tax environment in Bermuda is important to our success.

TWST: You said that the industry is cyclical. What is the next cycle? What are the opportunities that lie before you?

Mr. Roberts: We have had very solid underwriting conditions for the last four to five years. Rates, terms and conditions have been generally good, but the insurance marketplace is presently softening and opportunities are generally less attractive than they have been over the past few years. This means companies are typically working harder to make their premium dollars. In addition, companies must manage their expenses carefully and work to maximize their investment returns. As top-line premium income shrinks, it is important to manage some other areas of the business more closely.

I think there will be some merger or acquisition activity in the marketplace. We have had a solid period of good business for the insurance industry. I believe that balance sheets are certainly stronger than they were in the late 1990s and early 2000s. So we have a number of companies with strong balance sheets and good platforms and we may see some of those companies join together for strategic or operational reasons.

TWST: What are the key elements in your strategic agenda as you look out over the next three years?

Mr. Roberts: The key for us is the continued execution of our business plan. That sounds simple, but it remains the principal driver of our success. We have good systems in place at Max, we have a diverse platform, and we have some very talented underwriting groups. The key for us is to play to these strengths and to continue to do what we've been doing well. In the past four or five years, we've been more of a traditional insurance and reinsurance player. We have had solid ROEs — in excess of 15% in three of the past four years. The year that we didn't have 15% — 2005 — was the year of hurricanes Katrina, Rita and Wilma. Even in that year we turned a profit, when a large number of insurance companies didn't. So our strategy is to continue to execute and serve our clients well. That will help book value grow, which is a fundamental metric for our company.

TWST: What about possible problems? What are you going to be worrying about?

Mr. Roberts: One of the biggest concerns is excess capacity in the marketplace, with more competition for each premium dollar. So it is incumbent upon Max to ensure we are a market of choice by providing excellent service, putting good opportunities in front of potential and existing clients, and using our infrastructure and broker community connections to deliver not only top-line premium, but, more important, bottom-line net income. Top-line premium is not the driver of everything for us — we don't intend to chase top-line premium as aggressively as some of our competitors are likely to. We believe our investment strategy should enable us to return a solid ROE without us having to compromise our underwriting standards as the market softens. Equally, we want to maintain our place in the market and the good relationships that we have established since we commenced operations in 2000.

TWST: Would you go back to September 11 and explain the effects on your company? I think you came out of that pretty well.

Mr. Roberts: That's correct. We did not have a significant amount of exposure to the World Trade Center events and had manageable exposure to the hurricanes of 2004 and 2005. Although we did suffer some losses, we didn't lose more than our net income for either year, so our viability wasn't impacted and we were in the right position to continue business as the market hardened. Generally, after significant loss events, there is a drawdown on the capital base within the industry. Premium rates then rise and coverage becomes more expensive for clients, insurers and reinsurers purchasing protection. When rates harden, however, new capital is attracted by the potentially enhanced returns. This was certainly the case after September 11, when we saw a number of new entrants in Bermuda that planned to take advantage of the market opportunities.

“With our recent move into the United States, we expect that segment to be our fastest growing. We expect it to bring significant premium growth for us over the next few years. Even though the market is softening, the premium written will be additive to Max, as this is a new market for us.”

TWST: I believe that Max works from Ireland as well as Bermuda. Would you explain what you do from Ireland and the advantages of Ireland?

Mr. Roberts: We operate now from three places. Bermuda was our original location, and we set up a reinsurance operation in Dublin, Ireland, in 2001. We complemented that with an insurance operation in 2003 in both Bermuda and Dublin.

Dublin is an excellent place to do business, with a solid infrastructure and access to the European market, which we deem to be important. The Dublin office offers products that complement the products that we offer here in Bermuda, and Ireland is also a well-regulated, tax-efficient operating jurisdiction. More recently, we've extended our operations into the United States. We acquired a non-admitted excess and surplus company in April of this year. We expect to continue to grow that platform through the coming years.

TWST: What are your feelings about acquisitions? What are your criteria for possible acquisitions?

Mr. Roberts: I think the key criteria are whether it brings shareholder value and whether it will align with or augment our current strategy and operations. From a company perspective, we like our platform — we believe it's diverse through the products offered and geographical regions covered, and is well managed. We have some excellent underwriting talent at Max, and so don't believe we need to look actively for acquisition or merger targets. Equally, there is a lot of talk in the industry about consolidation and combining businesses in differing markets and geographical locations. We would certainly look at any opportunity to increase shareholder value.

TWST: What would you reasonably expect the company to look like in about three years?

Mr. Roberts: With our recent move into the United States, we expect that segment to be our fastest growing. We expect it to bring significant premium growth for us over the next few years. Even though the market is softening, the premium written will be additive to Max, as this is a new market for us. We see the products offered by our US company to also be complementary to the products that we offer here in Bermuda and in

Ireland. Most of our focus in the next couple of years will be the execution of our plan to develop our US operations.

TWST: For the benefit of the potential investor, what might be some year-over-year milestones to look for?

Mr. Roberts: The one we always like to look at is our ROE. It's key for every company. We don't necessarily expect to produce the highest ROE on the Street when the market is favorable. Equally, we don't expect to be the lowest in bad times. We like to have a nice balance between taking risk and showing solid returns. The secondary metric to look at is our combined ratios, which are the sums of our loss ratios and our expense ratios for each segment of our business. These are an indication of the success of our underwriting activities.

TWST: Would you tell us about the backgrounds and the expertise of yourself and a couple of your colleagues?

Mr. Roberts: At Max, we have a number of very talented individuals heading up our insurance and reinsurance businesses. Our strategy has been to find individuals who we consider to be some of the best in class — people who are seasoned underwriters, have very good relationships with clients and who can bring a substantial book of business with them and who have the talent to lead and develop that niche franchise that we are looking for in the specialty markets that we operate in.

Our CEO is Marty Becker. Marty has actually been on the Board since 2004, and, in October of last year, he took over on the departure of Bob Cooney, who was instrumental in setting the company up. Marty has excellent experience in building companies and we have already benefited significantly from his expertise. He has great rela-

tionships in the investor community and in the broker and market environment, and will take the platform forward from the excellent start that Bob gave us.

I have recently taken over from Keith Hynes as Chief Financial Officer. My background is mostly in public practice, where I worked with public accounting firms in both London and in Bermuda before joining Max Capital in 2002 in the role of Controller.

Our Chief Operating Officer is Peter Minton, who recently changed his role from being our Chief Risk Officer. Peter has a strong investment and underwriting background, which aids us in allocating our resources into the appropriate areas, as we see opportunities arise in the marketplace.

Angelo Guagliano is the Chief Executive Officer of Max Bermuda Ltd., our principal operating subsidiary. Angelo has been underwriting for more than 25 years and was formerly with XL Capital, where he worked with Bob Cooney. Angelo joined us in 2003 to head up our insurance operations.

John Doucette heads up our reinsurance business, which operates principally from Bermuda. John has been with Max since we commenced operations in 2000. Prior to Max, John spent a number of years at Swiss Re and started his career with Tillinghast. John has successfully developed our reinsurance team into one with strong underwriting talent, a good track record and an excellent reputation. In fact, in a recent survey, Max Bermuda was ranked fifth behind Munich Re, Swiss Re, Scor and RenRe as the “Treaty Reinsurer currently leading the industry in terms of its overall proposition” (*Global Broker* – July/August 2007).

John Boylan heads up our Dublin insurance operations. Since John joined the group in

2003, he has developed our Dublin operations and produced an excellent book of business. John was previously with XL Capital in Dublin.

Our recent entry into the United States is headed up by Steve Vaccaro. Steve and his team are the newest additions to the Max group. Steve was previously with the Markel Group. He has been in this industry for more than 30 years, underwriting business in both hard and soft markets, and had an excellent track record with Markel. We are hoping that he can replicate that success with Max.

TWST: As CFO, what occupies your own attention most on a day-to-day basis?

Mr. Roberts: It’s a combination of several things. The investor community and spending time with them is critical to our organization, as it is to any public company. On the operational side of the business, there are many challenges in managing the finances of a growing company, ranging from capital management to cash and investment activity. In addition, as a public company, we have significant regulatory requirements in the multiple jurisdictions in which we operate and detailed financial reporting requirements. Our goal in the finance department is to provide underwriters with the capital and the platform necessary to succeed.

TWST: What would be the two or three best reasons for the long-term investor to take a good look at Max Capital Group?

Mr. Roberts: Our platform is excellent. We have a very strong management team across the group, and the underwriting businesses we operate are well executed. We’ve shown that we can operate successfully in this market. We’ve turned a profit in each of the past four years, even in 2005, which was a particularly difficult year for the market. It’s important for customers and investors to know that we intend to be around not only this year, but for the foreseeable future to

continue to execute our plan and to deliver increases in book value and share price to our investors. That's the number-one goal for us, from an investment standpoint.

The secondary reason is that we believe we are undervalued compared to our peers. If you look at some other insurance, reinsurance or specialty insurance companies, we are relatively underpriced. Look at our track record over the past four years, our excellent platform, our development into the United States and our other operations that we believe will permit us to continue that success. We have a disciplined approach to taking risk and have a solid track record. For all these reasons, as I have said, we believe we are underpriced relative to our peers.

TWST: You said that 2005 was a difficult year. What was the problem?

Mr. Roberts: We had three of the largest hurricanes on record — Katrina, Rita and Wilma — all leading to unprecedented industry losses. A significant amount of capital moved out of the insurance industry to settle claims. Unfortunately, a number of the models used to assess property catastrophe risk failed to predict the impact of three such severe storms and a number of companies were forced out of business or suffered crippling losses. As a result of Max's risk management process and the way we purchase reinsurance protection, however, we managed to limit our downside more successfully than many other companies in the marketplace. We believe that speaks volumes to the way we do business — in a measured and controlled way. That's what people want to see — that we will be there to continue that good work going forward.

TWST: Do you feel that your own company and industry are better prepared for cataclysmic events than they were in the past?

Mr. Roberts: I believe they are. As an industry we are getting back to a state of good capitalization and we learned a lot of lessons collectively on the property side from those storms. The models being used today are more detailed. We're looking at different methods of getting better-quality data to allow a better assessment of the severity of loss events than was possible in the past. We should be better prepared for the next set of significant storms or natural catastrophes as and when they occur.

TWST: Have you taken steps to improve your capital structure?

Mr. Roberts: The industry generally has. The rating agencies and company managements recognized that there were a number of companies that were off target in estimating the severity of the 2005 storms. The rating agencies now look for more capital on the balance sheet to write those types of business. It is difficult to go to shareholders when you have significantly underestimated your exposure to certain events.

Max didn't have as big an issue for several reasons. Firstly, we have used different approaches to look at our exposure, plus we have always planned to limit our downside to the percentage of our total capital that we are willing to expose in that particular type of market. We do write a lot of casualty business, and that represents 60% to 65% of our business. Property is less of a play for us, and, consequently, we wouldn't expect to get the extreme high or low returns that could be the result of writing a predominance of that business in our company. We would like to have a platform for future business, and that's why we choose to do it this way.

TWST: Is there anything that you would like to add, especially regarding strategies, long-term objectives and reasons for investors to look at the company?

Mr. Roberts: Long-term growth and success are key, but they shouldn't come at the cost of compromised short-term execution. We need to execute our plan, deliver the ROEs that we said we could achieve, and manage our company so that we are around in the future. So, if we can execute those objectives, manage the company properly, be disciplined in the tougher market conditions, and look for strategic opportunities, we should be successful. We've done that in the past, and believe we can achieve that in the future.

TWST: Thank you. (MC)

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