We are pleased to report exceptional results for 1988. Total operating revenues increased by 78%, to $69.5 million. Net income was up 68%, to $11.1 million, and net income per share was up 54%, to $2.80. These results represent a return on average shareholders' equity of 31%, once again exceeding our long-term goal of earning 20% on equity. Markel's strategy of diversifying into different segments of the insurance industry (brokerage, claims and underwriting) and specializing in unique product niches has again proven to be successful.

Our brokerage operations had good results with total revenues increasing by 8%, though growth in this area was limited by the soft insurance market. Transportation and animal mortality revenues were down due to severe price competition. However, revenue from all other product lines increased. Our strategy of diversification and specialization minimized the effects of the prevailing soft market. Additionally, the Law Enforcement Liability book of business acquired from Special Risks, Inc. in October 1988, contributed to fourth quarter results. With this acquisition, along with further market penetration in other product lines, we expect 1989 to be an even stronger year for the brokerage operations.

The claims operations reported revenues of $29.8 million, up from $11.3 million last year, largely as the result of our acquisition of Lindsey & Newsom in late 1987. During 1988, we made a great deal of progress in consolidating the operations of Lindsey & Newsom, National Claims, and Gordon Boyd. Effective January 1, 1989, these companies were merged into one organization under the name Lindsey & Newsom Claim Services. Through several acquisitions and internal expansion the claims operation moved into 6 new states with 18 additional offices during 1988. Lindsey and Newsom now operates in 30 states through 130 offices. While we have made significant strides in developing a strong, quality, full-service claims operation, much remains to be done. The profit margins in this area have been impacted by the costs associated with the amalgamation and expansion program. However, we remain very optimistic about the future of Lindsey & Newsom and the claims business.

The insurance underwriting operations have continued to provide both growth and profits for the Corporation. Earned premiums increased 48%, largely due to expansion into additional states and the appointment of new agents. The combined loss and expense ratio was 84%, which was significantly better than our goal and the majority of the insurance industry. We have always tried to be very conservative in establishing our estimates for loss reserves. This strategy proved beneficial in 1988, as reserves set in prior years have proven to be redundant. Without the benefit of this redundancy our combined loss and expense ratio would have been 95%, which is still quite good and well within our objectives. We believe the reserves established at year-end 1988, are conservative, though any future benefits are difficult to predict. The insurance market continues to be very competitive and while we expect to see continued growth (albeit more slowly) and profitability, we do anticipate smaller margins as the combined ratio is likely to increase. Our goal of earning underwriting profits remains intact.

Our equity investments contributed $6.0 million to the Corporation in 1988, as compared to $1.6 million the previous year. This increase was the single most significant reason for our increased net income and is primarily due to the acquisition of the Shand/Evanston Group in December 1987. The Shand/Evanston Group maintained its underwriting disciplines and price levels, producing results which exceeded our expectations. Because the markets in which Shand/Evanston competes were impacted by the soft insurance market, earned premiums declined by 42%, to $61.5 million as compared to $105.4 million in 1987. More importantly, the combined loss and expense ratio improved from 109% in 1987, to 105% in 1988. Our objective is to earn underwriting profits and, while this will be difficult to achieve with declining premium volume, we remain committed to this goal.

Fairfax Financial once again enjoyed a successful year. Nineteen eighty-eight results were favorably affected by its investment in the Shand/Evanston Group, which more than offset several somewhat unusual items which affected 1987 results. The Canadian insurance industry, and thus the insurance operations of Fairfax, is experiencing the same competitive environment as in the United States. The claims adjusting business is not impacted by the soft cycle, allowing Fairfax's Morden & Helwig to prosper regardless of the cycle. Additionally, Fairfax has expanded its investment banking activities and completed several transactions during the year. In December 1988, we converted our convertible preferred stock into common stock. As a result, Markel Corporation's equity in Fairfax's earnings will be increased from 17% to 23% in 1989. Prospects for continued growth and profitability from this affiliate are favorable.

In June 1988, we completed the sale of an additional 650,000 shares of stock at $16.25 per share. The net proceeds of this offering were $9.6 million, which were used primarily to increase our investment in the Shand/Evanston Group. A successful offering is not possible without the investment community, and their support is appreciated. While we were reluctant to sell additional shares at a relatively low price/earnings multiple, we had an opportunity to invest the proceeds in our business at rates of return which would not cause dilution to existing shareholders. The additional capital also strengthened our balance sheet.

During the year we renegotiated our revolving credit and term loan agreement, and increased our borrowing under this facility to $15 million. We believe the interest rates and repayment terms of this facility are quite competitive and very manageable, and we are not uncomfortable with this level of debt.

Shareholders' equity, including redeemable common stock, at year end was $49.8 million, or $11.44 per share. This compares to $21.6 million, or $6.00 per share, at December 31, 1987.

In 1988, we achieved unusually good results by almost any measure. As previously stated, revenues were up 78%, net income per share was up 54%, and return on average shareholders' equity was 31%. Not only are these exceptional results, but they were accomplished in a very competitive, soft insurance cycle. We expect the insurance market to remain soft in 1989, and probably beyond. As our 1988 results were favorably affected by acquisitions completed in late 1987, we do not expect our 1989 revenue growth or net income growth to match 1988 levels. We are confident, however, that by adhering to our strategy of diversification into different segments of the insurance industry and specialization in unique product lines, we can achieve our long-term goals of increasing revenues by 20% annually and earning a 20% return on equity.

While we have grown very quickly in the past few years, we are still a relatively small company in the insurance industry. We view this as an advantage, and while we expect to continue to grow, we will seek to maintain our strategy of decentralization, allowing the key people in each of the business units to respond quickly and intelligently to opportunities in their respective market segments.

The insurance industry will continue to be cyclical and the current soft market is likely to continue for some time. However, the industry is quite large (over $200 billion in premiums) and regardless of the cycle, there will be opportunities for those who can take advantage of them. We have a group of very talented individuals capable of delivering customized products, superior customer service, and immediate response to the changing needs of our customers.

The insurance cycle has very little impact on the claims administration business, which generally responds to overall economic activity. Any occasional peaks and valleys are the result of unusual weather patterns. We now have the opportunity to develop a large, international claims organization in an industry characterized by small, local operations. The opportunity for profitable growth is very exciting and we will maintain a long-term focus on building a strong, quality claims operation.

Markel Corporation looks toward the future with optimism. In spite of the very competitive, soft market environment, we believe many opportunities for continued growth and development exist. The past few years have been marked by record financial results and we remain committed to our goal of sustaining this performance over the long term.

Our accomplishments are made possible only through the support of our customers, agents, suppliers, shareholders, and, most importantly, our people. It is our people who make the difference and deserve the credit. Their commitment is evidenced by participation, enthusiasm, and the fact that so many have chosen to share in the company's future through stock ownership. The men and women of the Markel Companies have made us successful for the past 60 years and they continue to put forth exceptional effort. Our people ***ARE*** Markel, and together we are committed to success.

Alan I. Kirshner
President and
Chairman of the Board

Anthony F. Markel
Executive
Vice President

Steven A. Markel
Executive
Vice President

The Markel way is to seek to be a market leader in each of our pursuits. We seek to know our customers' needs and to provide our customers with quality products and service.