GENCO SHIPPING & TRADING LTD
Form 10-Q
May 10, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2007

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ________________________ to ________________________

Commission file number **000-51442**

GENCO SHIPPING & TRADING LIMITED
(Exact name of registrant as specified in its charter)

Republic of the Marshall Islands	**98-043-9758**
(State or other jurisdiction incorporation or organization)	(I.R.S. Employer Identification No.)

299 Park Avenue, 20th Floor, New York, New York 10171
(Address of principal executive offices) (Zip Code)

(646) 443-8550
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities and Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes __X__ No ____

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer r Accelerated filer ý Non-accelerated filer r

Indicate by checkmark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ______ No __X__

APPLICABLE ONLY TO CORPORATE ISSUERS:

The number of shares outstanding of each of the issuer’s classes of common stock, as of May 10, 2007:
Common stock, $0.01 per share 25,518,475 shares.

Genco Shipping & Trading Limited
Form 10-Q for the three months ended March 31, 2007 and 2006

Genco Shipping & Trading Limited
Consolidated Balance Sheets as of March 31, 2007
and December 31, 2006
(U.S. Dollars in thousands, except for share data)

	March 31, 2007	December 31, 2006
Assets		
Current assets:		
Cash and cash equivalents	$ 87,158	$ 73,554
Vessel held for sale	-	9,450
Due from charterers, net	985	471
Prepaid expenses and other current assets	6,175	4,643
Total current assets	94,318	88,118
Noncurrent assets:		
Vessels, net of accumulated depreciation of $50,680 and $43,769, respectively	469,872	476,782
Deferred drydock, net of accumulated depreciation of $549 and $366, respectively	3,173	2,452
Other assets, net of accumulated amortization of $563 and $468, respectively	4,019	4,571
Fixed assets, net of accumulated depreciation and amortization of $439 and $348, respectively	1,987	1,877
Fair value of derivative instrument	3,973	4,462
Total noncurrent assets	483,024	490,144
Total assets	$ 577,342	$ 578,262
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued expenses	$ 8,557	$ 7,784
Current portion of long-term debt	-	4,322
Deferred revenue	3,947	3,067
Total current liabilities	12,504	15,173
Noncurrent liabilities:		
Deferred revenue	434	395
Deferred rent credit	739	743
Fair value of derivative instruments	1,265	807
Long-term debt	206,233	207,611
Total noncurrent liabilities	208,671	209,556
Total liabilities	221,175	224,729
Commitments and contingencies		
Shareholders' equity:		
Common stock, par value $0.01; 100,000,000 shares authorized; issued and outstanding 25,518,475 and 25,505,462 shares at March 31, 2007 and December 31, 2006, respectively	255	255

Paid-in capital		307,674		307,088
Accumulated other comprehensive income		2,599		3,546
Retained earnings		45,639		42,644
Total shareholders’ equity		356,167		353,533
Total liabilities and shareholders’ equity	$	577,342	$	578,262

See accompanying notes to consolidated financial statements.

Genco Shipping & Trading Limited
Consolidated Statements of Operations for the Three Ended March 31, 2007 and 2006
(U.S. Dollars in Thousands, Except for Earnings per Share and Share Data)
(Unaudited)

	For the Three Months Ended March 31, 2007	For the Three Months Ended March 31, 2006
Revenues	$ 37,220	$ 32,572
Operating expenses:		
Voyage expenses	1,413	1,104
Vessel operating expenses	6,389	4,559
General and administrative expenses	3,195	2,449
Management fees	351	347
Depreciation and amortization	7,186	6,417
Gain on sale of vessel	(3,575)	-
Total operating expenses	14,959	14,876
Operating income	22,261	17,696
Other (expense) income:		
Income from derivative instruments	-	476
Interest income	1,066	569
Interest expense	(3,490)	(2,163)
Other (expense) income	(2,424)	(1,118)
Net income	$ 19,837	$ 16,578
Earnings per share-basic	$ 0.78	$ 0.66
Earnings per share-diluted	$ 0.78	$ 0.66
Weighted average common shares outstanding-basic	25,308,953	25,260,000
Weighted average common shares outstanding-diluted	25,421,480	25,304,448

See accompanying notes to consolidated financial statements.

Genco Shipping & Trading Limited
Consolidated Statement of Shareholders' Equity (Unaudited)
For the Three Months Ended March 31, 2007
(U.S. Dollars in Thousands Except for Per Share and Share Data)

	Common Stock	Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Comprehensive Income	Total
Balance – January 1, 2007	$ 255	$ 307,088	$ 42,644	$ 3,546		$ 353,533
Net income			19,837		$ 19,837	19,837
Unrealized derivative (loss) on cash flow hedges				(947)	(947)	(947)
Comprehensive income					$ 18,890	
Cash dividends paid ($0.66 per share)			(16,842)			(16,842)
Issuance of 16,200 shares of nonvested stock, less forfeitures of 3,187 shares	-	-				-
Nonvested stock amortization		586				586
Balance – March 31, 2007	$ 255	$ 307,674	$ 45,639	$ 2,599		$ 356,167

See accompanying notes to consolidated financial statements.

Genco Shipping & Trading Limited
Consolidated Statement of Cash Flows for the Three Months Ended March 31, 2007 and 2006
(U.S. Dollars in Thousands)
(Unaudited)

	For the Three Months Ended March 31, 2007	2006
Cash flows from operating activities:		
Net income	$ 19,837	$ 16,578
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	7,186	6,417
Amortization of deferred financing costs	96	74
Amortization of value of time charter acquired	456	456
Unrealized gain on derivative instruments	-	(476)
Amortization of nonvested stock compensation expense	586	519
Gain on sale of vessel	(3,575)	-
Change in assets and liabilities:		
Increase in due from charterers	(513)	(87)
(Increase) decrease in prepaid expenses and other current assets	(1,512)	130
Increase in accounts payable and accrued expenses	715	273
Increase in deferred revenue	919	210
(Decrease) increase in deferred rent credit	(5)	117
Deferred drydock costs incurred	(861)	(299)
Net cash provided by operating activities	23,329	23,912
Cash flows from investing activities:		
Purchase of vessels, net of deposits	(43)	(23)
Proceeds from sale of vessel	13,004	-
Purchase of other fixed assets	(144)	(619)
Net cash provided by (used in) investing activities	12,817	(642)
Cash flows from financing activities:		
Repayment of credit facilities	(5,700)	-
Cash dividends paid	(16,842)	(15,261)
Payment of deferred financing costs	-	(27)
Net cash used in financing activities	(22,542)	(15,288)
Net increase in cash	13,604	7,982
Cash and cash equivalents at beginning of period	73,554	46,912
Cash and cash equivalents at end of period	$ 87,158	$ 54,894

Supplemental disclosure of cash flow information:

Cash paid during the period for interest	$	2,675	$	2,225

See accompanying notes to consolidated financial statements.

Genco Shipping & Trading Limited
(U.S. Dollars in Thousands Except Per Share and Share Data)

Notes to Consolidated Financial Statements for the Three Months Ended March 31, 2007 and 2006 (unaudited)

1 - GENERAL INFORMATION

The accompanying consolidated financial statements include the accounts of Genco Shipping & Trading Limited ("GS&T") and its wholly owned subsidiaries (collectively, the "Company," "we" or "us"). The Company is engaged in the ocean transportation of drybulk cargoes worldwide through the ownership and operation of drybulk carrier vessels. GS&T was incorporated on September 27, 2004 under the laws of the Marshall Islands and is the sole owner of all of the outstanding shares of the following subsidiaries: Genco Ship Management LLC; and the ship-owning subsidiaries as set forth below.

The Company began operations on December 6, 2004 with the delivery of its first vessel. The Company agreed to acquire a fleet of 16 drybulk carriers from an unaffiliated third party on November 19, 2004; these vessels were delivered during 2004 and 2005.

Additionally, on October 14, 2005, the Company acquired the Genco Muse with an existing time charter for $34,450, which was funded entirely by the Company's new credit facility entered into on July 29, 2005 (the "New Credit Facility"). The portion of the purchase price attributable to the vessel was $30,958 (see Note 4). On July 10, 2006, the Company acquired the Genco Acheron, the Genco Commander, and the Genco Surprise for a total purchase price of $81,250, all of which were delivered in the fourth quarter of 2006. During February 2007, the Company completed the sale of the Genco Glory to Cloud Maritime S.A. for $13,004, net of commission. Below is the list of the Company's wholly owned ship-owning subsidiaries as of March 31, 2007:

Wholly Owned Subsidiaries	Vessels Acquired	dwt	Date Delivered	Year Built	Date Sold
Genco Reliance Limited…………………	Genco Reliance	29,952	12/6/04	1999	—
Genco Glory Limited…………………	Genco Glory	41,061	12/8/04	1984	2/21/07
Genco Vigour Limited…………………	Genco Vigour	73,941	12/15/04	1999	—
Genco Explorer Limited…………………	Genco Explorer	29,952	12/17/04	1999	—
Genco Carrier Limited…………………	Genco Carrier	47,180	12/28/04	1998	—
Genco Sugar Limited…………………	Genco Sugar	29,952	12/30/04	1998	—
Genco Pioneer Limited…………………	Genco Pioneer	29,952	1/4/05	1999	—

Genco Progress Limited…………………	Genco Progress	29,952	1/12/05	1999	—
Genco Wisdom Limited…………………	Genco Wisdom	47,180	1/13/05	1997	—
Genco Success Limited…………………	Genco Success	47,186	1/31/05	1997	—
Genco Beauty Limited…………………	Genco Beauty	73,941	2/7/05	1999	—
Genco Knight Limited…………………	Genco Knight	73,941	2/16/05	1999	—
Genco Leader Limited…………………	Genco Leader	73,941	2/16/05	1999	—
Genco Marine Limited…………………	Genco Marine	45,222	3/29/05	1996	—
Genco Prosperity Limited…………………	Genco Prosperity	47,180	4/4/05	1997	—
Genco Trader Limited	Genco Trader	69,338	6/7/05	1990	—
Genco Muse Limited …………………	Genco Muse	48,913	10/14/05	2001	—
Genco Commander Limited …………	Genco Commander	45,518	11/2/06	1994	—
Genco Acheron Limited ……………..	Genco Acheron	72,495	11/7/06	1999	—
Genco Surprise Limited ……………..	Genco Surprise	72,495	11/17/06	1998	—

Prior to its initial public offering, GS&T was 100% owned by Fleet Acquisition LLC, a limited liability company organized on November 3, 2004 under the laws of the Marshall Islands. Fleet Acquisition LLC was owned approximately 65.65% by OCM Principal Opportunities III Fund, L.P. and OCM Principal Opportunities Fund IIIA, L.P., collectively, ("Oaktree") of which Oaktree Management LLC is the General Partner, approximately 26.57% by Peter Georgiopoulos, and 7.78% by others. As of December 31, 2005, Fleet Acquisition LLC maintained a 53.08% ownership in the Company. On April 14, 2006, Fleet Acquisition LLC distributed 1,050,210 shares to certain of its members, and on December 15, 2006, Fleet Acquisition LLC distributed 3,587,361 shares to

Peter Georgiopoulos, our Chairman. As a result, at December 31, 2006, Oaktree beneficially owned approximately 34.75% of the Company through Fleet Acquisition, LLC and Peter Georgiopoulos beneficially owned approximately 14.07%. In January 2007, we filed a registration statement on Form S-3 with the Securities and Exchange Commission (the "SEC") to register possible future offerings, including possible resales by Fleet Acquisition LLC. That registration statement, as amended, was declared effective by the SEC on February 7, 2007. Fleet Acquisition LLC utilized that registration statement to conduct an underwritten offering of 4,830,000 shares it owned, including an over-allotment option granted to underwriters for 630,000 shares which the underwriters exercised in full. Following completion of that offering, Fleet Acquisition LLC owns 15.80% of our common stock.

2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"), which include the accounts of Genco Shipping & Trading Limited and its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and, therefore, do not include all information and footnotes necessary for a fair presentation of financial position, results of operations and cash flows in conformity with accounting principles generally accepted in the United States of America. However, in the opinion of the management of the Company, all adjustments necessary for a fair presentation of financial position and operating results have been included in the statements. Interim results are not necessarily indicative of results for a full year. Reference is made to the December 31, 2006 consolidated financial statements of Genco Shipping & Trading Ltd. contained in its Annual Report on Form 10-K for the year ended December 31, 2006.

Business geographics

The Company's vessels regularly move between countries in international waters, over hundreds of trade routes and, as a result, the disclosure of geographic information is impracticable.

Vessel acquisitions

When the Company enters into an acquisition transaction, it determines whether the acquisition transaction was the purchase of an asset or a business based on the facts and circumstances of the transaction. As is customary in the shipping industry, the purchase of a vessel is normally treated as a purchase of an asset as the historical operating data for the vessel is not reviewed nor is material to our decision to make such acquisition.

When a vessel is acquired with an existing time charter, the Company allocates the purchase price of the vessel and the time charter based on, among other things, vessel market valuations and the present value (using an interest rate which reflects the risks associated with the acquired charters) of the difference between (i) the contractual amounts to be paid pursuant to the charter terms and (ii) management's estimate of the fair market charter rate, measured over a period equal to the remaining term of the charter. The capitalized above-market (assets) and below-market (liabilities) charters are amortized as a reduction or increase, respectively, to voyage revenues over the remaining term of the charter.

Segment reporting

The Company reports financial information and evaluates its operations by charter revenues and not by the length of ship employment for its customers, i.e., spot or time charters. The Company does not use discrete financial information to evaluate the operating results for different types of charters. Although revenue can be identified for these types of charters, management cannot and does not separately identify expenses, profitability or other financial information for these charters. As a result, management, including the chief operating decision maker, reviews operating results solely by revenue per day and operating results of the fleet and thus, the Company has determined that it operates under one reportable segment. Furthermore, when the Company charters a vessel to a charterer, the charterer is free to trade the vessel worldwide and, as a result, the disclosure of geographic information is impracticable.

Revenue and voyage expense recognition

Since the Company's inception, revenues have been generated from time charter agreements and pool agreements. A time charter involves placing a vessel at the charterer's disposal for a set period of time during which the charterer may use the vessel in return for the payment by the charterer of a specified daily hire rate. In time charters, operating costs including crews, maintenance and insurance are typically paid by the owner of the vessel and specified voyage costs such as fuel and port charges are paid by the charterer. There are certain other non-specified voyage expenses such as commissions which are borne by the Company.

The Company records time charter revenues over the term of the charter as service is provided. Revenues are recognized on a straight-line basis as the average revenue over the term of the respective time charter agreement. The Company recognizes vessel operating expenses when incurred.

In December 2005 and February 2006, respectively, the Genco Trader and the Genco Leader entered into the Baumarine Panamax Pool. Vessel pools, such as the Baumarine Panamax Pool, provide cost-effective commercial management activities for a group of similar class vessels. The pool arrangement provides the benefits of a large-scale operation, and chartering efficiencies that might not be available to smaller fleets. Under the pool arrangement, the vessels operate under a time charter agreement whereby the cost of bunkers and port expenses are borne by the charterer and operating costs including crews, maintenance and insurance are typically paid by the owner of the vessel. Since the members of the pool share in the revenue generated by the entire group of vessels in the pool, and the pool operates in the spot market, the revenue earned by these two vessels was subject to the fluctuations of the spot market. Effective December 24, 2006 and January 15, 2007, respectively, the Genco Trader and Genco Leader exited the Baumarine Panamax Pool.

Included in the standard time charter contracts with our customers are certain performance parameters, which if not met can result in customer claims. As of March 31, 2007, the Company had a reserve of $177 against due from charterers balance and an additional reserve of $670, each of which is associated with estimated customer claims against the Company including time charter performance issues. As of December 31, 2006, the Company had a reserve of $187 against due from charterers balance and an additional reserve of $571, each of which is associated with estimated customer claims against the Company, including time charter performance issues.

Vessel operating expenses

Vessel operating expenses include crew wages and related costs, the cost of insurance, expenses relating to repairs and maintenance, the cost of spares and consumable stores, and other miscellaneous expenses. Vessel operating expenses are recognized when incurred.

Vessels, net

Vessels, net are stated at cost less accumulated depreciation. Included in vessel costs are acquisition costs directly attributable to the acquisition of a vessel and expenditures made to prepare the vessel for its initial voyage. Vessels are depreciated on a straight-line basis over their estimated useful lives, determined to be 25 years from the date of initial delivery from the shipyard.

Depreciation expense is calculated based on cost less the estimated residual scrap value. The costs of significant replacements, renewals and betterments are capitalized and depreciated over the shorter of the vessel's remaining estimated useful life or the estimated life of the renewal or betterment. Undepreciated cost of any asset component being replaced that was acquired after the initial vessel purchase is written off as a component of vessel operating expense. Expenditures for routine maintenance and repairs are expensed as incurred. Scrap value is estimated by the Company by taking the cost of steel times the weight of the ship noted in lightweight ton (lwt). At March 31, 2007 and December 31, 2006, the Company estimated the residual value of vessels to be $175/lwt.

Fixed assets, net

Fixed assets, net are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are based on a straight-line basis over the estimated useful life of the specific asset placed in service. The following table is used in determining the estimated useful lives:

Description	Useful lives
Leasehold improvements	15 years
Furniture, fixtures & other equipment	5 years
Vessel equipment	2-5 years
Computer equipment	3 years

Deferred drydocking costs

The Company's vessels are required to be drydocked approximately every 30 to 60 months for major repairs and maintenance that cannot be performed while the vessels are operating. The Company capitalizes the costs associated with the drydockings as they occur and depreciates these costs on a straight-line basis over the period between drydockings. Costs capitalized as part of a vessel's drydocking include actual costs incurred at the drydocking yard; cost of parts that are reasonably made in anticipation of reducing the duration or cost of the drydocking; cost of travel, lodging and subsistence of personnel sent to the drydocking site to supervise; and the cost of hiring a third party to oversee the drydocking.

Inventory

Inventory consists of lubricants and bunkers (fuel) which are stated at the lower of cost or market. Cost is determined by the first-in, first-out method.

Impairment of long-lived assets

The Company follows the Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, which requires impairment losses to be recorded on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than their carrying amounts. In the evaluation of the fair value and future benefits of long-lived assets, the Company performs an analysis of the anticipated undiscounted future net cash flows of the related long-lived assets. If the carrying value of the related asset exceeds the undiscounted cash flows, the carrying value is reduced to its fair value. Various factors including anticipated future charter rates, estimated scrap values, future drydocking costs and estimated vessel operating costs, are included in this analysis.

For three months ended March 31, 2007 and 2006, no impairment charges were recorded, based on the analysis described above.

Deferred financing costs

Deferred financing costs, included in other assets, consist of fees, commissions and legal expenses associated with obtaining loan facilities. These costs are amortized over the life of the related debt, which is included in interest expense.

Cash and cash equivalents

The Company considers highly liquid investments such as time deposits and certificates of deposit with an original maturity of three months or less to be cash equivalents.

Income taxes

Pursuant to Section 883 of the U.S. Internal Revenue Code of 1986 as amended (the “Code”), qualified income derived from the international operations of ships is excluded from gross income and exempt from U.S. federal income tax if a company engaged in the international operation of ships meets certain requirements. Among other things, in order to qualify, the company must be incorporated in a country which grants an equivalent exemption to U.S. corporations and must satisfy certain qualified ownership requirements.

The Company is incorporated in the Marshall Islands. Pursuant to the income tax laws of the Marshall Islands, the Company is not subject to Marshall Islands income tax. The Marshall Islands has been officially recognized by the Internal Revenue Service as a qualified foreign country that currently grants the requisite equivalent exemption from tax.

Based on the publicly traded requirement of the Section 883 regulations as described in the next paragraph, we believe that the Company qualified for exemption from income tax for 2006.

In order to meet the publicly traded requirement for 2006 and future years, our stock must be treated as being primarily and regularly traded for more than half the days of any such year. Under the Section 883 regulations, our qualification for the publicly traded requirement may be jeopardized if shareholders of our common stock that own five percent or more of our stock (“5% shareholders”) own, in the aggregate, 50% or more of our common stock for more than half the days of the year. We believe that during 2006, the combined ownership of our 5% shareholders did not equal 50% or more of our common stock for more than half the days of 2006. However if our 5% shareholders were to increase their ownership to 50% or more of our common stock for more than half the days of 2007 or any future taxable year, we would not be eligible to claim exemption from tax under Section 883 for that taxable year. We can therefore give no assurance that changes and shifts in the ownership of our stock by 5% shareholders will not preclude us from qualifying for exemption from tax in 2007 or in future years.

If the Company does not qualify for the exemption from tax under Section 883, it would be subject to a 4% tax on the gross “shipping income” (without the allowance for any deductions) that is treated as derived from sources within the United States or “United States source shipping income.” For these purposes, “shipping income” means any income that is derived from the use of vessels, from the hiring or leasing of vessels for use, or from the performance of services directly related to those uses; and “United States source shipping income” includes 50% of shipping income that is attributable to transportation that begins or ends, but that does not both begin and end, in the United States.

Deferred revenue

Deferred revenue primarily relates to cash received from charterers prior to it being earned. These amounts are recognized as income when earned.

Comprehensive income

The Company follows SFAS No. 130 “Reporting Comprehensive Income,” which establishes standards for reporting and displaying comprehensive income and its components in financial statements. Comprehensive income is comprised of net income and amounts related to the adoption of SFAS No. 133 “Accounting for Derivative Instruments and Hedging Activities”.

Nonvested stock awards

In 2006, the Company adopted SFAS No. 123R, Share-Based Payment, for nonvested stock issued under its equity incentive plan. Adoption of this new accounting policy did not change the method of accounting for nonvested stock awards. However, deferred compensation costs from nonvested stock have been classified as a component of paid-in capital as required by SFAS No. 123R.

Accounting estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates include vessel and drydock valuations and the valuation of amounts due from charterers. Actual results could differ from those estimates.

Concentration of credit risk

Financial instruments that potentially subject the Company to concentrations of credit risk are amounts due from charterers. With respect to amounts due from charterers, the Company attempts to limit its credit risk by performing ongoing credit evaluations and, when deemed necessary, requiring letters of credit, guarantees or collateral. Although the Company earned 100% of revenues from fourteen and eleven customers, for the three months ended March 31, 2007 and 2006, respectively, management does not believe significant risk exists in connection with the Company's concentrations of credit at March 31, 2007 and December 31, 2006.

For the three months ended March 31, 2007 there are two customers that individually accounted for more than 10% of revenue, which represented 15.78% and 13.85% of revenue, respectively. For the three months ended March 31, 2006 there were three customers that individually accounted for more than 10% of revenue, which represented 23.51%, 15.81% and 10.59% of revenue, respectively.

Fair value of financial instruments

The estimated fair values of the Company's financial instruments such as amounts due from charterers, accounts payable and long term debt approximate their individual carrying amounts as of March 31, 2007 and December 31, 2006 due to their short-term maturity or the variable-rate nature of the respective borrowings.

The fair value of the interest rate swaps (used for purposes other than trading) is the estimated amount the Company would receive to terminate the swap agreements at the reporting date, taking into account current interest rates and the creditworthiness of the swaps' counterparty for assets and creditworthiness of the Company for liabilities.

The Company adopted SFAS No. 157, Fair Value Measurements ("SFAS No. 157") in the first quarter of 2007.

Interest rate risk management

The Company is exposed to the impact of interest rate changes. The Company's objective is to manage the impact of interest rate changes on its earnings and cash flow in relation to its borrowings. The Company held three interest rate risk management instruments at March 31, 2007 and at December 31, 2006, in order to manage future interest costs and the risk associated with changing interest rates.

The differential to be paid or received for the effectively hedged portion of any swap agreement is recognized as an adjustment to interest expense as incurred. Additionally, the change in value for the portion of the swaps that are effectively hedged is reflected as a component of other comprehensive income ("OCI").

For the portion of the forward interest rate swaps that are not effectively hedged, the change in the value and the rate differential to be paid or received is recognized as income or (expense) from derivative instruments and is listed as a component of other (expense) income until such time the Company has obligations against which the swap is designated and is an effective hedge.

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Derivative financial instruments

To manage its exposure to fluctuating interest rates, the Company uses interest rate swap agreements. Interest rate differentials to be paid or received under these agreements for any portion of designated debt that is effectively hedged is accrued and recognized as an adjustment of interest expense. The interest rate differential on the swaps that do not have designated debt or are not effectively hedged will be reflected as income or (expense) from derivative instruments and is listed as a component of other (expense) income. The fair value of the interest rate swap agreements is recognized in the financial statements as a non-current asset or liability.

Amounts receivable or payable arising at the settlement of hedged interest rate swaps are deferred and amortized as an adjustment to interest expense over the period of interest rate exposure provided the designated liability continues to exist. Amounts receivable or payable arising at the settlement of unhedged interest rate swaps are reflected as income or (expense) from derivative instruments and are included as a component of other (expense) income.

New accounting pronouncements

In September 2006, FASB issued SFAS No.157 which enhances existing guidance for measuring assets and liabilities using fair value. Previously, guidance for applying fair value was incorporated in several accounting pronouncements. The new statement provides a single definition of fair value, together with a framework for measuring it, and requires additional disclosure about the use of fair value to measure assets and liabilities. While the statement does not add any new fair value measurements, it does change current practice. One such change is a requirement to adjust the value of nonvested stock for the effect of the restriction even if the restriction lapses within one year. The early adoption of SFAS No. 157 on January 1, 2007, did not have a material impact on the financial statements of the Company.

In July 2006, the FASB issued Interpretation No. 48 (“FIN 48”), “Accounting for Uncertainty in Income Taxes–an Interpretation of FASB Statement No. 109.” FIN 48 clarifies the accounting for uncertainty in income taxes recognized by prescribing a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for years beginning after December 15, 2006. The Company has adopted FIN 48, and its adoption did not have a material impact on the Company’s consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (“SFAS No. 159”). Under this statement, the Company may elect to report financial instruments and certain other items at fair value on a contract-by-contract basis with changes in value reported in earnings. This election is irrevocable. SFAS No. 159 is effective for the Company commencing in 2008. Early adoption within 120 days of the beginning of the year is permissible, provided the Company has adopted SFAS No. 157. The adoption of SFAS 159 on January 1, 2008, is not expected to have a material impact on the financial statements of the Company.

3 - CASH FLOW INFORMATION

The Company entered into the 4.485% Swap during 2005 and the 5.075% Swap and 5.25% Swap during March 2006. These swaps are described and discussed in Note 7. The fair value of the 4.485% Swap is in an asset position of $3,973 and $4,462 as of March 31, 2007 and December 31, 2006, respectively. The fair values of the 5.075% Swap and 5.25% Swap are in a liability position of $1,265 and $807 as of March 31, 2007 and December 31, 2006.

The Company had non-cash operating and investing activities not included in the Consolidated Statement of Cash Flows for items included in accounts payable and accrued expenses for the purchase of fixed assets of approximately

$57 and $82 for the three months ended March 31, 2007 and 2006, respectively.

On February 8, 2007 the Company granted nonvested stock to certain directors and employees. The fair value of such nonvested stock was $494 on the grant date and was recorded in equity. Additionally, during January 2007, nonvested stock forfeited amounted to $54 for shares granted in 2005 and is recorded in equity.

During 2006, the Company granted nonvested stock to its employees. The fair value of such nonvested stock was $2,018 on the grant date and was recorded in equity. Additionally, during 2006, nonvested stock forfeited amounted to $12 for shares granted in 2005 and is recorded in equity.

4 - VESSEL ACQUISITIONS AND DISPOSITIONS

On February 21, 2007, the Genco Glory was sold to Cloud Maritime S.A. for $13,004 net of a brokerage commission paid to WeberCompass (Hellas) S.A. Based on the selling price and the net book value of the vessel, the Company recorded a gain of $3,575 during the quarter ended March 31, 2007.

On July 10, 2006, the Company entered into an agreement with affiliates of Franco Compania Naviera S.A. under which the Company purchased three drybulk vessels for an aggregate price of $81,250. These vessels were delivered in the fourth quarter of 2006. The acquisition consisted of a 1999 Japanese-built Panamax vessel, the Genco Acheron, a 1998 Japanese-built Panamax vessel, the Genco Surprise, and a 1994 Japanese-built Handymax vessel, the Genco Commander.

On October 14, 2005, the Company took delivery of the Genco Muse, a 48,913 dwt Handymax drybulk carrier and the results of its operations is included in the consolidated results of the Company after that date. The vessel is a 2001 Japanese-built vessel. The total purchase price of the vessel was $34,450. The purchase price included the assumption of an existing time charter with Qatar Navigation QSC at a rate of $26.5 per day. Due to the above market rate of the existing time charter at the time of the acquisition, the Company has capitalized $3,492 of the purchase price as an asset which is being amortized as a reduction of voyage revenues through September 2007 (the remaining term of the charter). For the three months ended March 31, 2007 and 2006, $456 was amortized for each respective period. The remaining unamortized balance at March 31, 2007 and December 31, 2006 $788 and $1,244, respectively, will be reflected as a reduction of voyage revenue during 2007.

See Note 1 for discussion on the initial acquisition of our initial 16 drybulk carriers.

The purchase and sale of the aforementioned vessels is consistent with the Company's strategy of selectively expanding the number and maintaining the high-quality vessels in the fleet.

5 - EARNINGS PER COMMON SHARE

The computation of basic earnings (loss) per share is based on the weighted average number of common shares outstanding during the year. The computation of diluted earnings (loss) per share assumes the vesting of nonvested stock awards (see Note 16), for which the assumed proceeds upon grant are deemed to be the amount of compensation cost attributable to future services and not yet recognized using the treasury stock method, to the extent dilutive. For the three months ended March 31, 2007 and 2006, the restricted stock grants are dilutive.

The components of the denominator for the calculation of basic earnings per share and diluted earnings per share are as follows:

	Three Months Ended March 31,	
	2007	**2006**
Common shares outstanding, basic:		
Weighted average common shares outstanding, basic	25,308,953	25,260,000
Common shares outstanding, diluted:		
Weighted average common shares outstanding, basic	25,308,953	25,260,000

Weighted average restricted stock awards	112,527	44,448
Weighted average common shares outstanding, diluted	25,421,480	25,304,448

6 - RELATED PARTY TRANSACTIONS

The following are related party transactions not disclosed elsewhere in these financial statements:

In June 2006, the Company made an employee performing internal audit services available to General Maritime Corporation ("GMC"), where the Company's Chairman, Peter C. Georgiopoulos, also serves as Chairman of the Board, Chief Executive Officer and President, and Stephen A. Kaplan, one of the Company's directors, also serves as a director. For the three months ended March 31, 2007 and 2006, the Company invoiced $35 and $0, respectively, to GMC for the time associated with such internal audit services. At March 31, 2007 and December 31, 2006, the amount due the Company from GMC is $15 and $25, respectively.

During the three months ended March 31, 2007 and 2006, the Company incurred travel related expenditures totaling $0 and $139, respectively, reimbursable to GMC or its service provider, where the Company Chairman, Peter C. Georgiopoulos also serves as Chairman of the Board, Chief Executive Officer and President, and Stephen A. Kaplan also serves as a director. For the three months ended March 31, 2006 approximately, $49 of these travel expenditures were paid from the gross proceeds received from the initial public offering and as such were included in the determination of net proceeds. There were no amounts due to GMC at March 31, 2007 or December 31, 2006.

During the three months ended March 31, 2007 and 2006, the Company incurred legal services aggregating $29 and $1 from Constantine Georgiopoulos, father of Peter C. Georgiopoulos, Chairman of the Board. At March 31, 2007 and December 31, 2006, $29 and $1, respectively, was outstanding to Constantine Georgiopoulos.

In December 2006, the Company engaged the services of WeberCompass (Hellas) S.A. ("WC"), a shipbroker, to facilitate the sale of the Genco Glory. One of our directors, Basil G. Mavroleon, is a Managing Director of WC and a Managing Director and shareholder of Charles R. Weber Company, Inc., which is 50% shareholder of WC. WC was paid a commission of $132, or 1% of the gross selling price of the Genco Glory. No amounts were due to WC at March 31, 2007 or at December 31, 2006.

During March 2007, the Company utilized the services of North Star Maritime, Inc. ("NSM") which is owned and operated by one of our directors, Rear Admiral Robert C. North, USCG (ret.). NSM, a marine industry consulting firm, specializes in international and domestic maritime safety, security and environmental protection issues. NSM was paid $7 for services rendered in March 2007. No amounts were due to NSM at March 31, 2007 or at December 31, 2006.

7 - LONG-TERM DEBT

Long-term debt consists of the following:

	March 31, 2007	**December 31, 2006**
Revolver, New Credit Facility	$ 206,233	$ 211,933
Less: Current portion of revolver	-	4,322
Long-term debt	$ 206,233	$ 207,611

New credit facility

The Company entered into the New Credit Facility as of July 29, 2005. The New Credit Facility is with a syndicate of commercial lenders including Nordea Bank Finland plc, New York Branch, DnB NOR Bank ASA, New York Branch and Citibank, N.A. The New Credit Facility has been used to refinance our indebtedness under our Original Credit Facility, and may be used in the future to acquire additional vessels and for working capital requirements. Under the terms of our New Credit Facility, borrowings in the amount of $106,233 were used to repay indebtedness under our Original Credit Facility and additional net borrowings of $24,450 were obtained to fund the acquisition of the Genco Muse. In July 2006, the Company increased the line of credit by $100,000 and during the second and third quarters of 2006 borrowed $81,250 for the acquisition of three vessels. At March 31, 2007,

$443,767 remains available to fund future vessel acquisitions. The Company may borrow up to $20,000 of the $443,767 for working capital purposes.

The New Credit Facility has a term of ten years and matures on July 29, 2015. The facility permits borrowings up to 65% of the value of the vessels that secure our obligations under the New Credit Facility up to the facility limit, provided that conditions to drawdown are satisfied. Certain of these conditions require the Company, among other things, to provide to the lenders acceptable valuations of the vessels in our fleet confirming that the aggregate amount outstanding under the facility (determined on a pro forma basis giving effect to the amount proposed to be drawn down) will not exceed 65% of the value of the vessels pledged as collateral. The facility limit is reduced by an amount equal to 8.125% of the total $550,000, commitment, semi-annually over a period of four years and is reduced to $0 on the tenth anniversary.

Additionally, on February 7, 2007, the Company reached an agreement with its syndicate of commercial lenders to allow the Company to increase the amount of the New Credit Facility by $100,000, for a total maximum availability of $650,000. The Company has the option to increase the facility amount by $25,000 increments up to the additional $100,000, so long as at least one bank within the syndicate agrees to fund such increase. Any increase associated with this agreement is generally governed by the existing terms of the New Credit Facility, although we and any banks providing the increase may agree to vary the upfront fees, unutilized commitment fees, or other fees payable by us in connection with the increase.

The obligations under the New Credit Facility are secured by a first-priority mortgage on each of the vessels in our fleet as well as any future vessel acquisitions pledged as collateral and funded by the New Credit Facility. The New Credit Facility is also secured by a first-priority security interest in our earnings and insurance proceeds related to the collateral vessels. The Company may grant additional security interest in vessels acquired that are not mortgaged.

All of our vessel-owning subsidiaries are full and unconditional joint and several guarantors of our New Credit Facility. Each of these subsidiaries is wholly owned by Genco Shipping & Trading Limited. Genco Shipping & Trading Limited has no independent assets or operations.

Interest on the amounts drawn is payable at the rate of 0.95% per annum over LIBOR until the fifth anniversary of the closing of the New Credit Facility and 1.00% per annum over LIBOR thereafter. We are also obligated to pay a commitment fee equal to 0.375% per annum on any undrawn amounts available under the facility. On July 29, 2005, the Company paid an arrangement fee to the lenders of $2.7 million on the original commitment of $450,000 and an additional $600 for the $100,000 commitment increase which equates to 0.6% of the total commitment of $550,000 as of July 12, 2006. These arrangement fees along with other costs have been capitalized as deferred financing costs.

Under the terms of our New Credit Facility, we are permitted to pay or declare dividends in accordance with our dividend policy so long as no default or event of default has occurred and is continuing or would result from such declaration or payment.

The New Credit Facility has certain financial covenants that require the Company, among other things, to: ensure that the fair market value of the collateral vessels maintains a certain multiple as compared to the outstanding indebtedness; maintain a specified ratio of total indebtedness to total capitalization; maintain a specified ratio of earnings before interest, taxes, depreciation and amortization to interest expense; maintain a net worth of approximately $263,000; and maintain working capital liquidity in an amount of not less than $500 per vessel securing the borrowings. Additionally, there are certain non-financial covenants that require the Company, among other things, to provide the lenders with certain legal documentation, such as the mortgage on a newly acquired vessel using funds from the New Credit Facility, and other periodic communications with the lenders that include certain compliance certificates at the time of borrowing and on a quarterly basis. For the period since facility inception through March 31, 2007, the Company has been in compliance with these covenants, except for an age covenant in conjunction with the acquisition of the Genco Commander, a 1994 vessel, for which the Company obtained a waiver for the term of the agreement.

The New Credit Facility permits the issuance of letters of credit up to a maximum amount of $50,000. The conditions under which letters of credit can be issued are substantially the same as the conditions for borrowing funds under the facility. Each letter of credit must terminate within twelve months, but can be extended for successive periods also not exceeding twelve months. The Company pays a fee of 1/8 of 1% per annum on the amount of letters of credit outstanding. At March 31, 2007 and December 31, 2006, there were no letters of credit issued under the New Credit Facility.

Due to the agreement related to the sale of the Genco Glory, the New Credit Facility requires a certain portion of the debt be repaid based on a pro-rata basis. The repayment amount is calculated by dividing the value of the vessel being sold by the value of the entire fleet and multiplying such percentage by the total debt outstanding. Therefore, the Company reflected $4,322 as current portion of long-term debt as of December 31, 2006. The Company repaid $5,700 during the first quarter of 2007 to comply with the repayment requirement from the sale of the Genco Glory.

The following table sets forth our maturity dates of the revolver as of:

		$
Period Ending		23,106
December 31,	**Total**	

Net credit swap revenue is discussed below for Primus Financial.

Net Credit Swap Revenue – Primus Financial

Net credit swap revenue was $116.7 million and $23.1 million for the years ended December 31, 2006 and 2005, respectively. Net credit swap revenue includes:

- Net premiums earned;
- Net realized gains (losses) on credit swaps; and
- Net unrealized gains (losses) on credit swaps.

Net credit swap revenue for Primus Financial excludes $321 thousand and $346 thousand, for the years ended December 31, 2006 and 2005, respectively, of net revenue earned on three credit swap transactions with its affiliate, Primus Re, as these amounts are eliminated in consolidation.

The table below shows the components of net credit swap revenue for the years ended December 31, 2006 and 2005 (in thousands):

	Years ended December 31, 2006	2005
Net premiums earned	$ 69,446	$ 52,705
Net realized losses on credit swaps	(1,496)	(5,162)
Net unrealized gains (losses) on credit swaps	48,701	(24,437)
Total net credit swap revenue	$ 116,651	$ 23,106

Net Premiums Earned – Primus Financial

Net premiums earned were $69.4 million and $52.7 million for the years ended December 31, 2006 and 2005, respectively. Net premiums earned include:

- Premium income on single name credit swaps sold;

- Premium income on tranches sold;
- Premium income on credit swaps sold on asset backed securities (ABS);
- Premium expense on credit swaps purchased as short-term investments; and
- Premium expense on credit swaps purchased to offset credit risk on certain credit swaps sold.

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The table below shows the components of net premiums earned for the years ended December 31, 2006 and 2005 (in thousands):

	Years ended December 31,	
	2006	2005
Premium income on single name credit swaps sold	$ 66,824	$ 53,702
Premium income on tranches sold	2,619	324
Premium income on ABS credit swaps sold	3	—
Premium expense on credit swaps purchased as short-term investments	—	(1,254)
Premium expense on credit swaps purchased to offset credit risk on certain swaps sold	—	(67)
Total net premiums earned	$ 69,446	$ 52,705

Premium income on single name credit swaps sold was $66.8 million and $53.7 million during the years ended December 31, 2006 and 2005, respectively. The increase was primarily due to the expansion of our credit swap portfolio. The average notional amounts outstanding of credit swaps sold were $14.9 billion and $12.2 billion for the years ended December 31, 2006 and 2005, respectively.

We began to sell credit swaps in tranche format during the second quarter of 2005, whereby we sell credit swaps referencing portfolios containing obligations of multiple Reference Entities. Premium income from the tranches sold was $2.6 million and $324 thousand for the years ended December 31, 2006 and 2005, respectively. The average notional amount outstanding was $288.0 million and $38.0 million for the years ended December 31, 2006 and 2005, respectively.

During the fourth quarter of 2006, we received rating agency approval to sell credit protection on asset-backed securities (ABS).

The portfolio of credit swaps purchased for short-term investment purposes and to offset credit risk was wound down to zero during 2005 and there was no premium expense for swaps of these types in 2006.

Net Realized Gains (Losses) on Credit Swaps – Primus Financial

Net realized gains (losses) for the years ended December 31, 2006 and 2005 are summarized below (in thousands):

	Years ended December 31,	
	2006	2005
Realized gains on terminated credit swaps sold	$ 1,519	$ 1,090
Realized gains on terminated tranches sold	483	—
Realized losses on terminated credit swaps sold	(3,498)	(4,601)
Realized gains on terminated credit swaps purchased as short-term investments	—	719
Realized losses on terminated credit swaps purchased as short-term investments	—	(2,196)
Realized losses on terminated credit swaps purchased to offset credit risk on certain swaps sold	—	(174)
Total net realized losses on credit swaps	$ (1,496)	$ (5,162)

Net realized losses on the early termination of credit swaps were $1.5 million and $5.2 million for the years ended December 31, 2006 and 2005, respectively. We terminated $445.7 million and $428.0 million notional amount of credit swaps sold during the years ended December 31, 2006 and 2005, respectively. We received $1.5 million and $1.1 million from the early termination of swaps at a realized gain during the years ended December 31, 2006 and 2005, respectively. We incurred realized losses of $3.5 million and $4.6 million during the years ended December 31, 2006 and 2005, respectively, from the early termination of swaps primarily in order to mitigate credit risk.

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We terminated $50.0 million notional of tranches sold during the fourth quarter of 2006, resulting in a realized gain of $483 thousand.

We terminated $484.0 million notional amount of credit swaps purchased during the year ended December 31, 2005, resulting in a net realized loss of $1.5 million. During the course of 2005 we wound down our portfolio of credit swaps purchased and, as a consequence, there were no realized gains or losses on this portfolio in 2006.

During the third quarter of 2005, we terminated our position where we had purchased credit swaps to offset credit risk on certain swaps sold and we realized a loss of $174 thousand.

Net Unrealized Gains (Losses) on Credit Swaps – Primus Financial

The unrealized gains (losses) on credit swaps sold and credit swaps purchased as short-term investments and for credit risk offset purposes for the years ended December 31, 2006 and 2005 are summarized below (in thousands):

	Years ended December 31,	
	2006	2005
Net unrealized gains (losses) on credit swaps sold	$ 52,437	$ (27,530)
Net unrealized gains (losses) on tranches sold	(3,713)	685
Net unrealized losses on ABS credit swaps sold	(23)	—
Net unrealized gains on credit swaps purchased as short-term investments	—	2,202
Net unrealized gains on credit swaps purchased to offset credit risk on certain credit swaps sold	—	206
Total net unrealized gains (losses) on credit swaps	$ 48,701	$ (24,437)

Net unrealized gains (losses) on Primus Financial’s credit swaps were $48.7 million and $(24.4) million for the years ended December 31, 2006 and 2005, respectively. The change in unrealized gains (losses) on credit swaps reflects the change in the fair value of our credit swap portfolio during these periods. The gain during the year of 2006 on credit swaps sold is primarily attributable to the increase in the fair value of the portfolio as market premiums fell during that period. Market premium levels at December 31, 2005 were higher than those prevailing at December 31, 2004, which resulted in the unrealized loss in the years ended December 31, 2005.

Asset Management and Advisory Fees

We earned $1.3 million and $190 thousand of asset management and advisory fees for the years ended December 31, 2006 and 2005, respectively. During the second quarter of 2006, we closed on our third investment grade Collateralized Swap Obligation or CSO, on behalf of third parties in exchange for management fees. During the third quarter of 2006, on behalf of another third party, we received an advisory fee of $400 thousand for the arrangement of a credit swap tranche transaction. On December 19, 2006, the offering of Primus CLO I, Ltd closed. Primus Asset Management will act as collateral manager of the CLO. Under the terms of the collateral management agreement of the CLO, Primus Asset Management will receive management fees quarterly for managing the selection, acquisition and disposition of the underlying collateral and for monitoring the underlying collateral. Some of our asset management contracts also provide for the receipt of contingent performance fees at maturity, none of which has been earned or accrued at December 31, 2006 or 2005, respectively.

Interest Income

We earned interest income of $28.4 million and $16.0 million for the years ended December 31, 2006 and 2005, respectively. The increase in interest income is primarily attributable to higher average invested balances resulting from the December 2005 issuance of $125 million of subordinated debt by Primus Financial and retained cash earnings, together with higher yields on our investment portfolio. The increase in yields is attributable to generally increasing market rates of interest during 2005 and 2006.

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Average yields on our cash, cash equivalents and investments were 4.39% during the year ended December 31, 2006 compared with 3.28% for the year ended December 31, 2005.

The table below summarizes our interest income for the years ended December 31, 2006 and 2005 and our total cash, cash equivalents, available-for-sale and trading account assets at December 31, 2006 and 2005 (in thousands):

	Years ended December 31,	
	2006	2005
Interest income	$ 28,374	$ 16,047
Cash and cash equivalents*	$ 204,428	$ 69,355
Available-for-sale and trading account assets	599,448	560,147
Total cash, cash equivalents and available-for-sale and trading account assets	$ 803,876	$ 629,502

* Included in cash and cash equivalents are the net proceeds of approximately $121 million from our 7% senior note offering on December 27, 2006.

Other Trading Revenue

During the year ended December 31, 2006, PRS Trading Strategies recorded other trading revenues of $1.7 million. Other trading revenues comprises the net trading gains from PRS Trading Strategies' total return swaps, loan warehousing and bond trading activities. PRS Trading Strategies commenced operations in January 2006 and therefore prior year comparison information is not available.

Foreign Currency Revaluation

We transact credit swaps denominated in U.S. dollars and euros. Euro-denominated credit swaps comprised 29% of the notional amount of our Primus Financial credit swaps sold portfolio at December 31, 2006. Until the fourth quarter of 2005, net premiums received from swaps denominated in euros were retained in euros. We now sell the majority of our euro premium receipts as they are received for U.S dollars, retaining only a small working cash balance in euros. During the year ended December 31, 2006, we recorded a revaluation loss of $26 thousand on our significantly reduced holdings of euros. During the year ended December 31, 2005, the euro depreciated in value against the U.S. dollar resulting in currency revaluation losses of $1.5 million on our holdings of euros.

Operating Expenses

Our operating expenses were $36.4 million and $27.5 million for the years ended December 31, 2006 and 2005, respectively, as summarized below (dollars in thousands):

	Years ended December 31,	
	2006	2005
Compensation and employee benefits	$ 21,512	$ 15,935
Professional and legal fees	5,147	4,534
Depreciation and amortization	2,517	2,123
Technology and data	2,427	1,630
Other	4,796	3,326
Total operating expenses	$ 36,399	$ 27,548
Number of full-time employees, at end of period	52	35

Compensation expense for the year ended December 31, 2006 increased $5.6 million over the comparable prior year. Overall, the increase was primarily the result of an increase in headcount as we expanded our business operations and higher performance based incentives. Included in the year

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ended December 31, 2006, was a credit of approximately $650 thousand related to a reduction in share compensation expense as a result of employee departures. Compensation expense for the year ended December 31, 2005 included approximately $800 thousand related to the accelerated compensation expenses and accelerated vesting of shares related to the departure of former employees. Our accrued cash incentive compensation expense was $8.8 million for the year ended December 31, 2006, compared with an accrued expense of $4.8 million in the corresponding year of 2005. Share compensation expense was approximately $3.7 million for both years ended December 31, 2006 and 2005, respectively.

The increase in professional fees is primarily related to increased provisions for legal fees and employee recruiting costs. The increase in depreciation and amortization expense is due to the increase in purchases of fixed assets and higher capitalized software costs. The increase in technology and data expense was primarily attributable to the expansion of our technology platform to accommodate new trading strategies associated with our asset management build out. The increase in other expenses was primarily due to travel related costs and occupancy expenses associated with the additional office space in New York and London.

Interest Expense and Preferred Distributions

For the years ended December 31, 2006 and 2005, we incurred $10.8 million and $2.7 million of interest expense, respectively. The interest expense was incurred on the $75 million 30-year subordinated debt and the $125 million 15.5 year subordinated deferrable interest notes that were issued by Primus Financial in July 2004 and December 2005, respectively. The interest rate for the 30-year subordinated debt averaged 5.06% and 3.11% for the years ended December 31, 2006 and 2005, respectively.

On December 27, 2006, Primus Guaranty, Ltd. completed an offering of $125 million, 7% senior notes, which mature in December 2036. Interest on the senior notes will be payable quarterly of each year, beginning on March 27, 2007.

On December 19, 2005, Primus Financial issued $125 million of subordinated deferrable interest notes, which mature in June 2021. The average interest rate on these notes was 5.32% during the year ended December 31, 2006.

Primus Financial also made net distributions of $5.7 million and $3.9 million during the years ended December 31, 2006 and 2005, respectively, on the Primus Financial Cumulative Preferred Shares issued in December 2002. The average rate on these securities was 5.73% and 3.95% during the years ended December 31, 2006 and 2005, respectively.

Income Taxes

Provision for income taxes was $42 thousand and $46 thousand for the years ended December 31, 2006 and 2005, respectively. Primus Guaranty had a net deferred tax asset, fully offset by a valuation allowance, of $9.5 million and $4.8 million as of December 31, 2006 and December 31, 2005, respectively. The change in the deferred tax asset and valuation allowance resulted primarily from Primus Asset Management's estimated net operating loss. It is expected that only the income of Primus Asset Management and its subsidiary, Primus Re, are likely to be subject to United States federal and local income taxes. However, were Primus Bermuda to be subject to income tax, at a combined United States federal, New York State and New York City income tax rate of 46%, on its United States GAAP income, then its income tax expense (excluding interest and penalties) would have been approximately $49.2 million and approximately $3.7 million for the years ended December 31, 2006 and 2005, respectively. These figures assume that Primus Financial is not deemed to be making distributions to Primus Bermuda; such distributions would subject Primus Bermuda to an additional United States federal branch profits tax.

Non-GAAP Financial Measures – Economic Results

In addition to the results of operations presented in accordance with U.S. generally accepted accounting principles (GAAP), our management and our Board of Directors use certain Non-GAAP

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financial measures called Economic Results. We believe that our Economic Results provide information useful to investors in understanding our underlying operational performance and business trends. Economic Results is an accrual based measure of our financial performance, which in our view, better reflects our long-term buy and hold strategy in our credit protection business. However, Economic Results is not a measurement of financial performance or liquidity under GAAP, therefore, these Non-GAAP financial measures should not be considered as an alternative or substitute for GAAP.

We define Economic Results as GAAP net income (loss) adjusted for the following:

- Unrealized gains (losses) on credit swaps sold by Primus Financial are excluded from GAAP net income (loss);
- Realized gains from early termination of credit swaps sold by Primus Financial are excluded from GAAP net income (loss) and;
- Realized gains from early termination of credit swaps sold by Primus Financial are amortized over the period that would have been the remaining life of the credit swap, and that amortization is added to GAAP net income (loss).
- Provision for credit events.

We exclude unrealized gains (losses) on credit swaps sold because the fair value will fluctuate significantly as a result of changes in market credit swap premium levels and are not necessarily indicative of the performance of our underlying business and our general strategy of holding credit swaps sold until maturity, at which time the mark to market values would revert to zero, to the extent no realized gains or losses had occurred. We exclude realized gains on credit swaps sold because our strategy is focused on generation of premium income as opposed to trading gains and losses, although we amortize these realized gains over the original remaining life of the terminated contracts.

The following table below presents a reconciliation of our Economic Results (Non-GAAP measures) to GAAP:

Years Ended December 31,	2007	2006	2005
GAAP net income (loss)	$ (563,541)	$ 94,891	$ 4,083
Adjustments:			
Less: Change in unrealized fair value of credit swaps sold (gain) loss by Primus Financial	614,551	(48,701)	26,639
Less: Realized gains from early termination of credit swaps sold by Primus Financial	(3,463)	(2,002)	(1,090)
Add: Amortization of realized gains from the early termination of credit swap sold by Primus Financial	6,044	7,098	6,783
Less: Provision for credit events	(40,880)	—	—
Net Economic Results	$ 12,711	$ 51,286	$ 36,415
Economic earnings per diluted share	$ 0.28	$ 1.15	$ 0.82
Economic weighted average common shares outstanding – diluted	45,194	44,472	44,645

During the fourth quarter of 2007, management has included for Economic Results, a provision of $40.9 million to account for the credit events that occurred subsequent to the year ended December 31, 2007, which related to the portfolio of credit swaps sold on ABS.

Economic earnings per diluted share is calculated by dividing net economic results by the weighted average number of common shares adjusted for the potential issuance of common shares (dilutive securities).

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Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements (as such term is defined in Item 303 of Regulation S-K) that are reasonably likely to have a current or future material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Contractual Obligations

The following table summarizes our contractual obligations at December 31, 2007 and the effect that those obligations are expected to have on our liquidity and cash flows in future periods (in thousands):

Payment due by period	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Property leases	$ 9,926	$ 1,255	$ 2,511	$ 2,503	$ 3,657
Senior notes	125,000	—	—	—	125,000
Interest on senior notes (b)	253,653	8,750	17,500	17,500	209,903
Subordinated deferrable interest notes	200,000	— (a)	— (a)	— (a)	200,000
Total	$ 588,579	$ 10,005	$ 20,011	$ 20,003	$ 538,560

(a) Payments on the subordinated deferrable interest notes for the next five years cannot be determined, as the notes are auction rate obligations. (b) Net interest payments on the $125 million, 7% senior notes will vary due to the interest rate swap agreement, as previously discussed.

Property leases: Primus Financial currently occupies approximately 17,500 square feet of office space at 360 Madison Avenue, New York, New York at a fixed yearly rental (subject to certain escalations specified in the lease). In 2006, Primus Financial amended the original lease to extend its term to 2016 and add approximately 5,500 square feet of additional space. In addition, in 2006, we leased approximately 2,900 square feet of office space in London under a lease that expires in 2012. There are no material restrictions imposed by our lease agreements and the leases are categorized as operating leases.

Senior notes and Subordinated deferrable interest notes: For information on the terms of our debt, see note 10 of our notes to consolidated financial statements.

We have no other material long-term contractual obligations.

Liquidity and Capital Resources

Capital Strategy

Our consolidated cash, cash equivalents, available-for-sale and trading account securities were $860.3 million and $803.9 million as of December 31, 2007 and December 31, 2006, respectively. Since its inception, Primus Guaranty has raised both debt and equity capital and has contributed capital to its operating subsidiaries. Primus Guaranty is a holding company with no direct operations of its own, and as such, it is largely dependent upon the ability of its operating subsidiaries to generate cash to service its debt obligations and working capital needs.

On December 27, 2006, Primus Guaranty completed an offering of $125 million , 7% senior notes, which mature in December 2036. The senior notes are senior unsecured obligations and rank equally with all of our other unsecured and unsubordinated indebtedness. The senior notes are also structurally subordinated to all liabilities of Primus Guaranty's subsidiaries. The senior notes are

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redeemable at the option of Primus Guaranty, in whole or in part, at any time on or after December 27, 2011, at redemption price equal to 100% of the principal amount to be redeemed, plus any accrued and unpaid interest thereon to the redemption date. Interest on the senior notes is payable quarterly, beginning on March 27, 2007. The senior notes are rated BBB+/Baa1 by S&P and Moody's, respectively. Primus Guaranty intends to generally maintain assets available for debt service equivalent to two years' annual debt service on these senior notes.

In order to support its credit ratings, Primus Financial, is required to maintain capital in an amount determined by its capital models as agreed upon with S&P and Moody's. The capital required is primarily a function of Primus Financial's credit swap portfolio characteristics, operating expenses and tax position. Retained cash flow and proceeds from financings are utilized to increase our capital resources to support our credit swap business. At December 31, 2007 and December 31, 2006, Primus Financial had cash, cash equivalents and available-for-sale investments of $749.5 million and $624.5 million, respectively, which management believes is sufficient to operate its credit swap business.

Primus Financial receives cash from the receipt of credit swap premiums, realized gains from the early termination of credit swaps, interest income earned on our investment portfolio and capital raising activities. Cash is used to pay operating and administrative expenses, premiums on credit swaps purchased, realized losses from the early termination of credit swaps, interest on debt and preferred share distributions.

During the fourth quarter of 2007, the Company decided to discontinue Harrier, due in part to Harrier's performance and difficulty in raising third-party capital, given the market environment at that time. As a result, Harrier returned $52.0 million of its capital to Primus Guaranty during the fourth quarter of 2007 and subsequently, Primus Guaranty contributed $50 million to Primus Financial to support its credit swap business. The remaining capital in Harrier will be returned to Primus Guaranty during the first half of 2008, upon the final settlement of its closed trading positions.

Cash Flows

Cash flows from operating activities – Net cash provided by operating activities were $68.7 million and $42.2 million for the years ended December 31, 2007 and 2006, respectively. This increase is primarily attributable to higher premium income on a larger credit swap portfolio during 2007 compared with 2006, as a result of the continued growth of our credit swap portfolio.

Net cash provided by operating activities were $42.2 million and $36.3 million for the years ended December 31, 2006 and 2005, respectively. This increase is primarily attributable to higher premium income on a larger credit swap portfolio during 2006 compared with 2005, as a result of the continued growth of our credit swap portfolio.

Cash flows from investing activities – Net cash used in investing activities were $29.6 million and $21.9 million for the years ended December 31, 2007 and 2006, respectively. The change was primarily due to increased net purchases of available-for-sale investments in 2007 compared with 2006.

Net cash used in investing activities were $21.9 million and $404.3 million for the years ended December 31, 2006 and 2005, respectively. The decrease was primarily due to reduced purchases of available-for-sale investments in 2006 compared with 2005.

Cash flows from financing a ctivities – Net cash used in financing activities was $0.8 million for the year ended December 31, 2007. Net cash provided by financing activities was $114.6 million for the year ended

December 31, 2006. In 2007, we used cash to pay preferred distributions by our subsidiary, Primus Financial, and repurchase and retire common shares, partially offset by the proceeds received from the exercise of warrants by XL Insurance (Bermuda) Ltd. In 2006, cash provided by financing was primarily the result of the net proceeds received from our senior notes offering.

Net cash provided by financing activities were $114.6 million and $116.4 million for the years ended December 31, 2006 and 2005, respectively. This decrease is primarily due to an increase in preferred distributions by our subsidiary, Primus Financial and higher debt issuance costs during 2006 compared with 2005, partly offset by lower repurchase and retirement of our common shares.

With our current capital resources and anticipated future credit swap premium receipts and interest income, we believe we have sufficient liquidity to pay our operating and financing expenses (including preferred distributions) over at least the next twelve months.

Recent Accounting Pronouncements

In April 2006, the FASB issued FASB Staff Position FIN 46(R)-6, Determining the Variability to Be Considered in Applying FASB Interpretation No. 46(R) (‘‘FSP FIN 46(R)-6’’). FSP FIN 46(R)-6 addresses how variability should be considered when applying FIN 46(R). Variability affects the determination of whether an entity is a variable interest entity (VIE), which interests are variable interests, and which party, if any, is the primary beneficiary of the VIE required to consolidate. FSP FIN 46(R)-6 clarifies that the design of the entity also should be considered when identifying which interests are variable interests. The Company adopted FSP FIN 46(R)-6 during the third quarter of 2006 and applied it prospectively to all entities in which the Company first became involved with. The adoption of FSP FIN 46(R)-6 did not have a material effect on the Company’s consolidated financial statements.

In June 2006, the FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109 (‘‘FIN 48’’). FIN 48 prescribes a recognition threshold and measurement attributes for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. Effective January 1, 2007, the Company adopted FIN 48. The adoption of FIN 48 did not have a material effect on the Company’s consolidated financial statements. See note 11 of notes to consolidated financial statements for further discussion.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (‘‘SFAS No. 157’’). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP), and expands disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. The Company has determined that the adoption of SFAS No. 157 will not have a material effect on its consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Liabilities (‘‘SFAS No. 159’’). SFAS No. 159 provides a fair value option election that allows companies to irrevocably elect fair value as the initial and subsequent measurement attribute for certain financial assets and liabilities, with changes in fair value recognized in earnings as they occur. SFAS No. 159 permits the fair value option election on an instrument by instrument basis at initial recognition of an asset or liability or upon an event that gives rise to a new basis of accounting for that instrument. SFAS No. 159 is effective as of the beginning of an entity’s first fiscal year that begins after November 15, 2007. The Company has determined that the adoption of SFAS No. 159 will not have a material effect on its consolidated financial statements.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

Market risk represents the potential for gains or losses that may result from changes in the value of a financial instrument as a consequence of changes in market conditions. Our primary market risk is changes in market credit swap premium levels, which increase or decrease the fair value of our credit swap portfolio. Market credit swap premium levels change as a result of specific events or news related to a Reference Entity, such as a change in a credit rating by any of the rating agencies. Additionally, market credit swap premium levels can vary as a result of changes in market sentiment. As a general matter, given our strategy of holding credit swaps sold until maturity, we do not seek to manage our overall exposure to market credit swap premium levels, and we expect fluctuations in the fair value of our credit swap portfolio as a result of these changes. As of December 31, 2007, each one basis point increase or decrease in market credit swap premiums would decrease or increase the fair value of our credit swap portfolio by approximately $10.7 million.

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We face other market risks, which are likely to have a lesser impact upon our net income than those associated with market credit swap premium level risk. These other risks include interest rate risk associated with market interest rate movements. These movements may affect the value of our credit swap portfolio as our pricing model includes an interest rate component, which is used to discount future expected cash flows. Interest rate movements may also affect the carrying value of and yield on our investments. The Primus Financial Cumulative Preferred Shares pays distributions that are based upon the auction rate preferred market. A difference between the rates we pay in the auction rate preferred market and the interest rates we receive on our investments may result in an additional cost to our company. Assuming that auction results with respect to the Primus Financial Cumulative Preferred Shares reflect prevailing short-term interest rates, each 25 basis point increase or decrease in the level of those rates would increase or decrease Primus Financial’s annual distribution cost by approximately $125,000 for each of the Series A and Series B MMP Receipts. In addition, interest rate movements may increase or decrease the interest expense we incur on our $200 million of subordinated deferrable interest notes. A 25 basis point increase in the level of those rates would increase Primus Financial’s interest expense by $500,000 annually.

In February 2007, the Company entered into an interest rate swap agreement with a major financial institution that effectively converted a notional amount of $75 million of the Company’s $125 million, 7% senior notes due in December 2036, to floating rate debt based on the three month LIBOR rate plus a spread as defined in the agreement. Assuming a 25 basis point increase or decrease in the three month LIBOR rate, our interest expense would increase or decrease by $187,500 annually.

Counterparty risk represents the potential for loss should one or more of our counterparties be unable to meet its obligations due to bankruptcy or a similar event, which could adversely affect our results of operations. Our counterparties generally have investment grade credit ratings.

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Item 8. Financial Statements and Supplementary Data

Primus Guaranty, Ltd.
Index to Consolidated Financial Statements

All Financial Statement Schedules are omitted because they are not applicable or the required information is shown in the Consolidated Financial Statements or the Notes thereto.

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders' of Primus Guaranty, Ltd.

We have audited the accompanying consolidated statements of financial condition of Primus Guaranty, Ltd. (the ''Company'') as of December 31, 2007 and 2006, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2007. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Primus Guaranty, Ltd. at December 31, 2007 and 2006, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2007, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Primus Guaranty, Ltd.'s internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 13, 2008 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP
New York, New York

March 13, 2008

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Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders of Primus Guaranty, Ltd.

We have audited the internal control over financial reporting of Primus Guaranty, Ltd. (the ‘‘Company’’) as of December 31, 2007, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). The Company’s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management’s Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company’s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Primus Guaranty, Ltd. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statements of financial condition of Primus Guaranty, Ltd. as of December 31, 2007 and 2006 and the related consolidated statements of operations, shareholders’ equity and cash flows for each of the three years in the period ended December 31, 2007 of Primus Guaranty, Ltd. and our report dated March 13, 2008 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP
New York, New York

March 13, 2008

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Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. Internal control over financial reporting is defined in Rule 13a-15(f) or 15d-15(f) under the Securities Exchange Act of 1934 as a process designed by, or under the supervision of, our principal executive and principal financial officers and effected by our board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2007. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control-Integrated Framework. Based on our assessment, we believe that as of December 31, 2007, the Company's internal control over financial reporting is effective based on that criteria.

/s/ Thomas W. Jasper /s/ Richard Claiden Thomas W. Jasper Richard Claiden Chief Executive Officer Chief Financial Officer

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Primus Guaranty, Ltd.
Consolidated Statements of Financial Condition
(in thousands except per share amounts)

	December 31, 2007	December 31, 2006
Assets		
Cash and cash equivalents	$ 242,665	$ 204,428
Available-for-sale investments	617,631	584,911
Trading account assets	—	14,537
Accrued interest receivable	7,684	6,374
Accrued premiums and receivables on credit and other swaps	4,187	4,022
Unrealized gain on credit and other swaps, at fair value	606	73,330
Fixed assets and software costs, net	5,036	5,510
Debt issuance costs, net	6,965	7,399
Other assets	3,872	1,957
Total assets	$ 888,646	$ 902,468
Liabilities and shareholders’ equity		
Accounts payable and accrued expenses	$ 2,182	$ 2,854
Accrued compensation	5,957	8,800
Interest payable	831	625
Unrealized loss on credit and other swaps, at fair value	544,731	2,931
Accrued premiums and payables on credit and other swaps	1,770	44
Trading account liabilities	—	1,002
Long-term debt	325,904	325,000
Restructuring liabilities	1,709	—
Other liabilities	503	600
Total liabilities	883,587	341,856
Preferred securities of subsidiary	98,521	98,521
Commitments and contingencies		
Shareholders’ equity (deficit)		
Common shares, $0.08 par value, 62,500,000 shares authorized, 45,035,593 and 43,380,893 shares issued and outstanding at December 31, 2007 and 2006	3,603	3,470
Additional paid-in-capital	280,224	269,420
Warrants	—	612
Accumulated other comprehensive loss	(4,712)	(2,375)
Retained earnings (deficit)	(372,577)	190,964
Total shareholders’ equity (deficit)	(93,462)	462,091
Total liabilities, preferred securities of subsidiary and shareholders’ equity	$ 888,646	$ 902,468

See accompanying notes.

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Primus Guaranty, Ltd.
Consolidated Statements of Operations
(in thousands except per share amounts)

Year Ended December 31,	2007	2006	2005
Revenues			
Net credit swap revenue (loss)	$ (535,064)	$ 116,083	$ 23,106
Premiums earned on financial guarantees	—	400	405
Asset management and advisory fees	3,481	1,263	190
Interest income	41,847	28,374	16,047
Other trading revenue (loss)	(2,689)	1,770	—
Foreign currency revaluation loss	(107)	(26)	(1,546)
Total net revenues (losses)	(492,532)	147,864	38,202
Expenses			
Compensation and employee benefits	22,450	21,512	15,935
Professional and legal fees	4,948	5,147	4,534
Depreciation and amortization	1,748	2,517	2,123
Technology and data	4,620	2,427	1,630
Interest expense	20,729	10,849	2,660
Restructuring costs	3,022	—	—
Other	5,872	4,796	3,326
Total expenses	63,389	47,248	30,208
Distributions on preferred securities of subsidiary	7,568	5,683	3,865
Income (loss) before provision for income taxes	(563,489)	94,933	4,129
Provision for income taxes	52	42	46
Net income (loss) available to common shares	$ (563,541)	$ 94,891	$ 4,083
Income (loss) per common share:			
Basic	$ (12.58)	$ 2.19	$ 0.09
Diluted	$ (12.58)	$ 2.13	$ 0.09
Average common shares outstanding:			
Basic	44,808	43,306	43,150
Diluted	44,808	44,472	44,645

See accompanying notes.

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Primus Guaranty, Ltd.
Consolidated Statements of Shareholders' Equity
(in thousands)

Year Ended December 31,	2007	2006	2005
Common shares			
Balance at beginning of year	$ 3,470	$ 3,454	$ 3,422
Conversion of warrants to common shares	113	—	—
Shares repurchased and retired	—	—	(15)
Shares vested under employee compensation plans	15	12	42
Issuance of common shares from exercise of options	5	4	5
Balance at end of year	3,603	3,470	3,454
Additional paid-in-capital			
Balance at beginning of year	269,420	265,966	264,973
Conversion of warrants to common shares	7,834	—	—
Shares repurchased and retired	(1,316)	(793)	(3,139)
Shares vested under employee compensation plans	3,733	3,642	3,644
Issuance of common shares from exercise of options	553	605	488
Balance at end of year	280,224	269,420	265,966
Warrants			
Balance at beginning of year	612	612	612
Conversion of warrants to common shares	(612)	—	—
Balance at end of year	—	612	612
Accumulated other comprehensive loss			
Balance at beginning of year	(2,375)	(4,254)	—
Foreign currency translation adjustments	(18)	203	—
Change in unrealized holding gains (losses) on available-for-sale securities	(2,319)	1,676	(4,254)
Balance at end of year	(4,712)	(2,375)	(4,254)
Retained earnings (deficit)			
Balance at beginning of year	190,964	96,073	91,990
Net income (loss)	(563,541)	94,891	4,083
Balance at end of year	(372,577)	190,964	96,073
Total shareholders' equity (deficit) at end of year	$ (93,462)	$ 462,091	$ 361,851
Comprehensive income (loss)			
Net income (loss)	$ (563,541)	$ 94,891	$ 4,083
Foreign currency translation adjustments	(18)	203	—
Change in unrealized gains (losses) on available-for-sale investments	(2,319)	1,676	(4,254)
Comprehensive income (loss)	$ (565,878)	$ 96,770	$ (171)

See accompanying notes.

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Primus Guaranty, Ltd.
Consolidated Statements of Cash Flows
(in thousands)

Year Ended December 31,	2007	2006	2005
Cash flows from operating activities			
Net income (loss)	$ (563,541)	$ 94,891	$ 4,083
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Non-cash items included in net income (loss):			
Depreciation and amortization	1,748	2,517	2,123
Share compensation	3,748	3,654	3,686
Net unrealized (gain) loss on credit swap portfolio	614,524	(48,578)	24,437
Net amortization of premium and discount on securities	(8,245)	(4,243)	—
Restructuring costs	3,022	—	—
Loss on disposal of assets	—	25	—
Amortization of debt issuance costs	311	166	64
Distributions on preferred securities of subsidiary	7,568	5,683	3,865
Increase (decrease) in cash resulting from changes in:			
Accrued interest receivable	(1,310)	(1,247)	(3,746)
Accrued premiums and interest receivable on credit and other swaps	(165)	(561)	85
Other assets	(1,205)	(447)	452
Trading account assets	14,537	(14,537)	—
Accounts payable and accrued expenses	(549)	(81)	2,117
Accrued compensation	(1,665)	3,967	(484)
Trading account liabilities	(1,002)	1,002	—
Interest payable	206	221	40
Accrued premiums and payables on credit swaps	1,726	—	—
Restructuring liabilities	(911)	—	—
Other liabilities	(97)	(273)	(425)
Net cash provided by operating activities	68,700	42,159	36,297
Cash flows from investing activities			
Fixed asset purchases and capitalized software costs	(2,805)	(3,059)	(1,019)
Cash receipts on CLO investment	981	—	—
Purchases of available-for-sale and other investments	(743,752)	(261,045)	(755,659)
Maturities and sales of available-for-sale investments	715,977	242,200	352,359
Net cash used in investing activities	(29,599)	(21,904)	(404,319)
Cash flows from financing activities			
Repurchase and retirement of common shares	(1,170)	(793)	(3,154)
Proceeds from employee exercise of options	557	609	493
Proceeds from exercise of warrants	7,335	—	—
Proceeds from issuance of debt	—	125,000	125,000
Debt issuance costs	—	(4,518)	(2,086)
Net preferred distributions of subsidiary	(7,568)	(5,683)	(3,865)
Net cash provided by (used in) financing activities	(846)	114,615	116,388
Net effect of exchange rate changes on cash	(18)	203	—
Net increase (decrease) in cash	38,237	135,073	(251,634)
Cash and cash equivalents at beginning of year	204,428	69,355	320,989
Cash and cash equivalents at end of year	$ 242,665	$ 204,428	$ 69,355
Supplemental disclosures			
Cash paid for interest	$ 20,212	$ 10,461	$ 2,572
Cash paid for taxes	53	90	4

See accompanying notes.

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Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

1. Organization and Business

Primus Guaranty, Ltd., together with its consolidated subsidiaries (‘‘Primus Guaranty’’ or ‘‘the Company’’), is a Bermuda holding company that conducts business through several operating subsidiaries, including Primus Financial Products, LLC (‘‘Primus Financial’’), Primus Asset Management, Inc. (‘‘Primus Asset Management’’), Harrier Credit Strategies Master Fund, LP (‘‘Harrier’’) and PRS Trading Strategies, LLC (‘‘PRS Trading Strategies’’).

Primus Financial is a Credit Derivative Product Company (‘‘CDPC’’), which is a ‘‘AAA/Aaa’’ rated seller of credit swaps to banks and credit swap dealers, referred to as counterparties, against primarily investment grade credit obligations of corporate and sovereign issuers. In exchange for a fixed quarterly premium Primus Financial agrees, upon the occurrence of a defined credit event (e.g., bankruptcy, failure to pay or restructuring) affecting a designated issuer, referred to as a Reference Entity, to pay its counterparty an agreed upon notional amount against delivery to Primus Financial of the Reference Entity’s debt obligation in the same notional amount. Credit swaps related to a single specified Reference Entity are referred to as ‘‘single name credit swaps.’’ Primus Financial seeks to minimize the risk inherent in its credit swap portfolio by maintaining a high quality, diversified credit swap portfolio across Reference Entities, industries, countries and rating grades. Primus Financial also sells credit swaps referencing portfolios containing obligations of multiple Reference Entities, which are referred to as ‘‘tranches’’ and sells credit swaps referencing residential mortgage-backed securities, which are referred to as ABS. Defined credit events related to ABS may include any or all of the following: failure to pay principal, write-down in the reference obligation and downgrades to CCC or below of the reference obligation.

Primus Asset Management, Inc., or Primus Asset Management, acts as an investment manager to affiliated companies and third party entities. It currently manages the credit swap and cash investment portfolios of its affiliate, Primus Financial. On July 10, 2007, the offering of Primus CLO II, Ltd on behalf of third parties was completed. Primus Asset Management added approximately $400 million to its existing assets under management. With the completion of this new CLO, Primus Asset Management now manages two CLO’s. A CLO issues securities backed by a diversified pool of primarily below investment grade rated senior secured loans of corporations. Additionally, Primus Asset Management manages three investment grade Collateralized Swap Obligations or CSO’s on behalf of third parties. A CSO issues securities backed by one or more credit swaps sold against a diversified pool of investment grade corporate or sovereign reference entities. Primus Asset Management receives fees from third party entities for its investment management services on the five transactions totaling $1.6 billion of assets currently under management. Primus Asset Management has entered into a Services Agreement with its affiliates, whereby it provides services to its affiliates including management, consulting and information technology.

In January 2006, PRS Trading Strategies, LLC (‘‘PRS Trading Strategies’’) commenced operations to trade in a broad range of fixed income products, including credit default swaps, investment grade and high yield bonds, as well as leveraged loans. This was part of Primus Asset Management’s strategy to expand its asset management business. In April 2007, Primus Guaranty formed Harrier Credit Strategies Master Fund, LP (‘‘Harrier’’), a Cayman Islands exempted limited partnership to enable it to more efficiently raise capital from third party investors. During the second quarter of 2007, Primus Guaranty transferred the trading portfolio of its subsidiary, PRS Trading Strategies to Harrier. Harrier traded in an expanded range of fixed income products from PRS Trading, including credit swaps, total return swaps on loan transactions, CDS Indices, leveraged loans and investment grade and non-investment grade securities.

During the fourth quarter of 2007, the Company decided to discontinue Harrier, due in part to Harrier's performance and difficulty in raising third-party capital, given the market environment at that time. As a result of this decision, in the fourth quarter of 2007, the Company recorded restructuring costs of $3.0 million. Of the total restructuring costs, approximately $2.2 million was in

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connection with the write-off of certain software and technology assets and approximately $0.8 million related to net employee termination benefits. As of December 31, 2007, significantly all of Harrier's trading positions have been closed.

Primus Re, Ltd. (''Primus Re''), is a Bermuda company that operates as a financial guaranty insurance company and is licensed as a Class 3 Insurer under the Bermuda Insurance Act of 1978. Primus Re's business is to act as a conduit, or transformer, between parties interested in buying or selling protection in insurance form and other parties interested in assuming the opposite risk position in the form of credit swaps. Primus Re was inactive during the year ended December 31, 2007. On December 31, 2006, the three-year financial guarantee insurance contracts written by Primus Re expired.

Primus Guaranty (UK), Ltd. (''PGUK'') was incorporated in England to expand the Company's presence and further develop its business and relationships across Europe. On January 9, 2008, PGUK was authorized by the United Kingdom's Financial Services Authority.

2. Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include the accounts of Primus Guaranty, Ltd. and its subsidiaries and are presented in accordance with U.S. generally accepted accounting principles (''GAAP''). Significant intercompany transactions have been eliminated in consolidation.

The consolidated financial statements represent a single reportable segment, as defined in Statement of Financial Accounting Standards (''SFAS'') No. 131, Disclosures about Segments of an Enterprise and Related Information.

The consolidated financial statements are presented in U.S. dollar equivalents. During the periods presented, the Company's credit swap activities were conducted in U.S. dollars and euros.

Certain prior year amounts have been reclassified to conform to current year presentation. There was no effect on net income (loss) as a result of these reclassifications.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Management's estimates and assumptions are used mainly in estimating the fair value of credit swaps and the deferred tax asset valuation.

Cash and Cash Equivalents

Primus Guaranty defines cash equivalents as short term, highly liquid securities and interest earning deposits with maturities at time of purchase of 90 days or less.

Investments

The Company accounts for its investments classified as debt securities and fixed maturity securities in accordance with SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities (SFAS 115) and Emerging Issues Task Force (''EITF'') Issue No. 99-20, Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets (EITF 99-20). The Company's management determines the appropriate classification of securities at the time of purchase and are recorded in the consolidated statements of financial

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condition on the trade date. The Company has certain debt securities and fixed maturity securities that are classified as available-for-sale investments. Available-for-sale investments have maturities at time of purchase greater than 90 days. Available-for-sale investments are carried at fair value with the unrealized gains or losses, net of tax, reported in accumulated other comprehensive loss as a separate component of shareholders' equity. The Company does not have any investments classified as held-to-maturity.

Interest Income

The Company earned interest income on its cash and cash equivalents, available-for-sale securities, which include U.S. government agency obligations, the Company's investment in CLO's and trading account assets, which included corporate and sovereign bonds.

Other trading revenue (loss)

Other trading revenue (loss) comprises of the net trading gains or losses from Harrier/PRS Trading. Other trading revenue (loss) includes the realized and unrealized gains or losses on total return swaps on loan transactions, corporate and sovereign bonds and the net interest earned on the total return swaps and from loans in the warehousing period.

Credit Swaps

Credit swaps are over-the-counter (''OTC'') derivative financial instruments and are recorded at fair value in accordance with SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities. Obtaining the fair value (as such term is defined in SFAS No. 133) for such instruments requires the use of management's judgment. These instruments are valued using pricing models based on the net present value of expected future cash flows and observed prices for other OTC transactions bearing similar risk characteristics. The fair value of these instruments appears on the consolidated statement of financial condition as unrealized gains or losses on credit and other swaps. The Company does not believe that its credit swaps fall outside the scope of the guidance of SFAS No. 133 paragraph 10d, as amended by SFAS No. 149, Amendment of Statement 133 on Derivative Instruments and Hedging Activities, because there is no contractual requirement that the protection purchaser be exposed to the underlying risk.

Net credit swap revenue (loss) includes realized and unrealized gains and losses on credit swaps and net premiums earned. Premiums are recognized as income as they are earned over the life of the transaction.

Foreign Currency Translation

Assets and liabilities denominated in non-U.S. dollar currencies are translated into U.S. dollar equivalents at exchange rates prevailing on the date of the consolidated statements of financial condition. Revenues and expenses are translated at average exchange rates during the period. The gains or losses resulting from translating foreign currency financial statements into U.S. dollars, are included in accumulated other comprehensive loss, a component of shareholders' equity. Gains and losses resulting from currency transactions to U.S. dollar equivalents are reflected in the foreign currency revaluation loss caption in the consolidated statements of operations.

Variable Interest Entities

In January 2003, the Financial Accounting Standards Board (‘‘FASB’’) issued FASB Interpretation 46, Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51 (FIN46). In December 2003, the FASB issued a revision of FIN46 to address certain technical corrections and implementation issues (FIN46R). Under FIN46R, a variable interest entity or VIE is defined as an

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entity that: (1) has an insufficient amount of equity investment to carry out its principal activities without additional subordinated financial support; (2) has a group of equity owners that are unable to make significant decisions about its activities; or (3) has a group of equity owners that do not have the obligation to absorb losses or the right to receive returns generated by the entity.

In accordance with FIN46R, the Company is required to consolidate the variable interest entity if it is determined to be the primary beneficiary. The primary beneficiary of the VIE, is the party that absorbs a majority of the entity's expected losses, receives a majority of the entity's expected residual returns, or both. The Company may be involved with various entities in the normal course of business that may be deemed to be VIE's and may hold interests therein, including debt securities and derivative instruments that may be considered variable interests. Transactions associated with these entities include structured financing arrangements, including collateralized loan obligations.

The Company determines whether it is the primary beneficiary of a VIE by performing a qualitative analysis of the VIE that includes a review of, among other factors, its capital structure, contractual terms, which interests create or absorb variability, related party relationships and the design of the VIE. When the primary beneficiary cannot be identified through a qualitative analysis, the Company performs a quantitative analysis, which computes and allocates expected losses or expected residual returns to variable interest holders. Under this method, the Company calculates its share of the VIE's expected losses and expected residual returns using the specific cash flows that would be allocated to it, based on the contractual arrangements and the Company's position in the VIE's capital structure, under various probability-weighted scenarios.

Property, Plant and Equipment

Fixed assets are stated at cost less accumulated depreciation and amortization. Fixed assets include computers, office and telephone equipment and furniture and fixtures, which are depreciated using a straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized using the straight-line method over the shorter of the lease term or estimated useful life.

Internal Use Software Costs

In accordance with Statement of Position SOP 98-1, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use (Statement 98-1), the Company capitalizes qualifying computer software costs. The Company amortizes capitalized internal use software costs using the straight-line method over the estimated useful lives of five years.

Deferred Debt Issuance Costs

The Company has incurred costs in connection with its debt issuances. These costs are capitalized as debt issuance costs in the consolidated statements of financial condition and are being amortized over the life of the related debt arrangement which ranges from fifteen to thirty years, from the date of issuance. Amortization of debt issuance costs are included in interest expense in the consolidated statements of operations.

Income Taxes

Income tax expense is computed in accordance with the requirements of SFAS No. 109, Accounting for Income Taxes, which prescribes the asset and liability approach to accounting for income taxes. The asset and liability approach requires the recognition of deferred tax liabilities and assets for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. The Company establishes a valuation allowance against deferred tax assets when it is more likely than not that some portion or all of those deferred tax assets will not be realized.

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Share-Based Compensation

Effective January 1, 2006, the Company adopted SFAS No. 123(R), Share-Based Payment, using the modified prospective transition method. SFAS No. 123(R) requires the measurement and recognition of compensation expense for all share-based payment awards made to employees and directors including employee options and other forms of equity compensation based on estimated fair values.

Share compensation expense is recognized based on the fair value of options, performance shares and restricted share units (''RSU'') as determined on the date of grant and is being expensed over the related vesting period. The fair value of the options granted is determined using the Black-Scholes option-pricing model. Upon the adoption of SFAS No. 123(R), the Company continues to apply the Black-Scholes option pricing model for determining the estimated fair value for share awards as it deems it to be the most appropriate model. The use of the Black-Scholes model requires certain estimates for values of variables used in the model. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. Share compensation expense is included in compensation and employee benefits in the consolidated statements of operations. See note 17 for further discussion.

Recent Accounting Pronouncements

In April 2006, the FASB issued FASB Staff Position FIN 46(R)-6, Determining the Variability to Be Considered in Applying FASB Interpretation No. 46(R) (''FSP FIN 46(R)-6''). FSP FIN 46(R)-6 addresses how variability should be considered when applying FIN 46(R). Variability affects the determination of whether an entity is a variable interest entity (VIE), which interests are variable interests, and which party, if any, is the primary beneficiary of the VIE required to consolidate. FSP FIN 46(R)-6 clarifies that the design of the entity also should be considered when identifying which interests are variable interests. The Company adopted FSP FIN 46(R)-6 during the third quarter of 2006 and applied it prospectively to all entities in which the Company first became involved with. The adoption of FSP FIN 46(R)-6 did not have a material effect on the Company's consolidated financial statements.

In June 2006, the FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109 (''FIN 48''). FIN 48 prescribes a recognition threshold and measurement attributes for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. Effective January 1, 2007, the Company adopted FIN48. The adoption of FIN 48 did not have a material effect on the Company's consolidated financial statements. See note 11 of notes to consolidated financial statements for further discussion.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (''SFAS No. 157''). SFAS 157 defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. The Company has determined that the adoption of SFAS No. 157 will not have a material impact on its consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Liabilities (''SFAS No. 159''). SFAS No. 159 provides a fair value option election that allows companies to irrevocably elect fair value as the initial and subsequent measurement attribute for certain financial assets and liabilities, with changes in fair value recognized in earnings as they occur. SFAS No. 159 permits the fair value option election on an instrument by instrument basis at initial recognition of an asset or liability or upon an event that gives rise to a new basis of accounting for that instrument. SFAS No. 159 is effective as of the beginning of an entity’s first fiscal year that begins

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after November 15, 2007. The Company has determined that the adoption of SFAS No. 159 will not have a material impact on its consolidated financial statements.

3. Cash and Cash Equivalents

As of December 31, 2007 and 2006, the Company’s cash and cash equivalents included U.S. government agency obligations (including government-sponsored enterprises) rated AAA and Aaa by the respective rating agencies, interest bearing bank deposits, commercial paper and money market funds. All outstanding obligations in this category mature within 90 days. Cash and cash equivalents were $242.7 million and $204.4 million at December 31, 2007 and 2006, respectively.

4. Available-for-sale investments

Available-for-sale investments include U.S. government agency obligations (including government-sponsored enterprises) rated AAA and Aaa by the respective rating agencies, commercial paper rated A-1 and P-1 by the respective rating agencies and the Company’s collateralized loan obligations or CLO investments. The Company accounts for its CLO investments as debt securities and fixed maturity securities in accordance with SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities (SFAS 115) and Emerging Issues Task Force (‘‘EITF’’) Issue No. 99-20, Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets (EITF 99-20). Accordingly, the CLO investments are classified as available-for-sale investments. Available-for-sale investments are carried at fair value with the unrealized gains or losses reported in accumulated other comprehensive loss as a separate component of shareholders’ equity. Available-for-sale investments have maturities at time of purchase greater than 90 days.

The following table summarizes the composition of the Company’s available-for-sale investments at December 31, 2007 and 2006 (in thousands):

December 31, 2007	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
U.S government agency obligations	$ 607,663	$ 480	$ (169)	$ 607,974
Collateralized loan obligations	14,880	—	(5,223)	9,657
Total	$ 622,543	$ 480	$ (5,392)	$ 617,631

December 31, 2006	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
U.S government agency obligations	$ 554,691	$ 89	$ (2,551)	$ 552,229
Commercial paper	26,275	1	—	26,276
Collateralized loan obligation	6,536	—	(130)	6,406
Total	$ 587,502	$		

90	$ (2,681)	$ 584,911
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The following table summarizes the fair value of investments that have been in a continuous unrealized loss position for less than 12 months and for 12 months or more at December 31, 2007 and 2006 (in thousands):

December 31, 2007						
Securities with Unrealized Losses	Less than 12 months		12 months or more		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. government agency obligations	$ 127,139	$ (59)	$ 104,600	$ (110)	$ 231,739	$ (169)
Collateralized loan obligations	5,302	(3,065)	4,355	(2,158)	9,657	(5,223)
Total	$ 132,441	$ (3,124)	$ 108,955	$ (2,268)	$ 241,396	$ (5,392)

December 31, 2006						
Securities with Unrealized Losses	Less than 12 months		12 months or more		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. government agency obligations	$ 19,978	$ (90)	$ 331,709	$ (2,461)	$ 351,687	$ (2,551)
Collateralized loan obligation	6,406	(130)	—	—	6,406	(130)
Total	$ 26,384	$ (220)	$ 331,709	$ (2,461)	$ 358,093	$ (2,681)

The Company makes an assessment to determine whether unrealized losses reflect declines in value of securities that are other-than-temporarily impaired. The Company considers many factors including the length of time and significance of the decline in fair value; the Company’s intent and ability to hold the investment for a sufficient period of time for a recovery in fair value; recent events specific to the issuer or industry; credit ratings and asset quality of collateral structure; and any significant changes in estimated cash flows. If the Company, based on its evaluation of the above factors, determines that the impairment is other-than-temporary, the carrying value of the security is written down to fair value and the unrealized loss is recognized through a charge to earnings in the consolidated statements of operations. Based on the Company’s evaluation, it does not consider these investments to be other-than-temporarily impaired at December 31, 2007 and 2006.

The U.S. government agency obligations mature before November 2008. The two CLO investments are scheduled to mature in 2019 and 2021, respectively, although the actual maturity of each may be sooner.

5. Trading account assets and liabilities

Trading account assets include debt securities held for trading purposes that the Company owns (long positions). Trading account liabilities include debt securities that the Company has sold to other parties but does not own (short positions). The Company is obligated to purchase securities at a future date to cover the short positions.

During the fourth quarter of 2007 the Company decided to discontinue Harrier, a fund formed in April 2007. As a result, during the fourth quarter of 2007, all debt security positions were closed by December 31, 2007.

During 2007 and 2006, Harrier/PRS Trading Strategies purchased and sold corporate and sovereign bonds for trading purposes. Trading positions were carried at fair value on the consolidated statements of financial condition, with unrealized gains or losses recorded in the consolidated statements of operations. At December 31, 2006, the fair value of these trading account assets and trading account liabilities was approximately $14.5 million and $1.0 million, respectively.

Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

6. Credit Swap Revenues and Portfolio

Overview

Net credit swap revenue (loss) as presented in the consolidated statements of operations comprises changes in the fair value of credit swaps, realized gains or losses on the termination of credit swaps and premium income or expense. The realized gains and losses on credit swaps represent realized gains and losses on the termination of credit swaps. The realization of gains or losses on credit swaps will generally result in a reduction in unrealized gains or losses and accrued premium at the point in time realization occurs.

Credit swaps are derivative transactions that obligate one party to the transaction (the ‘‘Seller’’) to pay an amount to the other party to the transaction (the ‘‘Buyer’’) should an unrelated third party or portfolio of third parties (the ‘‘Reference Entity’’) specified in the contract be subject to one of a specified group of events (‘‘credit events’’). The amount to be paid by the Seller will either be (a) the notional amount of the transaction, in exchange for which the Seller must be delivered a defined obligation of the Reference Entity (called physical settlement), or (b) the difference between the current market value of a defined obligation of the Reference Entity and the notional amount of the transaction (called cash settlement). In exchange for taking the risk of the contract, the Seller will receive a fixed premium for the term of the contract (or until the occurrence of a defined credit event). The fixed premium is generally paid quarterly in arrears over the term of the transaction. Premium income is recognized ratably over the life of the transaction as a component of net credit swap revenue (loss). When the Company purchases credit swaps from its counterparties, the Company pays fixed premiums over the term of the contract. Premium expense is recognized ratably over the life of the transaction as a component of net credit swap revenue (loss).

All credit swap transactions entered into between the Buyer and the Seller are subject to an International Swaps and Derivatives Association, Inc. Master Agreement or (‘‘ISDA Master Agreement’’) executed by both parties. The ISDA Master Agreement allows for the aggregation of the market exposures and termination of all transactions between the Buyer and Seller in the event a default (as defined by the ISDA Master Agreement) occurs in respect of either party.

The primary risks inherent in the Company’s activities are (a) where the Company is a Seller that Reference Entities specified in its credit swap transactions will experience credit events that will require the Company to make payments to the Buyers of the transactions. Defined credit events may include any or all of the following: bankruptcy, failure to pay, repudiation or moratorium, and modified or original restructuring, (b) where the Company is a Buyer of a credit swap and a defined credit event occurs, the Seller fails to make payment to the Company, and (c) that Buyers of the transactions from the Company will default on their required premium payments. Defined credit events related to the Company’s credit swaps against ABS may include any or all of the following: failure to pay principal, write-down in the reference obligation and distressed ratings downgrade of the reference obligation. See note 20 for further discussion.

The Company terminates a credit swap in one of two ways. The Company may negotiate an agreed termination with the original counterparty (an unwind). The Company may negotiate an assignment and novation of its rights and obligations under the credit swap to a third party (an assignment). In the event of an unwind or assignment, the Company pays or receives a cash settlement negotiated with the counterparty or assignee, based on the fair value of the credit swap contract and the accrued premium on the swap contract at the time of negotiation. The amounts the Company pays or receives are recorded as a realization of fair value and as a realization of accrued premiums in the period in which the termination occurs.

In accordance with accounting principles generally accepted in the United States, the Company carries its credit swaps on its consolidated statements of financial condition at their fair value. Changes in the fair value of the Company's credit swap portfolio are recorded as unrealized gains or losses as a

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component of net credit swap revenue (loss) in the Company's consolidated statements of operations. If a credit swap has an increase or decline in fair value during a period, the increase will add to the Company's net credit swap revenue and the decline will subtract from the Company's net credit swap revenue for that period, respectively. Changes in the fair value of the Company's credit swap portfolio are a function of the notional amount and composition of the portfolio and prevailing market credit swap premiums for comparable credit swaps. The Company generally holds the credit swaps it sells to maturity, at which point, assuming no defined credit event has occurred, the cumulative unrealized gains and losses on each credit swap would equal zero.

Primus Financial and Harrier each enters into valid ISDA Master Agreements with their counterparties and each entity aggregates their respective transactions on a counterparty basis for presentation on the Company's consolidated statements of financial condition. If the aggregate total of fair values with a counterparty is a net gain, the total is recorded as a component of unrealized gains on credit swaps, at fair value in the consolidated statements of financial condition. If the aggregate total of fair values with a counterparty is a net loss, the total is recorded as a component of unrealized losses on credit and other swaps, at fair value in the consolidated statements of financial condition.

Primus Financial

Under the terms of Primus Financial's operating guidelines, derivatives transactions can only include credit swaps.

Primus Financial is primarily a Seller of credit swaps. As a general rule, when Primus Financial sells credit swaps, it intends to hold the transaction until maturity. However, there are two sets of circumstances in which the Company could elect to terminate transactions prior to maturity, and the Company monitors its portfolio on a continuing basis to assess whether those circumstances are present.

First, whenever Primus Financial receives new information suggesting that the credit quality of the underlying risk has deteriorated to a material degree, the Company considers the possibility of terminating the transaction, usually at a loss, to avoid the larger loss that could result if the credit swap were to remain in place until a defined credit event occurs.

Second, Primus Financial may elect to terminate a transaction for which it has an unrealized gain or loss based on one or more of the following considerations: the likelihood of further gains or losses arising from the position, its view as to whether the capital dedicated to the position could be profitably reallocated, its total exposure to a particular Reference Entity, the total size of its portfolio in relation to its capital and the total size of its swap positions and exposures with a particular counterparty which might be reduced so that the counterparty may enter into additional swaps with Primus Financial.

Harrier/PRS Trading Strategies

In April 2007, Primus Guaranty formed Harrier, a Cayman Islands exempted limited partnership. During the second quarter of 2007, Primus Guaranty transferred the trading portfolio of PRS Trading Strategies to Harrier. Harrier traded in a broad range of fixed income products, including credit swaps, total return swaps on loan transactions, leveraged loans and investment grade and non-investment grade securities. At December 31, 2007, Harrier has closed substantially all of its credit swap positions.

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Consolidated Net Credit Swap Revenue (Loss) and Credit Swap Portfolio Information

The tables below present the components of consolidated net credit swap revenue (loss) for the years ended December 31, 2007, 2006 and 2005 (in thousands):

Years ended December 31,	2007	2006	2005
Net premium income	$ 84,771	$ 69,408	$ 52,705
Net realized losses	(5,190)	(1,769)	(5,162)
Change in unrealized gains (losses)	(614,645)	48,444	(24,437)
Total net credit swap revenue (loss)	$ (535,064)	$ 116,083	$ 23,106

The table below, in thousands, represent the Company's consolidated notional amount, fair value and average fair value of open credit swap transactions entered into with third parties at December 31, 2007 and 2006 (excluding CDS index and index tranches and total return swaps transacted by PRS Trading Strategies with net fair values of $48 thousand as of December 31, 2006):

	December 31, 2007	December 31, 2006
Gross Notional Amounts:		
Credit swaps sold-single name	$ 18,260,653	$ 15,485,145
Credit swaps sold-tranche	4,700,000	500,000
Credit swaps sold-ABS	80,000	15,000
Credit swaps purchased-single name	(25,410)	(147,597)
Fair value:		
Asset	606	73,281
Liability	544,731	2,930
Average fair value:		
Asset	33,217	57,433
Liability	165,087	1,990

''Asset'' in the table above represents unrealized gains on credit swaps while ''Liability'' represents unrealized losses on credit swaps. All credit swaps are subject to netting arrangements that have been contractually established independently by Primus Financial and Harrier with each of their counterparties under an ISDA Master Agreement. The notional amounts of the credit swap contracts in the preceding table are presented on a gross basis and the fair values of such contracts are netted by counterparty.

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The tables that follow summarize in thousands, by credit rating of Reference Entities and of counterparties, the notional amounts and fair values of credit swap transactions outstanding for the Company as of December 31, 2007 and 2006 (excluding CDS index and index tranches and total return swaps transacted by PRS Trading Strategies with net fair values of $48 thousand as of December 31, 2006):

	December 31, 2007		December 31, 2006	
Moody's Rating Category	Notional Amount	Fair Value	Notional Amount	Fair Value
By Single Name Reference Entity/Tranche				
Credit Swaps Sold-Single Name:				
Aaa	$ 828,504	$ (3,953)	$ 761,211	$ 1,483
Aa	3,832,904	(91,863)	2,690,166	9,364
A	6,047,762	(36,544)	6,075,786	29,501
Baa	6,882,813	(22,162)	5,427,937	32,786
Ba	570,090	(17,235)	470,842	1,467
B	71,080	(2,390)	59,203	(706)
Caa	27,500	(2,791)	—	—
Total	$ 18,260,653	$ (176,938)	$ 15,485,145	$ 73,895
Credit Swaps Sold-Tranche:				
Aaa	$ 3,450,000	$ (172,175)	$ —	$ —
Aa	950,000	(94,312)	300,000	(2,494)
A	300,000	(53,569)	200,000	(534)
Total	$ 4,700,000	$ (320,056)	$ 500,000	$ (3,028)
Credit Swaps Sold-ABS(1):				
A	$ 25,000	$ (12,821)	$ 10,000	$ (15)
Baa	35,000	(20,470)	5,000	(8)
Ba	15,000	(11,353)	—	—
B	5,000	(4,038)	—	—
Total	$ 80,000	$ (48,682)	$ 15,000	$ (23)
Credit Swaps Purchased-Single Name:				
Aa	$ (8,160)	$ 403	$ (15,000)	$ (15)
A	(12,380)	335	(36,000)	(10)
Baa	(4,870)	813	(83,636)	(484)
Ba	—	—	(6,961)	235
B	—	—	(6,000)	(219)
Total	$ (25,410)	$ 1,551	$ (147,597)	$ (493)
By Counterparty Buyer / (Seller)				
Credit Swaps Sold-Single Name:				
Aaa	$ 3,625,845	$ (34,091)	$ 982,194	$ 5,003
Aa	12,153,764	(118,109)	12,037,591	57,175
A	2,481,044	(24,738)	2,465,360	11,717
Total	$ 18,260,653	$ (176,938)	$ 15,485,145	$ 73,895

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Moody's Rating Category	December 31, 2007 Notional Amount	December 31, 2007 Fair Value	December 31, 2006 Notional Amount	December 31, 2006 Fair Value
Credit Swaps Sold-Tranche:				
Aaa	$ 400,000	$ (33,706)	$ —	$ —
Aa	3,850,000	(246,490)	500,000	(3,028)
A	450,000	(39,860)	—	—
Total	$ 4,700,000	$ (320,056)	$ 500,000	$ (3,028)
Credit Swaps Sold-ABS:				
Aaa	$ 15,000	$ (10,241)	$ 10,000	$ (15)
Aa	40,000	(21,969)	5,000	(8)
A	25,000	(16,472)	—	—
Total	$ 80,000	$ (48,682)	$ 15,000	$ (23)
Credit Swaps Purchased-Single Name:				
Aaa	$ (5,000)	$ 383	$ (9,961)	$ (120)
Aa	(20,410)	1,168	(137,636)	(373)
Total	$ (25,410)	$ 1,551	$ (147,597)	$ (493)

(1) — See note 20 for further discussion.

S&P Rating Category By Single Name Reference Entity/Tranche	December 31, 2007 Notional Amount	December 31, 2007 Fair Value	December 31, 2006 Notional Amount	December 31, 2006 Fair Value
Credit Swaps Sold-Single Name:				
AAA	$ 1,071,504	$ (32,181)	$ 940,031	$ 1,721
AA	3,704,784	(56,437)	2,275,564	8,845
A	6,550,733	(42,398)	6,490,958	30,644
BBB	6,326,638	(20,200)	5,271,390	32,958
BB	478,820	(14,583)	438,499	1,060
B	128,174	(11,139)	68,703	(1,333)
Total	$ 18,260,653	$ (176,938)	$ 15,485,145	$ 73,895
Credit Swaps Sold-Tranche:				
AAA	$ 3,800,000	$ (212,582)	$ 150,000	$ (2,010)
AA	700,000	(67,998)	200,000	(1,613)
A	100,000	(21,880)	150,000	595
BBB	100,000	(17,596)	—	—
Total	$ 4,700,000	$ (320,056)	$ 500,000	$ (3,028)
Credit Swaps Sold-ABS(1):				
A	$ 50,000	$ (29,921)	$ 15,000	$ (23)
BBB	15,000	(7,242)	—	—
BB	15,000	(11,519)	—	—
Total	$ 80,000	$ (48,682)	$ 15,000	$ (23)

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S&P Rating Category	December 31, 2007 Notional Amount	December 31, 2007 Fair Value	December 31, 2006 Notional Amount	December 31, 2006 Fair Value
Credit Swaps Purchased-Single Name:				
AA	$ (8,160)	$ 403	$ (15,000)	$ (15)
A	(12,250)	765	(56,000)	(10)
BBB	(5,000)	383	(58,636)	(473)
BB	—	—	(13,961)	214
B	—	—	(4,000)	(209)
Total	$ (25,410)	$ 1,551	$ (147,597)	$ (493)
By Counterparty Buyer / (Seller)				
Credit Swaps Sold-Single Name:				
AAA	$ 5,000	$ 3	$ 31,406	$ 104
AA	14,367,841	(131,277)	11,732,030	58,698
A	3,887,812	(45,664)	3,721,709	15,093
Total	$ 18,260,653	$ (176,938)	$ 15,485,145	$ 73,895
Credit Swaps Sold-Tranche:				
AAA	$ —	$ —	$ 100,000	$ (1,335)
AA	4,250,000	(280,196)	400,000	(1,693)
A	450,000	(39,860)	—	—
Total	$ 4,700,000	$ (320,056)	$ 500,000	$ (3,028)
Credit Swaps Sold-ABS:				
AA	$ 55,000	$ (32,210)	$ 15,000	$ (23)
A	25,000	(16,472)	—	—
Total	$ 80,000	$ (48,682)	$ 15,000	$ (23)
Credit Swaps Purchased-Single Name:				
AA	$ (25,410)	$ 1,551	$ (127,995)	$ (665)
A	—	—	(19,602)	172
Total	$ (25,410)	$ 1,551	$ (147,597)	$ (493)

(1) — See note 20 for further discussion.

Primus Financial’s and Harrier’s counterparties are generally financial institutions with whom they have entered into ISDA Master Agreements. For the year ended December 31, 2007, no individual counterparty generated greater than ten percent of the Company’s consolidated net premium revenue. For the year ended December 31, 2006, two counterparties each generated greater than ten percent of the Company’s consolidated net premium revenue.

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Primus Guaranty, Ltd.
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The table below shows the geographical distribution of the Company’s credit swap portfolio by domicile of the Reference Entity and domicile of the counterparty as of December 31, 2007 and 2006 (in thousands):

	December 31, 2007		December 31, 2006	
Country of Domicile	Notional Amount	Fair Value	Notional Amount	Fair Value
Credit Swaps Sold-Single Name				
By Reference Entity:				
North America	$ 9,531,846	$ (149,169)	$ 9,133,328	$ 46,286
Europe	7,837,807	(21,719)	5,612,817	25,097
Pacific	712,000	(4,791)	570,000	1,351
Others	179,000	(1,259)	169,000	1,161
Total	$ 18,260,653	$ (176,938)	$ 15,485,145	$ 73,895
By Counterparty:				
North America	$ 9,431,827	$ (100,747)	$ 7,904,024	$ 36,321
Europe	8,686,826	(75,709)	7,486,121	37,502
Pacific	132,000	(534)	75,000	(17)
Others	10,000	52	20,000	89
Total	$ 18,260,653	$ (176,938)	$ 15,485,145	$ 73,895
Credit Swaps Sold-Tranche				
By Counterparty:				
North America	$ —	$ —	$ 50,000	$ 851
Europe	4,700,000	(320,056)	450,000	(3,879)
Total	$ 4,700,000	$ (320,056)	$ 500,000	$ (3,028)
Credit Swaps Sold-ABS				
By Reference Entity:				
North America	$ 80,000	$ (48,682)	$ 15,000	$ (23)
Total	$ 80,000	$ (48,682)	$ 15,000	$ (23)
By Counterparty:				
North America	$ 45,000	$ (24,418)	$ 10,000	$ (15)
Europe	35,000	(24,264)	5,000	(8)
Total	$ 80,000	$ (48,682)	$ 15,000	$ (23)
Credit Swaps Purchased-Single Name				
By Reference Entity:				
North America	$ (25,410)	$ 1,551	$ (127,000)	$ (491)
Europe	—	—	(20,597)	(2)
Total	$ (25,410)	$ 1,551	$ (147,597)	$ (493)
By Counterparty:				
North America	$ —	$ —	$ (65,563)	$ (362)
Europe	(25,410)	1,551	(82,034)	(131)
Total	$ (25,410)	$ 1,551	$ (147,597)	$ (493)

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The table below shows the distribution of the Company's credit swap portfolio by year of maturity as of December 31, 2007 and 2006 (in thousands). With respect to the credit swaps sold-ABS caption below, the actual maturity date for any contract will vary depending on the level of voluntary prepayments, defaults and interest rates with respect to the underlying mortgage loans. As a result, the actual maturity date for any contract may be earlier or later than the estimated maturity indicated.

	December 31, 2007		December 31, 2006	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Credit Swaps Sold-Single Name				
Year of Maturity				
2007	$ —	$ —	$ 2,432,827	$ 6,589
2008	1,180,401	(302)	1,127,551	6,509
2009	2,723,618	(6,449)	2,739,561	16,964
2010	6,052,998	(56,037)	6,132,240	33,056
2011	2,953,911	(53,905)	3,004,357	10,842
2012	5,309,725	(60,119)	44,609	(41)
2013	40,000	(126)	4,000	(24)
Total	$ 18,260,653	$ (176,938)	$ 15,485,145	$ 73,895
Credit Swaps Sold-Tranche				
Year of Maturity				
2010	$ —	$ —	$ 50,000	$ 851
2012	1,000,000	(6,204)	—	—
2013	350,000	(58,715)	350,000	(2,544)
2014	3,350,000	(255,137)	100,000	(1,335)
Total	$ 4,700,000	$ (320,056)	$ 500,000	$ (3,028)
Credit Swaps Sold-ABS(1)				
Year of Maturity				
2010	$ 10,000	$ (4,632)	$ —	$ —
2011	10,000	(6,368)	5,000	(8)
2012	15,000	(9,322)	5,000	(12)
2013	15,000	(9,443)	5,000	(3)
2014	20,000	(12,438)	—	—
2016	10,000	(6,479)	—	—
Total	$ 80,000	$ (48,682)	$ 15,000	$ (23)
Credit Swaps Purchased-Single Name				
Year of Maturity				
2011	$ —	$ —	$ (96,961)	$ (255)
2012	(5,000)	383	(16,602)	(16)
2013	—	—	(34,034)	(222)
2014	(20,410)	1,168	—	—
Total	$ (25,410)	$ 1,551	$ (147,597)	$ (493)

(1) — See note 20 for further discussion.

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Primus Guaranty, Ltd.
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7. Net Total Return Swap Transactions

During the fourth quarter of 2007 the Company decided to discontinue Harrier, a fund formed in April 2007. As a result, all transactions completed under a total return swap program were closed by December 31, 2007.

During the second quarter of 2006, the Company’s subsidiary, Harrier/PRS Trading Strategies entered into a master agreement for transactions under a total return swap program with a counterparty, which expires in May 2008. Under the terms of the agreement, Harrier/PRS Trading Strategies received interest and other payments based on certain mutually agreed reference loans, and paid financing interest based on the principal amount of such loans. Harrier/PRS Trading Strategies took the risk that the referenced loans deteriorated in value and conversely received the benefit from any appreciation in the value of loans referenced in each total return swap. The net fair value of each swap was determined by the net fair value of the referenced loan. Harrier/PRS Trading Strategies determined the fair value of the swaps based on the estimated cost to close-out the swap positions. The total return swap with the counterparty was documented under an ISDA Master Agreement between Harrier/PRS Trading Strategies and the counterparty. The net fair value of all transactions under the total return swap program was netted with the fair values of any credit swaps outstanding between Harrier/PRS Trading Strategies and the counterparty for presentation in the consolidated statements of financial condition.

The total notional amount of loans outstanding under the total return swaps was $63.2 million at December 31, 2006. The net fair value of the total return swaps was $135 thousand at December 31, 2006.

Revenue generated from the transactions under the total return swap program was recorded in other trading revenue (loss) as presented in the consolidated statements of operations, and comprises changes in the fair value of the total return swaps, realized gains or losses on the termination of the total return swaps, and the net interest earned on the total return swaps.

8. CLO Transactions

Each time the Company is involved in a CLO transaction, the Company performs an analysis to determine whether it is the primary beneficiary and accordingly, would be required to consolidate the SPE in its consolidated financial statements. During 2007, the Company determined, pursuant to FASB Interpretation No. 46 (R), Consolidation of Variable Interest Entities, that it is not the primary beneficiary of Primus CLO II, Ltd. and accordingly, the special purpose entity or SPE will not be consolidated in the Company’s financial statements.

The Company accounts for its CLO investments as debt securities and fixed maturity securities in accordance with SFAS No. 115 and EITF 99-20. Accordingly, the CLO investments are classified as available-for-sale investments. Available-for-sale investments are carried at fair value with the unrealized gains or losses reported in accumulated other comprehensive loss as a separate component of shareholders’ equity.

Revenue generated from the warehouse loan agreements during the warehouse period (the interim period during which the SPE accumulates loans and before the CLO securities are issued) is recorded in other trading revenue (loss), as presented in the condensed consolidated statements of operations. These revenues comprise the Company’s share of net realized losses on the termination of individual loan positions and net interest earned on warehouse loans.

Primus CLO I, Ltd.

On December 19, 2006, the offering of Primus CLO I, Ltd (‘‘CLO I’’, a special purpose entity or SPE) on behalf of third parties was completed. Upon closing, Primus Asset Management added

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Primus Guaranty, Ltd.
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approximately $400 million to its assets under management and is acting as collateral manager of CLO I. Under the terms of the collateral management agreement of CLO I, Primus Asset Management will receive management fees quarterly for managing the selection, acquisition and disposition of the underlying collateral and for monitoring the underlying collateral, subject to the terms of the agreement. The Company has invested $6.5 million for a 25% interest in the Subordinated Notes of CLO I. The Company's ultimate exposure to loss in CLO I is limited to the $6.5 million of its investment in CLO I. During 2007, the Company received a cash return of approximately $1.0 million on its investment in CLO I. The Company has determined that it does not have to consolidate the SPE in the Company's financial statements. At December 31, 2007 and 2006, the fair value of the Company's investment in CLO I was $4.4 million and $6.4 million, respectively. Based on the Company's evaluation, it does not consider its investment in CLO I to be other-than-temporarily impaired at December 31, 2007 and 2006.

Primus CLO II, Ltd.

On July 10, 2007, the offering, Primus CLO II, Ltd. (''CLO II'') on behalf of third parties was completed. Primus Asset Management has added approximately $400 million to its existing assets under management. Primus Asset Management receives management fees quarterly for managing the selection, acquisition and disposition of the underlying collateral and monitoring the underlying collateral, subject to the terms of the agreement. The Company has invested $7.9 million or a 25% interest in the Subordinated Notes of CLO II. The Company's ultimate exposure to loss in CLO II is limited to its investment of $7.9 million. At December 31, 2007, the fair value of the Company's investment in CLO II was $5.3 million. Based on the Company's evaluation, it does not consider its investment in CLO II to be other-than-temporarily impaired at December 31, 2007.

9. Fixed Assets and Internal Use Software Costs

Fixed assets include computer hardware, telephone equipment, furniture and fixtures, and office equipment, which are depreciated using a straight-line method over the estimated useful lives of three to five years, and leasehold improvements which are amortized using the straight-line method over the shorter of the lease term or estimated useful life of ten years. At December 31, 2007 and 2006, fixed assets and internal use software costs consist of the following (in thousands):

	December 31,	
	2007	2006
Asset category		
Furniture and fixtures	$ 1,317	$ 1,137
Computers	1,059	587
Office and telephone equipment	393	335
Leasehold improvements	2,717	2,208
Internal use software costs	15,024	15,418
	20,510	19,685
Less accumulated depreciation and amortization	15,474	14,175
Total fixed assets and internal use software costs	$ 5,036	$ 5,510

The Company recorded depreciation and amortization expense of approximately $1.7 million, $2.5 million and $2.1 million for the years ended December 31, 2007, 2006 and 2005, respectively.

10. Long Term Debt

$125 million Senior Notes

On December 27, 2006, Primus Guaranty, Ltd. completed an offering of $125 million, 7% senior notes, which mature in December 2036. The senior notes are senior unsecured obligations and rank

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Primus Guaranty, Ltd.
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equally with all other unsecured and unsubordinated indebtedness of the Company. The senior notes are also subordinated to all liabilities of Primus Guaranty's subsidiaries. The senior notes are redeemable at the option of Primus Guaranty, in whole or in part, at any time on or after December 27, 2011, at a redemption price equal to 100% of the principal amount to be redeemed, plus any accrued and unpaid interest thereon to the redemption date. Interest on the senior notes is payable quarterly, beginning on March 27, 2007. In connection with the issuance of the senior notes, the Company incurred approximately $4.5 million in capitalized debt issuance costs, which are amortized over the life of the debt. These senior notes are rated BBB+/Baa1 by S&P and Moody's, respectively. Primus Guaranty intends to generally maintain assets available for debt service equivalent to two years' annual debt service on these senior notes.

$125 million Subordinated Deferrable Interest Notes

On December 19, 2005, Primus Financial issued in aggregate $125 million of subordinated deferrable interest notes, consisting of $75 million of Series A notes and $50 million of Series B notes, which mature in June 2021. The notes are subordinated in right of payment to the prior payment in full of all existing and future senior indebtedness of the Company, including counterparty claims and the notes issued in July 2004. The notes are redeemable at the option of Primus Financial, in whole or in part, on any auction date, at a redemption price equal to 100% of the principal amount of the notes to be redeemed, plus any accrued and unpaid interest thereon to the redemption date. The interest rate on the Series A notes and the Series B notes set every 28 days through a monthly auction process. In connection with the above issuance of the subordinated deferrable notes, the Company incurred approximately $2.0 million in debt issuance costs, which are amortized over the life of the debt. These deferrable interest notes are rated AA/Aa2 by S&P and Moody's respectively.

$75 million Subordinated Deferrable Interest Notes

On July 23, 2004, Primus Financial issued $75 million of subordinated deferrable interest notes that mature in July 2034. The notes are subordinated in right of payment to the prior payment in full of all existing and future senior indebtedness of the Company, including counterparty claims. The notes are redeemable at the option of Primus Financial, in whole or in part, on any auction date, at a redemption price equal to 100% of the principal amount of the notes to be redeemed, plus any accrued and unpaid interest thereon to the redemption date. The interest rate on the notes set every 28 days through a monthly auction process. In connection with the above issuance of the subordinated deferrable notes, the Company incurred approximately $1.1 million in debt issuance costs, which are amortized over the life of the debt. These deferrable interest notes are rated AAA/Aaa by S&P and Moody's respectively.

During the second half of 2007, the turbulent market conditions also affected the debt capital markets. Beginning in August 2007, there was limited investor demand for our subordinated deferrable notes issued in the auction rate market. As a result of the insufficient demand, the auctions did not clear and the rates on these subordinated deferrable interest notes were set at the maximum spread rates as specified in the respective security agreements. These maximum rates are subject to increase if the credit ratings on these securities are downgraded. This resulted in higher interest expense during the second half of 2007.

The Company recorded interest expense related to the above debt of approximately $20.7 million, $10.8 million and $2.7 million for the years ended December 31, 2007, 2006 and 2005, respectively. At December 31, 2007, 2006 and 2005, the carrying value of the subordinated deferrable interest notes approximates fair value. At December 31, 2007, the fair value of the $125 million, 7% senior notes was approximately $76.3 million.

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11. Income taxes

Effective January 1, 2007, the Company adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). The adoption of FIN 48 did not have a material effect on the Company's consolidated financial statements.

As of December 31, 2007, and January 1, 2007, the Company did not have any unrecognized tax benefits. The Company's accounting policy with respect to interest and penalties, if any, would be to recognize them in the provision for income taxes in the consolidated statements of operations. The Company did not incur any income tax related interest income, interest expense or penalties for the years ended December 31, 2007 and 2006. The Company does not believe that it is reasonably possible that the total amounts of unrecognized tax benefits will significantly increase within the next 12 months.

Primus Guaranty and certain subsidiaries file income tax returns in the U.S. federal jurisdiction and various state, local and foreign jurisdictions, which are no longer subject to U.S. federal, state, local and foreign income tax examinations by tax authorities for years before 2004. The Company and certain of its subsidiaries are currently undergoing U.S. federal tax audits, but no audit has yet been completed.

Primus Guaranty is a Bermuda company. Primus Guaranty believes that it is not involved in the active conduct of a trade or business in the United States. For U.S. tax purposes, Primus Guaranty will be treated either as a controlled foreign corporation or as a passive foreign investment company by its U.S. shareholders. As such, Primus Guaranty has not provided for any federal or state and local income taxes in its separate financial statements. However, on a consolidated basis, it has provided for income taxes for certain of its subsidiaries, which are described below. Primus Guaranty was incorporated in Bermuda to domicile itself in a jurisdiction that is internationally recognized as a base for financial companies and in a jurisdiction that has an efficient and predictable corporate tax regime. Primus Guaranty does not have any full time employees in, nor does the Company lease or own any real property in Bermuda.

PRS Trading Strategies is a limited liability company organized under Delaware law, with all of its interests being held by Primus Guaranty, a non-U.S. corporation. PRS Trading Strategies is treated as a disregarded entity for U.S. tax purposes, and the results of its operations are treated as the operations of a branch of its foreign parent corporation, Primus Guaranty. As a disregarded entity, PRS Trading Strategies is not itself subject to U.S. net income taxation. In addition, because PRS Trading Strategies' activities in the U.S. are confined to holding investments in debt instruments and credit swaps for its own account, management believes that PRS Trading Strategies' activities fall within the provisions of IRC Section 864(b) and therefore does not believe that Primus Guaranty, a non-U.S. corporation, should be subject to taxation in the U.S. on a net income basis as a result of its interest in PRS Trading Strategies. Accordingly, PRS Trading Strategies, and thus Primus Guaranty, did not provide for any income taxes in its financial statements for this period.

If the activities of PRS Trading Strategies, and thus Primus Guaranty, were found to fall outside the provisions of IRC Section 864(b), and PRS Trading Strategies, and thus Primus Guaranty, were found to be subject to U.S. federal, state and local corporate income tax, it is difficult to predict the exact treatment that would apply to Primus Guaranty and, therefore, to estimate the resulting income tax expense. However, since inception, PRS Trading Strategies has incurred a net cumulative loss and therefore would not be subject to any income tax. This analysis assumes that PRS Trading Strategies is not deemed to be making distributions to Primus Guaranty; such distributions could subject

Primus Guaranty to U.S. branch profits tax.

Harrier is a limited partnership organized under Cayman Islands law, with all of its interests ultimately being held by Primus Guaranty, a non-U.S. corporation. Harrier will be electing to be treated as a disregarded entity for U.S. tax purposes, and the results of its operations will be treated

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as the operations of a branch of its foreign parent corporation, Primus Guaranty. Because Harrier's activities in the U.S. are confined to holding investments in debt instruments and credit swaps for its own account, management believes that Harrier's activities fall within the provisions of IRC Section 864(b) and therefore does not believe that Primus Guaranty, a non-U.S. corporation, should be subject to taxation in the U.S. on a net income basis as a result of its interest in Harrier. Accordingly, Harrier, and thus Primus Guaranty, did not provide for any income taxes in its financial statements for this period.

If the activities of Harrier, and thus Primus Guaranty, were found to fall outside the provisions of IRC Section 864(b), and Harrier, and thus Primus Guaranty, were found to be subject to U.S. federal, state and local corporate income tax, it is difficult to predict the exact treatment that would apply to Primus Guaranty and, therefore, to estimate the resulting income tax expense. However, since inception, Harrier has incurred a net cumulative loss and therefore would not be subject to any income tax. This analysis assumes that Harrier is not deemed to be making distributions to Primus Guaranty; such distributions could subject Primus Guaranty to U.S. branch profits tax.

Primus (Bermuda), Ltd. (''Primus Bermuda'') is a Bermuda company. Primus Bermuda believes that it is not involved in the active conduct of a trade or business in the United States. For U.S. tax purposes, Primus Bermuda will be treated either as a controlled foreign corporation or as a passive foreign investment company by its U.S. shareholders. As such, Primus Bermuda has not provided for any federal or state and local income taxes in its separate financial statements.

Primus Financial is a limited liability company organized under Delaware law, with the controlling interest being held by Primus Group Holdings, LLC (''Primus Group Holdings''), a limited liability company organized under Delaware law and a disregarded entity for U.S. tax purposes. All of the interests in Primus Group Holdings are held by Primus Bermuda, a non-U.S. corporation. Primus Financial is treated as a partnership for U.S. tax purposes. As a result, all of Primus Financial's items of taxable income and expense flow through to its interest-holders for U.S. federal income tax purposes and any taxes that may be attributable to such items are the responsibility of the interest-holders. In addition, because Primus Financial's activities in the U.S. are confined to holding investments in debt instruments and credit swaps for its own account, Primus Financial believes that its activities fall within the provisions of Internal Revenue Code (''IRC'') Section 864(b). Based on the application of the provisions of IRC Section 864(b) and the investment nature of its operations, Primus Financial believes that Primus Bermuda, a non U.S. corporation, will not be subject to U.S. net income taxes with respect to its indirect interest in Primus Financial. Accordingly, Primus Financial, and thus Primus Bermuda, did not provide for any income taxes in its financial statements for this period.

If the activities of Primus Financial, and thus Primus Bermuda, were found to fall outside the provisions of IRC Section 864(b), and Primus Financial, and thus Primus Bermuda, were found to be subject to U.S. federal, state and local corporate income tax, it is difficult to predict the exact treatment that would apply to Primus Bermuda and, therefore, to estimate the resulting income tax expense. However, were Primus Bermuda to be subject to income tax, at a combined U.S. federal, New York State and New York City corporate income tax rate of 46%, on its GAAP income, then its income tax expense or (benefit), excluding interest and penalties, would have been approximately $(248) million for 2007, $49.2 million for 2006 and $3.7 million for 2005. These figures assume that Primus Financial is not deemed to be making distributions to Primus Bermuda; such distributions could subject Primus Bermuda to an additional U.S. federal branch profits tax.

Primus Asset Management has entered into a Services Agreement with its affiliates, whereby Primus Asset Management provides services to its affiliates including management, consulting and information technology. Since Primus Asset Management is a U.S. domiciled corporation it is subject to U.S. income taxes and income taxes of other taxing jurisdictions on fees received from its affiliates.

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The significant components of the consolidated provision for income taxes for the years ended December 31, 2007, 2006 and 2005 were as follows (in thousands):

December 31,	2007	2006	2005
Current:			
Federal	$ —	$ —	$ —
State/City	52	42	46
Total current	52	42	46
Deferred:			
Federal	—	—	—
State/City	—	—	—
Total deferred	—	—	—
Total provision for income taxes	$ 52	$ 42	$ 46

The Company's effective tax rate differs from the Bermudian effective rate of zero percent mainly due to taxation of its U.S. subsidiary, Primus Asset Management, which is subject to U.S. federal income tax at a rate of 35%, as well as U.S. state and local taxes. The Bermuda Minister of Finance has given the Company a tax exemption certificate effective through 2016 that prevents the Company from being subject to tax in the event that any legislation is enacted that would impose tax computed on profits or income, or computed on any capital asset, gain or appreciation, or any tax in the nature of estate, duty or inheritance tax.

A reconciliation of the difference between the provision for income taxes and the expected tax provision at the applicable zero percent domestic rate for the years ended December 31, 2007, 2006, and 2005, is provided below (in thousands):

	2007	2006	2005
U.S. federal income tax provision on Primus Asset Management's taxable income	$ —	$ —	$ —
U.S. state and local tax provision	52	42	46
Total income tax provision	$ 52	$ 42	$ 46

The Company has a net U.S. deferred tax asset of $8.4 million, $9.5 million and $4.8 million as of December 31, 2007, 2006 and 2005, respectively. The net deferred tax asset is primarily comprised of share compensation expense and capitalized costs and pre-operating formation costs, which are being amortized for tax purposes. In addition, included within the gross deferred tax assets are tax effected net operating losses related to Primus Asset Management of $5.3 million related to the net operating losses during years 2002 through 2007. Net operating losses will begin to expire in the year 2022 if not utilized.

The tax consequences of various restructurings that took place in 2002, included certain limitations and uncertainties, including issues with respect to the application of IRC Section 382, which could limit the utilization of certain amortized costs as an offset against Primus Asset Management's taxable income. However, the Company believes it is more likely than not that these costs will be allowable tax deductions.

The Company has recorded a 100% valuation allowance against its deferred tax asset because management has determined that it is more likely than not that the deferred tax asset will not be realized due to Primus Asset Management's history of net operating losses and inability to generate future taxable income sufficient to utilize such deferred tax asset. A rollforward of the valuation allowance against Primus Asset Management's deferred tax asset is provided below.

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The components of the net deferred tax asset at December 31, 2007, 2006 and 2005, are as follows (in thousands):

December 31,	2007	2006	2005
Deferred tax assets			
Capitalized and pre-operating formation costs	$ —	$ 631	$ 700
Share compensation	3,057	3,478	1,483
Net operating losses	5,330	5,317	3,345
Other	382	475	—
Gross deferred tax asset	8,769	9,901	5,528
Deferred tax liability			
Other	—	—	(20)
Depreciation	(348)	(447)	(745)
Gross deferred tax liability	(348)	(447)	(765)
Net deferred tax asset	8,421	9,454	4,763
Valuation allowance	8,421	(9,454)	(4,763)
Net deferred tax asset after valuation allowance	$ —	$ —	$ —

The changes in the valuation allowance for the deferred tax asset for the years ended December 31, 2007, 2006 and 2005, are as follows (in thousands):

December 31,	2007	2006	2005
Balance at beginning of period	$ 9,454	$ 4,763	$ 9,307
Capitalized and pre-operating costs	(631)	(69)	(1,941)
Share compensation	(421)	1,995	(1,787)
Tax depreciation / other	6	793	(288)
Net operating loss	13	1,972	(528)
Balance at end of period	$ 8,421	$ 9,454	$ 4,763

12. Preferred Securities of Subsidiary

On December 19, 2002, Primus Financial issued $110 million of perpetual Floating Rate Cumulative Preferred Securities (‘‘Preferred Securities’’) in two series, Series I and Series II to a Trust. The securities are held by Deutsche Bank Trust Company Americas, as custodian and auction agent. Pursuant to Statement of Position (SOP) 98-5 Reporting on the Costs of Start-Up Activities, specific incremental costs directly attributable to the offering of the Trust preferred securities have been charged against these gross proceeds.

In conjunction with the receipt of the Securities, the Trust issued $100 million of Money Market Preferred Securities Custodial Receipts (‘‘MMP’’) in two series, Series A and Series B, with a liquidation preference of $1,000 per share, to various institutional investors in a private placement. The Trust also issued $10 million of Variable Inverse Preferred Securities Custodial Receipts (‘‘VIP’’), which were retained by Primus Financial.

In 2003, the Company adopted FIN 46R and deconsolidated the Trust effective December 19, 2002. The preferred securities referred to in the financial statements are Primus Financial’s Preferred Securities, which are shown net of the $10 million of VIP issued by the Trust that are held by Primus Financial.

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Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

Distributions to the Trust on the Preferred Securities are adjusted through the VIP to equal the distributions required on the MMP. The Series A MMP pays distributions every 28 days based upon an auction rate set on the prior business day. The Series B MMP made dividend payments quarterly during 2006 based on the auction rate of 5.8%, which was set on January 19, 2006. In January 2007, the distribution rate on the Series B MMP was amended to pay distributions every 28 days which will coincide with the Series A MMP distributions. After December 19, 2012, the Company may redeem the Preferred Securities, in whole or in part, on any distribution date at $1,000 per share plus accumulated and unpaid dividends. These preferred securities are rated A/A2 by S&P and Moody's respectively.

Distributions on perpetual preferred securities of our subsidiary were $7.6 million, $5.7 million and $3.9 million for the years ended December 31, 2007, 2006 and 2005, respectively, which are recorded in the consolidated statements of operations.

During the second half of 2007, the turbulent market conditions also affected the debt capital markets. Beginning in August 2007 there was limited investor demand for our preferred securities issued in the auction rate market. As a result of the insufficient demand, the auctions did not clear and the rates on these preferred securities were set at the maximum spread rates, as specified in the security agreement. These maximum rates are subject to increase if the credit ratings on these securities are downgraded. This resulted in higher distributions during the second half of 2007.

13. Shareholders' Equity

Warrants

On February 14, 2007, XL Insurance (Bermuda) Ltd., a subsidiary of XL Capital Ltd., exercised its warrants to purchase 1,414,747 common shares of the Company at an exercise price of approximately $5.18 per share, yielding proceeds to the Company of $7.3 million.

14. Earnings per share

Basic earnings per share (''EPS'') is calculated by dividing earnings available to common shareholders by the weighted-average number of common shares outstanding. Diluted EPS is similar to basic EPS, but adjusts for the effect of the potential issuance of common shares. The following table presents the computations of basic and diluted EPS:

Years ended December 31, (in thousands, except per share data)	2007	2006	2005
Net earnings (loss) available to common shareholders	$ (563,541)	$ 94,891	$ 4,083
Weighted-average basic shares outstanding	44,808	43,306	43,150
Effect of dilutive instruments:			
Employee options	—	53	188
Restricted share units	—	322	467
Warrants	—	791	840
Dilutive potential shares	—	1,166	1,495
Weighted average diluted shares outstanding	44,808	44,472	44,645
Basic EPS	$ (12.58)	$ 2.19	$ 0.09
Diluted EPS	$ (12.58)	$ 2.13	$ 0.09

For the years ended December 31, 2007, 2006 and 2005, approximately 1.8 million, 498 thousand and 245 shares, respectively, were not included in the computation of diluted EPS because to do so would have been anti-dilutive for the periods presented.

Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

15. Commitments and Contingencies

Leases

Primus Financial currently occupies approximately 17,500 square feet of office space at 360 Madison Avenue, New York, New York at a fixed yearly rental (subject to certain escalations specified in the lease). In 2006, Primus Financial amended the original lease to extend its term to 2016 and add approximately 5,500 square feet of additional space. In addition, in 2006, the Company leased approximately 2,900 square feet of office space in London under a lease that expires in 2012. There are no material restrictions imposed by the lease agreements.

The leases are categorized as operating leases and future payments as of December 31, 2007 under the leases are as follows (in thousands):

2008	$ 1,255
2009	1,255
2010	1,255
2011	1,256
2012	1,248
2013 and thereafter	3,657
Total	$ 9,926

Pursuant to the terms of the original lease, dated July 25, 2002, Primus Financial was not required to make any rent payments until March 2003. Primus Financial recognizes rent expense from the lease commencement date based on a straight-line amortization of the total lease obligation. Primus Financial has recorded a deferred rent payable, which is included in other liabilities in the consolidated statements of financial condition, which represents the amortized cost that will be payable in the future. Rent expense was approximately $1.5 million, $1.5 million and $0.8 million for the years ended December 31, 2007, 2006 and 2005, respectively.

Primus Financial has an outstanding letter of credit as of December 31, 2007 for $695 thousand from Bank of Montreal related to this lease.

Statutory Requirements

Primus Re is an insurance company subject to Bermuda insurance regulations. Primus Re’s ability to pay dividends and make capital distributions is subject to restrictions based principally on the amount of Primus Re’s net premiums written and net loss reserves, subject to an overall minimum statutory capital and surplus of $1.0 million. In addition, Primus Re is required to maintain a minimum statutory liquidity ratio. At December 31, 2007, Primus Re’s statutory capital and surplus was $1.17 million and the minimum amount required to be maintained was $1.0 million. At December 31, 2006, Primus Re’s statutory capital and surplus was $1.18 million and the minimum amount required to be maintained was $1.0 million.

16. Restructuring

In January 2006, PRS Trading Strategies commenced operations to trade in a broad range of fixed income products, including credit default swaps, investment grade and high yield bonds, as well as leveraged loans. This was part of Primus Asset Management’s strategy to expand its asset management business. In April 2007, Primus Guaranty formed Harrier, a Cayman Islands exempted limited partnership to enable it to more efficiently raise capital from third party investors. During the second quarter of 2007, Primus Guaranty transferred the trading portfolio of its subsidiary, PRS

Trading Strategies to Harrier. Harrier traded in an expanded range of fixed income products from PRS Trading, including credit swaps, total return swaps on loan transactions, CDS Indices, leveraged loans and investment grade and non-investment grade securities.

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Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

During the fourth quarter of 2007, the Company decided to discontinue Harrier, due in part to Harrier's performance and difficulty in raising third-party capital, given the market environment at that time. As a result of this decision, in the fourth quarter of 2007, the Company recorded restructuring costs of $3.0 million. Of the total restructuring costs, approximately $2.2 million was in connection with the write-off of certain software and technology assets and approximately $0.8 million related to net employee termination benefits. As of December 31, 2007, substantially all of Harrier's trading positions have been closed.

At December 31, 2007, the balance of restructuring liabilities was approximately $1.7 million, which consisted entirely of payments for employee termination benefits. This balance is expected to be paid by the end of the first quarter of 2008.

17. Employee Share-Based Compensation Plans

Primus Guaranty has established incentive compensation plans for the benefit of its employees. Share compensation expense is included in compensation and employee benefits in the consolidated statements of operations.

Initial Staffing Award Pool

During 2001, an award pool of common shares of Primus Guaranty totaling 1,500,000 shares was established (the ''Initial Staffing Award Pool''). All of these shares were awarded from 2001 to 2003 at the fair value of the common shares on the grant date ranging from $0.08 per share to $6.93 per share.

Share compensation expense related to Initial Staffing Award Pool grants was zero, $86 thousand and $278 thousand for the years ended December 31, 2007, 2006 and 2005, respectively.

Annual Performance Bonus Plan

The Annual Performance Bonus Plan (''Bonus Plan'') was created in 2002 and provides for the awards of cash to employees of Primus Asset Management and Restricted Share Units, or RSUs convertible at the option of the holder into common shares of Primus Guaranty. The total value of awards under the Bonus Plan is determined by the Compensation Committee of Primus Guaranty based on quantitative and non-quantitative measures of the performance of Primus Guaranty. Individual awards are then determined by the Chief Executive Officer of Primus Guaranty, and are subject to the approval of the Compensation Committee. The Compensation Committee also determines the awards to the executive officers. Under the terms of the Bonus Plan individual awards will be made 75% in cash and 25% in RSUs (70% in cash and 30% in RSUs for certain members of management), with the number of RSUs determined on the basis of the value of the common shares on the date the award is authorized. The RSUs vest ratably over a three year period on the anniversary dates of each award, with vesting subject to certain terms including the continued employment of the award recipient by Primus Asset Management. The Bonus Plan includes provision for the award of up to 1,393,652 RSUs and options (discussed below) over a five year period beginning in February 2003.

During 2007, 2006 and 2005, the Company granted 234,019, 147,988 and 129,025 shares, respectively, of its RSUs to its employees related to the Annual Performance Bonus Plan, with a weighted average grant date fair value per share of $11.75, $12.74 and $16.05, respectively. The value of the RSUs is expensed ratably over the vesting period. For the years ended December 31, 2007, 2006 and 2005, share compensation expense was $1.4 million, $1.2 million, and $1.2 million, respectively, related to this plan.

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Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

Share Incentive Plan

The Share Incentive Plan (''Incentive Plan'') was created in 2002 and provides for the award of options on common shares of Primus Guaranty to selected employees of Primus Asset Management. Individual awards are determined by the Chief Executive Officer of the Company, and are subject to the approval of the Compensation Committee. The Compensation Committee also determines the awards to the executive officers. The options become exercisable ratably over a four year period on the anniversary date of each award, subject to certain terms including the continued employment of each recipient by Primus Asset Management. The options expire ten years from the date of grant and do not qualify for Incentive Share Option Treatment under the Economic Recovery Tax Act of 1981 (ISO Treatment). Upon the IPO by the Company, 50% of the then unvested options vested. The total number of equity incentive awards authorized for issuance under the Incentive Plan is 12% of total authorized shares.

During 2007 and 2006, the Company granted 847,607 and 422,122 options, respectively, to its employees related to the Incentive Plan, with a weighted average exercise price of $11.70 and $12.46, respectively. The fair value of the options is expensed ratably over the vesting period. For the years ended December 31, 2007, 2006 and 2005, share compensation expense was $1.1 million, $600 thousand and $508 thousand, respectively, related to this plan. There were no grants made under the Incentive Plan in 2005.

2004 Share Incentive Plan

In 2004, the Company's board of directors adopted the 2004 Share Incentive Plan, and authorized the grant of options and performance shares in the aggregate amount of up to 2.4% of total authorized shares. The board of directors delegated to the Compensation Committee decisions regarding the terms and conditions of such awards, including the apportionment between options and performance shares, the employees to whom such awards are to be granted and the performance factors required to earn such shares. The performance factors are (i) the return on economic equity and (ii) the compound annual growth rate of the economic results over a specified three year period. The performance shares vest only at the end of the respective performance period. In the fourth quarter of 2007, the board of directors established the Primus Guaranty, Ltd., Restricted Stock Unit Deferral Plan (''Deferral Plan''), to be effective December 31, 2007. The Deferral Plan permits selected participants in the 2004 Share Incentive Plan to defer distributions associated with their vested RSUs until the participant separates from service with the Company.

During 2006 and 2005, the Company granted 110,250 and 146,537 performance award shares, respectively, to its employees. The expense associated with the performance share awards will be adjusted over the vesting period to reflect the projected actual award, which is based upon the aggregate performance of the company over a three year period.

During 2007, 2006 and 2005, the Company granted to its employees and directors 188,468, 244,303 and 57,565 RSUs, respectively. During 2005, the Company granted 30,000 options at an exercise price of $10.50. The cost of the RSUs and options is recognized over the vesting period.

For the years ended December 31, 2007, 2006 and 2005, share compensation expense was $1.2 million, $1.8 million and $1.7 million relating to the plan.

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Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

Unvested RSUs and performance share awards as of and for the year ended December 31, 2007 was as follows:

	December 31, 2007	
	Number of shares	Weighted average grant date fair value
Unvested at December 31, 2006	591,034	$ 13.34
Granted	422,487	$ 11.52
Vested	(252,953)	$ 11.62
Forfeited	(207,960)	
Unvested at December 31, 2007	552,608	$ 12.25

Options

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model using the following weighted average assumptions for the periods indicated:

Years ended December 31,	2007	2006	2005
Risk free interest rate	5.32%	5.16%	4.90%
Volatility	32.8%	33.8%	31.8%
Expected dividend yield	0.00%	0.00%	0.00%
Expected option life	7 years	7 years	7 years
Weighted average fair value of options	$3.73	$4.02	$2.78

The following table is a summary of the information concerning outstanding and exercisable options for the years ended December 31, 2007, 2006 and 2005:

	2007		2006		2005	
	Number of shares	Weighted average exercise price	Number of shares	Weighted average exercise price	Number of shares	Weighted average exercise

price

Outstanding at beginning of year	858,158	$ 11.18	710,860	$ 10.43	776,094	$ 10.28
Granted	847,607	$ 11.70	422,122	$ 12.46	30,000	$ 10.50
Exercised	(67,968)	$ 8.20	(56,641)	$ 8.73	(58,983)	$ 8.35
Forfeited	(326,173)	$ 11.41	(218,183)	$ 11.84	(36,251)	$ 10.61
Outstanding at end of year	1,311,624	$ 11.61	858,158	$ 11.18	710,860	$ 10.43
Exercisable at end of year	332,438	$ 10.85	275,623	$ 9.92	280,077	$ 9.54

The following table summarizes the status of the Company's options as of December 31, 2007:

	Options Outstanding				Options Exercisable		
Range of Exercise Prices	Number of Shares	Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Aggregate Intrinsic Value	Number of Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value
$0.00-$6.94	65,625	5.1	$ 6.94	$ 4,856	65,625	$ 6.94	$ 4,856
$6.95-$9.76	113,125	6.1	$ 9.76	—	84,844	$ 9.76	—
$9.77-$13.50	1,132,874	5.6	$ 12.07	—	181,969	$ 12.77	—
Total	1,311,624			$ 4,856	332,438		$ 4,856

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Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

At December 31, 2007, total unrecognized share-based compensation expense related to nonvested share awards was approximately $6.8 million. This share-based compensation expense is expected to be recognized over a weighted average period of 1.9 years.

18. Dividend Restrictions

Primus Financial's operating guidelines restrict the payment of dividends to once per year. The payment of dividends by Primus Financial is contingent upon a dividend payment not resulting in a capital shortfall under its operating guidelines and the dividend not exceeding 100% (amended from 25% during 2006) of Primus Financial's net income (excluding mark-to-market unrealized gains or losses on credit swaps). Primus Financial is further restricted from paying dividends under the terms of its Preferred Securities unless all of the cumulative distributions on the Preferred Securities have been previously made or set aside. The Company's insurance subsidiary, Primus Re, is also subject to significant regulatory restrictions limiting its ability to declare and pay dividends.

Further, the Company is subject to Bermuda law and regulatory constraints that will affect its ability to pay dividends on its common shares and make other payments. Under the Bermuda Companies Act, each of Primus Guaranty, Primus Bermuda and Primus Re may not declare or pay a dividend out of distributable reserves if there are reasonable grounds for believing that they are, or would after the payment be, unable to pay the respective liabilities as they become due; or if the realizable value of their respective assets would thereby be less than the aggregate of their respective liabilities and issued share capital and share premium accounts.

19. Interest Rate Swap Agreement

In February 2007, the Company entered into an interest rate swap agreement with a major financial institution that effectively converted a notional amount of $75 million of the Company's $125 million, 7% senior notes due in December 2036, to floating rate debt based on the three month LIBOR rate plus a spread as defined in the agreement. The interest rate swap is designated as a fair value hedge on the fixed senior notes in accordance with SFAS No. 133. The fair value of the interest rate swap is included in other liabilities and the offsetting adjustment to the carrying value of the debt is included in long term debt in the accompanying consolidated statements of financial condition. Payments or receipts on the interest rate swap are recorded in the interest expense caption in the consolidated statements of operations.

20. Subsequent Event

On January 30, 2008, Standard and Poor's Rating Services (''S&P'') announced a change in their ratings methodology and assumptions relating to CDOs and other structured products, including certain asset backed securities (ABS). As a result of these changes, the S&P ratings on six residential mortgage backed securities referenced by credit default swaps written by Primus Financial were downgraded to CCC or below. At December 31, 2007, the notional principal amount and the fair values of these credit swaps were $45.0 million and $(32.1) million, respectively. At December 31, 2007, the notional principal amount and the fair values on credit swaps sold on ABS, not downgraded to CCC (S&P) or below was $35.0 million and $(16.6) million, respectively. See note 6 for further discussion.

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Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

The table below summarizes, in thousands, the notional amounts of credit swaps on ABS sold by Primus Financial and S&P credit ratings for the underlying ABS as of December 31, 2007 and January 30, 2008:

Notional Amount Credit Swaps Sold-ABS:	December 31, 2007	January 30, 2008
A	$ 50,000	$ 15,000
BBB	15,000	10,000
BB	15,000	10,000
CCC	—	40,000
CC	—	5,000
Total	$ 80,000	$ 80,000

Under the terms of our agreements governing the credit swaps on ABS, a downgrade of the underlying ABS securities to CCC or below is considered a defined credit event. Upon the occurrence of a defined credit event, a counterparty to the credit swap has the right to present the underlying ABS, in whole or in part, to Primus Financial in exchange for the cash notional value of the credit swap corresponding to the face amount of the securities presented (‘‘Physical Settlement’’). If, following a defined credit event, no Physical Settlement occurs, a counterparty may make a loss claim in the event of a principal write-down event, if any (Pay-As-You-Go). A principal write-down event occurs when the ABS servicer determines that there is insufficient collateral to pay a portion or all of the face value of the underlying securities. Any principal write-down claims will be paid by Primus Financial up to the notional amount of the credit default swap.

To date, of the six ABS credit swaps which suffered a downgrade, one counterparty has physically settled by delivering to Primus Financial an ABS with $5 million face amount and Primus Financial paid $5 million to the counterparty. That swap is terminated as a result of the physical settlement and Primus Financial will no longer receive premiums from the counterparty. As the owner of the ABS, Primus Financial is entitled to receive payments of principal and interest thereon.

21. Quarterly Operating Results (unaudited)

(in thousands)

2007:	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Total net revenues (losses)	$ 7,071	$ (4,409)	$ (112,031)	$ (383,163)
Operating loss	(9,662)	(21,520)	(128,435)	(403,872)
Net loss	(9,718)	(21,516)	(128,435)	(403,872)
Basic earnings (loss) per share	$ (0.22)	$ (0.48)	$ (2.85)	$ (8.97)
Diluted earnings (loss) per share	$ (0.22)	$ (0.48)	$ (2.85)	$ (8.97)

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Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

(in thousands)

2006:	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Total net revenues	$ 46,873	$ 23,941	$ 37,047	$ 40,003
Operating income	35,160	10,658	23,718	25,397
Net income	35,105	10,658	23,732	25,396
Basic earnings per share	$ 0.81	$ 0.25	$ 0.55	$ 0.59
Diluted earnings per share	$ 0.79	$ 0.24	$ 0.54	$ 0.57

22. Primus Guaranty, Ltd. Standalone Financial Statements

Primus Guaranty, Ltd.
Statements of Financial Condition

(in thousands)	December 31, 2007	2006
Assets		
Cash and cash equivalents	$ 70,455	$ 112,774
Investment in subsidiaries, at equity	—	471,329
Prepaid expenses and other assets	437	203
Intercompany receivable	2,942	—
Intercompany loans	13,931	—
Debt issuance costs, net	4,235	4,503
Other assets	904	—
Total assets	$ 92,904	$ 588,809
Liabilities and shareholders’ equity		
Accounts payable	$ 314	$ 432
Interest payable	109	97
Long-term debt	125,904	125,000
Intercompany payable	2,175	1,189
Losses of subsidiary’s in excess of investment	57,864	—
Total liabilities	186,366	126,718
Common shares	3,603	3,470
Additional paid-in-capital	280,224	269,420
Accumulated other comprehensive loss	(4,712)	(2,375)
Warrants	—	612
Retained earnings (deficit)	(372,577)	190,964
Total shareholders’ equity (deficit)	(93,462)	462,091
Total liabilities and shareholders’ equity	$ 92,904	$ 588,809

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Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

Primus Guaranty, Ltd.
Statements of Operations

(in thousands) Year ended December 31	2007	2006	2005
Revenues			
Interest income	$ 5,157	$ 252	$ 1,526
Foreign currency revaluation loss	—	—	(1,281)
Total revenues	5,157	252	245
Expenses			
Intercompany expenses*	7,687	5,911	6,787
Share compensation	367	270	423
Interest expense	8,458	99	—
Professional and legal fees	809	92	20
Other	374	2	43
Total expenses	17,695	6,374	7,273
Income (loss) before equity in earnings (loss) of subsidiaries	(12,538)	(6,122)	(7,028)
Equity in earnings (loss) of subsidiaries, net of tax	(551,003)	101,013	11,111
Net income (loss)	$ (563,541)	$ 94,891	$ 4,083

* Charges for services provided by subsidiaries under modified intercompany service agreement.

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Primus Guaranty, Ltd.
Notes to Consolidated Financial Statements

Primus Guaranty, Ltd.
Statements of Cash Flows

(in thousands) Year ended December 31	2007	2006	2005
Cash flows from operating activities:			
Net income (loss)	$ (563,541)	$ 94,891	$ 4,083
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Share compensation	3,748	3,654	423
Amortization of debt issuance costs	146	2	—
Change in accumulated comprehensive loss of subsidiaries	(2,337)	1,879	—
Equity in subsidiaries’ (earnings) loss, net of tax	551,003	(101,013)	(11,111)
Increase (decrease) in cash resulting from changes in:			
Intercompany receivables/payables and loans	(16,032)	(6,001)	14,141
Prepaid expenses and other assets	(234)	(159)	7
Accounts payable	4	432	—
Interest payable	12	97	—
Net cash provided by (used in) operating activities	(27,231)	(6,218)	7,543
Cash flows from investing activities:			
Investment in subsidiaries	(21,810)	(54,887)	(5,402)
Net cash used in investing activities	(21,810)	(54,887)	(5,402)
Cash flows from financing activities:			
Repurchase and retirement of common shares	(1,170)	(793)	(3,154)
Proceeds from exercise of warrants	7,335	—	—
Proceeds from exercise of options	557	609	493
Proceeds from issuance of debt	—	125,000	—
Debt issuance costs	—	(4,505)	—
Net cash provided by (used in) financing activities	6,722	120,311	(2,661)
Net increase (decrease) in cash	(42,319)	59,206	(520)
Cash and cash equivalents at beginning of year	112,774	53,568	54,088
Cash and cash equivalents at end of year	$ 70,455	$ 112,774	$ 53,568

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Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosures

None.

Item 9A. Controls and Procedures

The company has carried out an evaluation, under the supervision and with the participation of the company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended, as of the end of the period covered by this Annual Report. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the disclosure controls and procedures are effective to provide reasonable assurance that all material information relating to the company required to be filed in this report have been made known to them in a timely fashion. There have been no changes in internal control over financial reporting that occurred during the most recent fiscal quarter that have materially affected, or are reasonably likely to affect, internal control over financial reporting.

The company's management, including the Chief Executive Officer and the Chief Financial Officer, does not expect that the company's disclosure controls or its internal controls will prevent all errors and all fraud. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. As a result of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company have been detected. These inherent limitations include the realities that judgments in decision-making are faulty, and that breakdowns can occur because of simple error or mistake. As a result of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected. Accordingly, the company's disclosure controls and procedures are designed to provide reasonable, not absolute, assurance that the disclosure controls and procedures are met.

See Management's Report on Internal Control over Financial Reporting in Item 8 of this Annual Report on Form 10-K, which is incorporated by reference herein.

Item 9B. Other information

None.

All items requiring disclosure in a report on Form 8-K during the fourth quarter of the year ended December 31, 2007 have been so reported.

Part III.

Item 10. Directors, Executive Officers and Corporate Governance

Information regarding directors is set forth under ''Election of Directors'' in the company's Proxy Statement to be filed on or before April 30, 2008 (the ''Proxy Statement''), which is incorporated in this Item 10 by reference.

Information regarding executive officers is set forth under ''Executive Officers'' in the Proxy Statement, which is incorporated in this Item 10 by reference.

Information regarding Section 16(a) is set forth under ‘‘Section 16(a) Beneficial Ownership Reporting Compliance’’ in the Proxy Statement, which is incorporated in this Item 10 by reference.

Information regarding the audit committee and the audit committee financial expert is set forth under ‘‘Audit Committee’’ in the Proxy Statement, which is incorporated in this Item 10 by reference.

The company has adopted a code of business conduct and ethics for all employees, including its Chief Executive Officer and Chief Financial Officer. A copy of such code of ethics can be found on the Company’s website, at www.primusguaranty.com, free of charge. The Company would intend to

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satisfy the disclosure requirements regarding an amendment to, or waiver from, a provision of its code of ethics and that relates to a substantive amendment or material departure from a provision of the code by posting such information on its website at www.primusguaranty.com.

Item 11. Executive Compensation

Information regarding compensation of the company's executive officers is set forth under ''Executive Officer Compensation'' in the compensation tables in the Proxy Statement, which is incorporated in this Item 11 by reference.

Item 12.
Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters

Information regarding securities authorized for issuance under equity compensation plans, is set forth in the Proxy Statement, which is incorporated in this Item 12 by reference.

Information regarding security ownership of certain beneficial owners and management is set forth under ''Security Ownership of Certain Beneficial Owners and Management'' in the Proxy Statement, which is incorporated in this Item 12 by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence

Information regarding relationships and related transactions and director independence is set forth under ''Certain Relationships and Related Transactions'' in the Proxy Statement, which is incorporated in this Item 13 by reference.

Item 14. Principal Accountant Fees and Services

Information concerning principal accountant fees and services will be set forth under ''Audit Committee Report-Fees of the Independent Registered Public Accounting Firm'' in the Proxy Statement, which is incorporated in this Item 14 by reference.

Part IV.

Item. 15 Exhibits and Financial Statement Schedules

(a) Financial Statements

The financial statements are set forth under Item 8 of this Annual Report on Form 10-K.

(b) Financial Statement Schedules

The following information is filed as part of this Annual Report on Form 10-K and should be read in conjunction with the financial statements contained in Item 8:

Reports of Independent Registered Public Accounting Firm

All other schedules have been omitted because they were not applicable or because the required information has been included in the financial statements or notes thereto.

(c) Exhibits

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Index to Exhibits

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Exhibit 3 .1 Memorandum of Association (Incorporated by reference to Exhibit 3.1 to the S-1 dated July 23, 2004) 3 .2 By-laws (Incorporated by reference to Exhibit 3.2 to the S-1/A dated June 10, 2004) 4 .1 Specimen Common Share Certificate (Incorporated by reference to Exhibit 4.1 to the S-1/A dated July 23, 2004) 4 .2 Senior Indenture dated as of December 27, 2006 between Primus Guaranty, Ltd. and the Trustee (Incorporated by reference to Exhibit 4.1 to Form 8-K filed on December 27, 2006) 4 .3 First Supplemental Indenture dated as of December 27, 2006 between Primus Guaranty, Ltd. and the Trustee (Incorporated by reference to Exhibit 4.2 to Form 8-K filed on December 27, 2006) 4 .4 7% Senior Notes due 2036 10 .1 Employment Agreement with Thomas W. Jasper, dated August 16, 2004 (Incorporated by reference to Exhibit 10.1 to the S-1 dated August 17, 2004) 10 .2 Employment Letter with Richard Claiden, dated October 20, 2003 (Incorporated by reference to Exhibit 10.3 to the S-1/A dated June 10, 2004) 10 .3 Form of Registration Rights Agreement by and among the Registrant and the signatories thereto (Incorporated by reference to Exhibit 10.4 to the S-1/A dated June 10, 2004) 10 .4 Primus Guaranty, Ltd. Share Incentive Plan (Incorporated by reference to Exhibit 10.5 to the S-1 dated April 26, 2004) 10 .5 Primus Guaranty, Ltd. 2004 Share Incentive Plan (As amended on February 1, 2007) 10 .6 Primus Guaranty, Ltd. Annual Performance Bonus Plan (Incorporated by reference to Exhibit 10.7 to the S-1 dated April 26, 2004) 10 .7 Primus Guaranty, Ltd. Severance Plan (As amended on February 1, 2007) 10 .8 Office Lease Agreement, dated July 25, 2002, between Madison 45 LLC and Primus Financial Products, LLC (Incorporated by reference to Exhibit 10.9 to the S-1 dated April 26, 2004) 10 .9 Form of Indemnification Agreement between Primus Guaranty, Ltd. and each of its directors and officers (Incorporated by reference to Exhibit 10.11 to the S-1/A dated June 10, 2004) 10 .10 Indemnification Agreement, dated September 22, 2004, between Primus Guaranty, Ltd. and XL Capital Ltd. (Incorporated by reference to Exhibit 10.12 to the S-1/A dated September 24, 2004) 10 .11 Primus Guaranty, Ltd. Restricted Share Unit Deferral Plan effective December 31, 2007 12 Ratio of Earnings to Combined Fixed Charges and Preferred Share Dividend Requirements 21 Subsidiaries of Primus Guaranty, Ltd. 23 Consent of Ernst & Young LLP, Independent Registered Public Accounting Firm

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Annual Report to be signed on its behalf by the undersigned, thereunto duly authorized.

PRIMUS GUARANTY, LTD.
(Registrant) By/s/ Thomas W. Jasper Thomas W. Jasper
Chief Executive Officer
Dated: March 14, 2008

Pursuant to the requirements of the Securities Exchange Act of 1934, this Annual Report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Thomas W. Jasper Thomas W. Jasper	Chief Executive Officer and Director (Principal Executive Officer)	March 14, 2008
/s/ Richard Claiden Richard Claiden	Chief Financial Officer (Principal Financial and Accounting Officer)	March 14, 2008
/s/ Michael P. Esposito, Jr. Michael P. Esposito, Jr.	Director and Chairman of the Board	March 14, 2008
/s/ Frank P. Filipps Frank P. Filipps	Director	March 14, 2008
/s/ Paul S. Giordano Paul S. Giordano	Director	March 14, 2008
/s/ Thomas J. Hartlage Thomas J. Hartlage	Director	March 14, 2008
/s/ James K. Hunt James K. Hunt	Director	March 14, 2008
/s/ Fiona E. Luck Fiona E. Luck	Director	March 14, 2008
/s/ Robert R. Lusardi Robert R. Lusardi	Director	March 14, 2008
/s/ John A. Ward, III John A. Ward, III	Director	March 14, 2008

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