

RADIAN GROUP INC  
Form 10-Q  
May 10, 2011

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

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FORM 10-Q

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(Mark One)

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

For the quarterly period ended March 31, 2011

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 1-11356

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Radian Group Inc.  
(Exact name of registrant as specified in its charter)

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Delaware  
(State or other jurisdiction of incorporation or organization)

23-2691170  
(I.R.S. Employer Identification No.)

1601 Market Street, Philadelphia, PA  
(Address of principal executive offices)  
(215) 231-1000  
(Registrant's telephone number, including area code)

19103  
(Zip Code)

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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 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 ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

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

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☐  
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

APPLICABLE ONLY TO CORPORATE ISSUERS:

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 133,113,518 shares of common stock, \$0.001 par value per share, outstanding on April 30, 2011.

Radian Group Inc.  
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Forward Looking Statements—Safe Harbor Provisions

All statements in this report that address events, developments or results that we expect or anticipate may occur in the future are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, Section 21E of the Securities Exchange Act of 1934 and the United States ("U.S.") Private Securities Litigation Reform Act of 1995. In most cases, forward-looking statements may be identified by words such as "anticipate," "may," "will," "could," "should," "would," "expect," "intend," "plan," "goal," "contemplate," "believe," "estimate," "predict," "project," "potential," "continue," or the negative or other variations on these words and other similar expressions. These statements, which may include, without limitation, projections regarding our future performance and financial condition, are made on the basis of management's current views and assumptions with respect to future events. Any forward-looking statement is not a guarantee of future performance and actual results could differ materially from those contained in the forward-looking information. The forward-looking statements, as well as our prospects as a whole, are subject to risks and uncertainties, including the following:

changes in general financial and political conditions, such as the failure of the U.S. economy to fully recover from the most recent recession or the U.S. economy reentering a recessionary period, the lack of meaningful liquidity in the capital markets or in the credit markets, a prolonged period of high unemployment rates and limited home price appreciation or further depreciation (which has resulted in some borrowers voluntarily defaulting on their mortgages when their mortgage balances exceed the value of their homes), changes or volatility in interest rates or consumer confidence, changes in credit spreads, changes in the way customers, investors or regulators perceive the strength of private mortgage insurers or financial guaranty providers, or investor concern over the credit quality and specific risks faced by the particular businesses, municipalities or pools of assets covered by our insurance;

catastrophic events or further economic changes in geographic regions where our mortgage insurance or financial guaranty insurance exposure is more concentrated;

our ability to successfully execute upon our capital plan for our mortgage insurance business (which depends, in part, on the performance of our financial guaranty portfolio), and if necessary, to obtain additional capital to support our mortgage insurance business and the long-term liquidity needs of our holding company;

a further reduction in, or prolonged period of depressed levels of, home mortgage originations due to reduced liquidity in the lending market, tighter underwriting standards, the risk retention requirements established under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") and the decrease in housing demand throughout the U.S.;

our ability to maintain adequate risk-to-capital ratios and surplus requirements in our mortgage insurance business in light of ongoing losses in this business and further deterioration in our financial guaranty portfolio which, in the absence of new capital, could depend on our ability to execute strategies for which regulatory and other approvals are required and may not be obtained;

our ability to continue to effectively mitigate our mortgage insurance and financial guaranty losses;

reduced opportunities for loss mitigation in markets where housing values do not appreciate or continue to decline;

- a more rapid than expected decrease in the level of insurance rescissions and claim denials from the current elevated levels (including as a result of successful challenges to previously rescinded policies or claim denials), which rescissions and denials have materially mitigated our paid losses and resulted in a significant reduction in our loss reserves;

the negative impact our insurance rescissions and claim denials may have on our relationships with customers and potential customers, including the potential loss of business and the heightened risk of disputes and litigation;

the need, in the event that we are unsuccessful in defending our rescissions or denials, to increase our loss reserves for, and reassume risk on, rescinded loans and pay additional claims;

the concentration of our mortgage insurance business among a relatively small number of large customers;

any disruption in the servicing of mortgages covered by our insurance policies;

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the aging of our mortgage insurance portfolio and changes in severity or frequency of losses associated with certain of our products that are riskier than traditional mortgage insurance or financial guaranty insurance policies;

the performance of our insured portfolio of higher risk loans, such as Alternative-A and subprime loans, and of adjustable rate products, such as adjustable rate mortgages and interest-only mortgages;

a decrease in persistency rates of our mortgage insurance policies;

an increase in the risk profile of our existing mortgage insurance portfolio due to the availability of mortgage refinancing to only the most qualified borrowers in the current mortgage and housing market;

further downgrades or threatened downgrades of, or other ratings actions with respect to, our credit ratings or the ratings assigned by the major rating agencies to any of our rated insurance subsidiaries at any time (in particular, the credit rating of Radian Group Inc. and the financial strength ratings assigned to Radian Guaranty Inc.);

- heightened competition for our mortgage insurance business from others such as the Federal Housing Administration (the "FHA"), the Veteran's Administration and private mortgage insurers (in particular, the FHA and those private mortgage insurers that have been assigned higher ratings from the major rating agencies or new entrants to the industry that are not burdened by legacy obligations);

changes in the charters or business practices of, or rules or regulations applicable to, Federal National Mortgage Association ("Fannie Mae") and Freddie Mac, the largest purchasers of mortgage loans that we insure, and our ability to remain an eligible provider to both Freddie Mac and Fannie Mae;

changes to the current system of housing finance, including the possibility of a new system in which private mortgage insurers are not required or their products are significantly limited in scope;

the effect of the Dodd-Frank Act on the financial services industry in general, and on our mortgage insurance and financial guaranty businesses in particular, including whether and to what extent loans with mortgage insurance are considered "qualified residential mortgages" for purposes of the Dodd-Frank Act securitization provisions or "qualified mortgages" for purposes of the ability to repay provisions of the Dodd-Frank Act and potential obligations to post collateral on our existing insured derivatives portfolio;

the application of existing federal or state consumer, lending, insurance, tax, securities and other applicable laws and regulations, or changes in these laws and regulations or the way they are interpreted; including, without limitation:

- (i) the outcome of existing, or the possibility of additional, lawsuits or investigations, and (ii) legislative and regulatory changes (a) affecting demand for private mortgage insurance, (b) limiting or restricting our use of (or increasing requirements for) additional capital and the products we may offer, or (c) affecting the form in which we execute credit protection or affecting our existing financial guaranty portfolio;

the possibility that we may fail to estimate accurately the likelihood, magnitude and timing of losses in connection with establishing loss reserves for our mortgage insurance or financial guaranty businesses or premium deficiencies for our mortgage insurance business, or to estimate accurately the fair value amounts of derivative instruments in our mortgage insurance and financial guaranty businesses in determining gains and losses on these contracts;

the ability of our primary insurance customers in our financial guaranty reinsurance business to provide appropriate surveillance and to mitigate losses adequately with respect to our assumed insurance portfolio;

volatility in our earnings caused by changes in the fair value of our derivative instruments and our need to reevaluate the possibility of a premium deficiency in our mortgage insurance business on a quarterly basis;

our ability to realize the tax benefits associated with our gross deferred tax assets, which will depend on our ability to generate sufficient sustainable taxable income in future periods;

our ability to obtain the necessary regulatory approval to consummate our purchase of Municipal and Infrastructure Assurance Corporation (the "FG Insurance Shell") and to successfully develop and implement a strategy to utilize the FG Insurance Shell in the public finance financial guaranty market, which strategy may depend on, among other items, our ability to obtain further necessary regulatory or other approvals, to attract third-party capital and to obtain ratings sufficient to support such a strategy;

• changes in accounting guidance from the Securities and Exchange Commission or the Financial Accounting Standards Board; and

• legal and other limitations on amounts we may receive from our subsidiaries as dividends or through our tax- and expense-sharing arrangements with our subsidiaries.

For more information regarding these risks and uncertainties as well as certain additional risks that we face, you should refer to the Risk Factors detailed in Item 1A of Part I of our Annual Report on Form 10-K for the year ended December 31, 2010, and in Item 1A of Part II of this Quarterly Report on Form 10-Q. We caution you not to place undue reliance on these forward-looking statements, which are current only as of the date on which we filed this report. We do not intend to, and we disclaim any duty or obligation to, update or revise any forward-looking statements made in this report to reflect new information or future events or for any other reason.



## PART I—FINANCIAL INFORMATION

## Item 1. Financial Statements. (Unaudited)

Radian Group Inc.

## CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(In thousands, except share and per share amounts)	March 31, 2011	December 31, 2010
<b>ASSETS</b>		
Investments		
Fixed-maturities held to maturity—at amortized cost (fair value \$9,250 and \$11,416)	\$8,743	\$10,773
Fixed-maturities available for sale—at fair value (amortized cost \$332,445 and \$340,795)	262,722	273,799
Equity securities available for sale—at fair value (cost \$160,083 and \$160,242)	194,921	184,365
Trading securities—at fair value (including variable interest entity (“VIE”) securities of \$90,187 and \$83,184)	4,640,719	4,562,821
Short-term investments—at fair value (including VIE investments of \$149,984 and \$149,981)	1,224,931	1,537,498
Other invested assets—at cost	61,218	59,627
Total investments	6,393,254	6,628,883
Cash	19,209	20,334
Restricted cash	29,801	31,413
Deferred policy acquisition costs	145,721	148,326
Accrued investment income	45,492	40,498
Accounts and notes receivable (less allowance of \$50,000 and \$50,000)	115,116	116,452
Property and equipment, at cost (less accumulated depreciation of \$93,822 and \$92,451)	12,411	13,024
Derivative assets (including VIE derivative assets of \$8,955 and \$10,855)	24,554	26,212
Deferred income taxes, net	27,531	27,531
Reinsurance recoverables	218,963	244,894
Other assets (including VIE other assets of \$108,163 and \$112,426)	319,511	323,320
Total assets	\$7,351,563	\$7,620,887
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Unearned premiums	\$666,019	\$686,364
Reserve for losses and loss adjustment expenses (“LAE”)	3,627,695	3,596,735
Reserve for premium deficiency	9,353	10,736
Long-term debt	968,199	964,788
VIE debt—at fair value (including \$7,561 and \$9,514 of non-recourse debt)	373,007	520,114
Derivative liabilities (including VIE derivative liabilities of \$17,430 and \$19,226)	487,345	723,579
Accounts payable and accrued expenses (including VIE accounts payable of \$883 and \$837)	247,048	258,791
Total liabilities	6,378,666	6,761,107
Commitments and Contingencies (Note 13)		
Stockholders' equity		
Common stock: par value \$.001 per share; 325,000,000 shares authorized; 150,567,283 and 150,507,853 shares issued at March 31, 2011 and December 31, 2010, respectively; 133,105,845 and 133,049,213 shares outstanding at March 31, 2011 and December 31, 2010, respectively	150	150
Treasury stock, at cost: 17,461,438 and 17,458,640 shares at March 31, 2011 and December 31, 2010, respectively	(892,036)	(892,012)
Additional paid-in capital	1,963,382	1,963,092

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Retained deficit	(101,920	) (204,926	)
Accumulated other comprehensive income (loss)	3,321	(6,524	)
Total stockholders' equity	972,897	859,780	
Total liabilities and stockholders' equity	\$7,351,563	\$7,620,887	
See notes to unaudited condensed consolidated financial statements.			

Radian Group Inc.

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

	Three Months Ended March 31,	
(In thousands, except per share amounts)	2011	2010
Revenues:		
Premiums written—insurance:		
Direct	\$ 190,841	\$ 184,278
Assumed	1,624	(1,248 )
Ceded	(9,716 )	(27,529 )
Net premiums written	182,749	155,501
Decrease in unearned premiums	20,274	42,767
Net premiums earned—insurance	203,023	198,268
Net investment income	42,240	45,358
Net gains on investments	37,435	57,948
Total other-than-temporary impairment ("OTTI") losses	—	(18 )
Losses recognized in other comprehensive income (loss)	—	—
Net impairment losses recognized in earnings	—	(18 )
Change in fair value of derivative instruments	243,892	(77,954 )
Net gains (losses) on other financial instruments	75,251	(101,564 )
Other income	1,448	5,775
Total revenues	603,289	127,813
Expenses:		
Provision for losses	427,373	543,880
Change in reserve for premium deficiency	(1,383 )	(1,231 )
Policy acquisition costs	14,131	14,868
Other operating expenses	46,219	65,056
Interest expense	17,024	10,804
Total expenses	503,364	633,377
Equity in net income of affiliates	65	8,098
Pretax income (loss)	99,990	(497,466 )
Income tax benefit	(3,016 )	(187,111 )
Net income (loss)	\$ 103,006	\$ (310,355 )
Basic net income (loss) per share	\$ 0.78	\$ (3.77 )
Diluted net income (loss) per share	\$ 0.77	\$ (3.77 )
Weighted-average number of common shares outstanding—basic	132,427	82,341
Weighted-average number of common and common equivalent shares outstanding—diluted	133,703	82,341
Dividends per share	\$ 0.0025	\$ 0.0025

See notes to unaudited condensed consolidated financial statements.

Radian Group Inc.  
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN COMMON STOCKHOLDERS' EQUITY  
(UNAUDITED)

(In thousands)	Common Stock	Treasury Stock	Additional Paid-in Capital	Retained Earnings/(Deficit)	Foreign Currency Translation Adjustment	Unrealized Holding Gains/Losses	Other	Total
BALANCE, JANUARY 1, 2010	\$ 100	\$(889,496)	\$1,363,255	\$ 1,602,143	\$ 18,285	\$(72,802 )	\$(16,491)	\$2,004,994
Comprehensive loss:								
Net loss	—	—	—	(310,355 )	—	—	—	(310,355 )
Unrealized foreign currency translation adjustment, net of tax of \$1,512	—	—	—	—	(2,006 )	—	—	—
Less: Reclassification adjustment for net gains included in net loss, net of tax of \$240	—	—	—	—	447	—	—	—
Net foreign currency translation adjustment, net of tax of \$1,272	—	—	—	—	(2,453 )	—	—	(2,453 )
Unrealized holding gains arising during the period, net of tax of \$9,077	—	—	—	—	—	16,857	—	—
Less: Reclassification adjustment for net gains included in net loss, net of tax of \$39	—	—	—	—	—	72	—	—
Net unrealized gain on investments, net of tax of \$9,038	—	—	—	—	—	16,785	—	16,785
Comprehensive loss	—	—	—	—	—	—	—	(296,023 )
Repurchases of common stock under incentive plans	—	(749 )	108	—	—	—	—	(641 )
Issuance of common stock under benefit plans	—	—	1,155	—	—	—	—	1,155
Amortization of restricted stock	—	—	1,624	—	—	—	—	1,624
Stock-based compensation expense	—	—	1,457	—	—	—	—	1,457
Dividends declared	—	—	—	(205 )	—	—	—	(205 )
BALANCE, March 31, 2010	\$ 100	\$(890,245)	\$1,367,599	\$ 1,291,583	\$ 15,832	\$(56,017 )	\$(16,491)	\$1,712,361
BALANCE, JANUARY 1, 2011	\$ 150	\$(892,012)	\$1,963,092	\$ (204,926 )	\$ 21,094	\$(27,857 )	\$239	\$859,780

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Comprehensive income:									
Net income	—	—	—	103,006	—	—	—	103,006	
Unrealized foreign currency translation adjustment	—	—	—	—	1,565	—	—		
Less: Reclassification adjustment for net losses on sales	—	—	—	—	(292	)—	—		
Net foreign currency translation adjustment	—	—	—	—	1,857	—	—	1,857	
Unrealized holding gains arising during the period	—	—	—	—	—	8,066	—		
Less: Reclassification adjustment for net gains included in net income	—	—	—	—	—	78	—		
Net unrealized gain on investments	—	—	—	—	—	7,988	—	7,988	
Comprehensive income	—	—	—	—	—	—	—	112,851	
Repurchases of common stock under incentive plans	—	(24	)	—	—	—	—	(24	)
Issuance of common stock under benefit plans	—	—	359	—	—	—	—	359	
Amortization of restricted stock	—	—	274	—	—	—	—	274	
Additional convertible debt issuance costs, net	—	—	(33	)—	—	—	—	(33	)
Stock-based compensation expense	—	—	23	—	—	—	—	23	
Dividends declared	—	—	(333	)—	—	—	—	(333	)
BALANCE, March 31, 2011	\$ 150	\$(892,036)	\$1,963,382	\$ (101,920	)\$ 22,951	\$ (19,869	)\$239	\$972,897	

See notes to unaudited condensed consolidated financial statements.

Radian Group Inc.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(In thousands)	Three Months Ended	
	March 31, 2011	2010
Cash flows used in operating activities	\$(260,863	) \$(287,011 )
Cash flows from investing activities:		
Proceeds from sales of fixed-maturity investments available for sale	515	6,555
Proceeds from sales of equity securities available for sale	376	5,353
Proceeds from sales of trading securities	313,036	229,349
Proceeds from redemptions of fixed-maturity investments available for sale	8,594	12,799
Proceeds from redemptions of fixed-maturity investments held to maturity	2,195	2,320
Purchases of trading securities	(376,825	) (371,150 )
Sales and redemptions of short-term investments, net	312,739	425,848
Purchases of other invested assets, net	(1,591	) (2,684 )
Purchases of property and equipment, net	(760	) (296 )
Net cash provided by investing activities	258,279	308,094
Cash flows from financing activities:		
Dividends paid	(333	) (205 )
Redemption of long-term debt	—	(29,348 )
Net cash used in financing activities	(333	) (29,553 )
Effect of exchange rate changes on cash	1,792	(608 )
Decrease in cash	(1,125	) (9,078 )
Cash, beginning of period	20,334	77,181
Cash, end of period	\$19,209	\$68,103
Supplemental disclosures of cash flow information:		
Income taxes paid	\$826	\$1,453
Interest paid	\$7,283	\$7,414
See notes to unaudited condensed consolidated financial statements.		

Radian Group Inc.  
Notes to Unaudited Condensed Consolidated Financial Statements

1. Condensed Consolidated Financial Statements—Basis of Presentation

Our condensed consolidated financial statements include the accounts of Radian Group Inc. and its subsidiaries. We refer to Radian Group Inc. together with its consolidated subsidiaries as "Radian," "we," "us" or "our," unless the context requires otherwise. We generally refer to Radian Group Inc. alone, without its consolidated subsidiaries, as "Radian Group."

Our condensed consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") and include the accounts of all wholly-owned subsidiaries. Companies in which we, or one of our subsidiaries, own interests ranging from 20% to 50%, are accounted for in accordance with the equity method of accounting. VIEs where we are the primary beneficiary are consolidated. See Note 5 for further information. All intercompany accounts and transactions, and intercompany profits and losses, have been eliminated. We have condensed or omitted certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with GAAP pursuant to the instructions of Article 10 of Regulation S-X of the Securities and Exchange Commission ("SEC").

The financial information presented for interim periods is unaudited; however, such information reflects all adjustments that are, in the opinion of management, necessary for a fair statement of the financial position, results of operations, and cash flows for the interim periods. These interim financial statements should be read in conjunction with the audited financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2010. The results of operations for interim periods are not necessarily indicative of results to be expected for the full year or for any other period. The total assets for the mortgage insurance segment as of March 31, 2010, reflected in Note 2 have been revised to conform to the presentation in the audited financial statements for the year ended December 31, 2010. The year-end condensed balance sheet data was derived from our audited financial statements, but does not include all disclosures required by GAAP.

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. While the amounts included in our condensed consolidated financial statements include our best estimates and assumptions, actual results may vary materially.

Our future performance and financial condition is subject to significant risks and uncertainties, including but not limited to, the following:

Potential adverse effects on us of the failure or significant delay of the United States ("U.S.") economy to fully recover, including ongoing uncertainty in the housing and related credit markets and high unemployment, which could increase our mortgage insurance or financial guaranty incurred losses beyond existing expectations (See Notes 7, 8 and 9).

Potential adverse effects if the capital and liquidity levels of Radian Group or our regulated subsidiaries' statutory capital levels are deemed inadequate to support current business operations and strategies. Radian Group had immediately available, directly or through an unregulated direct subsidiary, unrestricted cash and marketable securities of approximately \$819.2 million at March 31, 2011, which includes \$150 million of investments contained in our committed preferred custodian trust securities ("CPS") as discussed in Note 5. Radian Guaranty Inc.'s ("Radian Guaranty") statutory policyholders' surplus declined from \$1.3 billion at December 31, 2010, to \$1.1 billion at March 31, 2011.

Potential adverse effects if Radian Guaranty's regulatory risk-to-capital ratio were to increase above 25 to 1, including the possibility that insurance regulators or the Government Sponsored Enterprises ("GSEs") may limit or cause Radian Guaranty to cease underwriting new mortgage insurance risk, and Radian Guaranty's customers may decide not to insure loans with Radian Guaranty or may otherwise limit the type or amount of business done with Radian Guaranty. We have been preparing Amerin Guaranty Corporation ("Amerin Guaranty") to write new first-lien mortgage ("first-lien") insurance, if needed, and could pursue waivers from those states that impose a 25 to 1 limitation. If we are unable to continue writing new first-lien insurance business through Amerin Guaranty or obtain the necessary waivers from the risk-to-capital limitations, it will significantly impair our franchise value and reduce

our cash flow associated with new business while we continue to honor and settle all valid claims and related expenses. At March 31, 2011, this ratio was 20.3 to 1.



Radian Group Inc.

Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

Potential adverse effects if Radian Guaranty were to lose its eligibility status with the GSEs, which could occur at any time at the discretion of the GSEs. Loss of GSE eligibility would likely result in a significant curtailment of our ability to write new mortgage insurance business, which would significantly impair our franchise value and limit our cash flow arising from new business while we continue to honor and settle all valid claims and related expenses.

Potential adverse effects from legislative efforts to reform the housing finance market, including the possibility that new federal legislation could reduce or eliminate the requirement for private mortgage insurance.

Potential impact on our businesses as a result of the implementation of regulations under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), the effect of the Dodd-Frank Act on the financial services industry in general, and on our mortgage insurance and financial guaranty businesses in particular, including whether and to what extent loans with mortgage insurance are considered "qualified residential mortgages" for purposes of the Dodd-Frank Act securitization provisions or "qualified mortgages" for purposes of the ability to repay provisions of the Dodd-Frank Act and potential obligations to post collateral on our existing insured derivatives portfolio.

Potential adverse effects on Radian Group liquidity if regulators or the GSEs limit, disallow or terminate our expense allocation agreements among Radian Group and its subsidiaries. In the first three months of 2011, Radian Group received \$29.7 million in reimbursements from its subsidiaries under these agreements.

It is possible that the actual outcome of one or more of our plans or forecasts could be materially different, or that one or more of our estimates about the potential effects of the risks and uncertainties above or described elsewhere in this report, could prove to be materially different than our actual results. If one or more possible adverse outcomes were realized, there could be material adverse effects on our financial position, results of operations and cash flows.

Basic net income (loss) per share is based on the weighted-average number of common shares outstanding, while diluted net income (loss) per share is based on the weighted-average number of common shares outstanding and common share equivalents that would be issuable upon the exercise of stock options and other stock-based compensation. For the three months ended March 31, 2011, 2,708,882 shares of our common stock equivalents issued under our stock-based compensation plans were not included in the calculation of diluted net income per share because they were anti-dilutive. As a result of our net loss for the three months ended March 31, 2010, 4,278,010 shares of our common stock equivalents issued under our stock-based compensations plans were not included in the calculation of diluted net loss per share as of such date because they were anti-dilutive.

We have reflected the additional disclosures required by the update to the accounting standard regarding fair value measurements and disclosures effective January 1, 2011, in Note 4. The 2010 information has been revised to be consistent with the 2011 disclosure.

## 2. Segment Reporting

We currently have two reportable segments: mortgage insurance and financial guaranty.

Our reportable segments are strategic business units that are managed separately. We allocate corporate income and expenses to our mortgage insurance and financial guaranty segments based on either an allocated percentage of time spent or internally allocated capital. We allocate corporate cash and investments to our mortgage insurance and financial guaranty segments based on internally allocated capital.

Prior to January 1, 2011, we also had a third reportable segment—financial services. Our financial services segment had consisted mainly of our ownership interest in Credit-Based Asset Servicing and Securitization LLC ("C-BASS"), which was a credit-based consumer asset business. We wrote off our entire investment in C-BASS in 2007. C-BASS filed for Chapter 11 bankruptcy protection on November 12, 2010, and was subsequently liquidated. Our interest in C-BASS was extinguished pursuant to the Plan of Liquidation that was confirmed on April 25, 2011. In addition, until May 3, 2010, when we sold our remaining interest therein, our financial services segment included our interest in

Sherman Financial Group LLC, a consumer asset and servicing firm specializing in credit card and bankruptcy-plan consumer assets. Consequently, as of January 1, 2011, we no longer had any on-going activity in this reporting segment.

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

Summarized financial information concerning our current and previous operating segments, as of and for the periods indicated, are as follows:

(In thousands)	Three Months Ended	
	March 31, 2011	2010
Mortgage Insurance		
Net premiums written—insurance	\$ 180,846	\$ 157,032
Net premiums earned—insurance	\$ 186,134	\$ 177,339
Net investment income	26,833	26,359
Net gains on investments	17,762	28,781
Net impairment losses recognized in earnings	—	(18 )
Change in fair value of derivative instruments	(394 )	277 )
Net gains (losses) on other financial instruments	2,466	(30,200 )
Other income	1,400	1,799
Total revenues	234,201	204,337
Provision for losses	413,973	529,091
Change in reserve for premium deficiency	(1,383 )	(1,231 )
Policy acquisition costs	10,216	10,504
Other operating expenses	34,137	46,233
Interest expense	9,789	2,120
Total expenses	466,732	586,717
Equity in net income of affiliates	—	—
Pretax loss	(232,531 )	(382,380 )
Income tax provision (benefit)	3,501	(145,847 )
Net loss	\$(236,032 )	\$(236,533 )
Cash and investments	\$3,977,445	\$3,546,637
Deferred policy acquisition costs	42,322	36,762
Total assets	4,471,425	4,919,093
Unearned premiums	191,910	219,753
Reserve for losses and LAE	3,542,797	3,597,035
VIE debt	72,369	268,443
Derivative liabilities	—	—

Radian Group Inc.

Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

(In thousands)	Three Months Ended	
	March 31, 2011	2010
Financial Guaranty		
Net premiums written—insurance	\$ 1,903	\$(1,531 )
Net premiums earned—insurance	\$ 16,889	\$ 20,929
Net investment income	15,407	18,999
Net gains on investments	19,673	29,167
Net impairment losses recognized in earnings	—	—
Change in fair value of derivative instruments	244,286	(78,231 )
Net gains (losses) on other financial instruments	72,785	(71,364 )
Other income	48	3,913
Total revenues	369,088	(76,587 )
Provision for losses	13,400	14,789
Change in reserve for premium deficiency	—	—
Policy acquisition costs	3,915	4,364
Other operating expenses	12,082	18,673
Interest expense	7,235	8,684
Total expenses	36,632	46,510
Equity in net income of affiliates	65	78
Pretax income (loss)	332,521	(123,019 )
Income tax benefit	(6,517 )	(44,041 )
Net income (loss)	\$ 339,038	\$(78,978 )
Cash and investments	\$ 2,464,819	\$ 2,523,751
Deferred policy acquisition costs	103,399	120,169
Total assets	2,880,138	3,161,663
Unearned premiums	474,109	560,808
Reserve for losses and LAE	84,898	138,789
VIE debt	300,638	327,618
Derivative liabilities	487,345	234,504

Radian Group Inc.  
Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

(In thousands)	Three Months Ended March 31, 2010
Financial Services	
Net premiums written—insurance	\$—
Net premiums earned—insurance	\$—
Net investment income	—
Net gains on investments	—
Net impairment losses recognized in earnings	—
Change in fair value of derivative instruments	—
Net (losses) gains on other financial instruments	—
Gain on sale of affiliate	—
Other income	63
Total revenues	63
Provision for losses	—
Change in reserve for premium deficiency	—
Policy acquisition costs	—
Other operating expenses	150
Interest expense	—
Total expenses	150
Equity in net income of affiliates	8,020
Pretax income	7,933
Income tax provision	2,777
Net income	\$5,156
Cash and investments	\$—
Deferred policy acquisition costs	—
Total assets	127,402
Unearned premiums	—
Reserve for losses and LAE	—
VIE debt	—
Derivative liabilities	—

A reconciliation of segment net income (loss) to consolidated net income (loss) is as follows:

(In thousands)	Three Months Ended March 31,	
	2011	2010
Consolidated		
Net income (loss):		
Mortgage Insurance	\$(236,032)	\$(236,533)
Financial Guaranty	339,038	(78,978)
Financial Services	—	5,156
Total	\$103,006	\$(310,355)



Radian Group Inc.

Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

## 3. Derivative Instruments

The following table sets forth our gross unrealized gains and gross unrealized losses on derivative assets and liabilities as of the dates indicated. Certain contracts are in an asset position because the net present value of the contractual premium we receive exceeds the net present value of our estimate of the expected future premiums that a financial guarantor of similar credit quality to us would charge to provide the same credit protection, assuming a transfer of our obligation to such financial guarantor as of the measurement date.

(In millions)	March 31, 2011	December 31, 2010
Balance Sheets		
Derivative assets:		
Financial Guaranty credit derivative assets	\$ 15.1	\$ 14.5
Net interest margin securities ("NIMS") assets	9.0	10.8
Other	0.5	0.9
Total derivative assets	24.6	26.2
Derivative liabilities:		
Financial Guaranty credit derivative liabilities	469.9	704.4
Financial Guaranty VIE derivative liabilities	17.4	19.2
Total derivative liabilities	487.3	723.6
Total derivative liabilities, net	\$(462.7	) \$(697.4

The notional value of our derivative contracts at March 31, 2011, and December 31, 2010, was \$41.3 billion and \$41.6 billion, respectively.

The components of the gains (losses) included in change in fair value of derivative instruments are as follows:

(In millions)	Three Months Ended March 31, 2011	2010
Statements of Operations		
Net premiums earned—derivatives	\$ 10.9	\$ 12.1
Financial Guaranty credit derivatives	234.6	(84.1
Financial Guaranty VIE derivative liabilities	(0.9	) (3.2
NIMS	(1.9	) (0.2
Put options on CPS	—	(2.1
Other	1.2	(0.5
Change in fair value of derivative instruments	\$ 243.9	\$(78.0

The valuation of derivative instruments may result in significant volatility from period to period in gains and losses as reported on our condensed consolidated statements of operations. Generally, these gains and losses result from changes in corporate credit or asset-backed spreads and changes in the creditworthiness of underlying corporate entities or the credit performance of the assets underlying asset-backed securities ("ABS"). Additionally, when determining the fair value of our liabilities, we are required to incorporate into the fair value of those liabilities an adjustment that reflects our own non-performance risk and consequently, changes in the market's perception of our non-performance risk also result in gains and losses on our derivative instruments. Any incurred gains or losses on our financial guaranty contracts that are accounted for as derivatives are recognized as a change in fair value of derivative instruments. See Note 4 for information on our fair value of financial instruments.





Radian Group Inc.  
Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The following table shows selected information about our derivative contracts:

(\$ in millions)	March 31, 2011		
	Number of Contracts	Par/ Notional Exposure	Total Net Asset/ (Liability)
Product			
NIMS related and other (1)	—	\$—	\$ 9.5
Corporate collateralized debt obligations ("CDOs")	84	33,511.3	(45.7 )
Non-Corporate CDOs and other derivative transactions:			
Trust Preferred Securities ("TruPs")	19	2,006.7	(211.8 )
CDOs of commercial mortgage-backed securities ("CMBS")	4	1,831.0	(54.3 )
Other:			
Structured finance	9	833.7	(82.3 )
Public finance	26	1,693.9	(37.6 )
Total Non-Corporate CDOs and other derivative transactions	58	6,365.3	(386.0 )
Assumed financial guaranty credit derivatives:			
Structured finance	274	1,083.0	(19.0 )
Public finance	14	350.5	(4.1 )
Total Assumed	288	1,433.5	(23.1 )
Financial Guaranty VIE derivative liabilities (2)	—	—	(17.4 )
Grand Total	430	\$41,310.1	\$ (462.7 )

Represents NIMS derivative assets related to consolidated NIMS VIEs. Also includes one common stock warrant.

(1) Because neither of these investments represent financial guaranty contracts that we issued, they cannot become liabilities, and therefore, do not represent additional par exposure.

Represents the fair value of an interest rate swap included in the consolidation of one of our financial guaranty transactions. The notional amount of the interest rate swap does not represent additional par exposure, and (2) therefore, is excluded from this table. See Note 5 for information on our maximum exposure to loss from our consolidated financial guaranty transactions.

#### 4. Fair Value of Financial Instruments

Our fair value measurements are intended to reflect the assumptions market participants would use in pricing an asset or liability based on the best information available. Assumptions include the risks inherent in a particular valuation technique (such as a pricing model) and the risks inherent in the inputs to the model. We define fair value as the current amount that would be exchanged to sell an asset or transfer a liability, other than in a forced liquidation. In the event that our investments or derivative contracts were sold or transferred in a forced liquidation, the amounts received or paid may be materially different than those determined in accordance with the accounting standard regarding fair value measurements. There have been no significant changes to our fair value methodologies during the quarter ended March 31, 2011.

When determining the fair value of our liabilities, we are required to incorporate into the fair value of those liabilities an adjustment that reflects our own non-performance risk. Radian Group's five-year credit default swap ("CDS") spread is the only observable quantitative measure of our non-performance risk and is used by typical market

participants to determine the likelihood of default. As Radian Group's CDS spread tightens or widens, it has the effect of increasing or decreasing, respectively, the fair value of our liabilities.

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The following table quantifies the impact of our non-performance risk on our derivative assets, derivative liabilities (in aggregate by type, excluding assumed financial guaranty derivatives) and VIE liabilities presented in our condensed consolidated balance sheets. Radian Group's five-year CDS spread is presented as an illustration of the market's view of our non-performance risk; the CDS spread actually used in the valuation of specific fair value liabilities is typically based on the remaining term of the instrument.

(In basis points)	March 31, 2011	December 31, 2010	March 31, 2010	December 31, 2009
Radian Group's five-year CDS spread	642	465	983	1,530

(In millions)	Fair Value Liability before Consideration of Radian Non-Performance Risk March 31, 2011	Impact of Radian Non-Performance Risk March 31, 2011	Fair Value Liability Recorded March 31, 2011
Product			
Corporate CDOs	\$(324.1)	) \$278.4	\$(45.7)
Non-Corporate CDO-related (1)	(1,579.1)	) 1,072.5	(506.6)
NIMS-related (2)	(68.8)	) 5.4	(63.4)
Total	\$(1,972.0)	) \$1,356.3	\$(615.7)

(In millions)	Fair Value Liability before Consideration of Radian Non-Performance Risk December 31, 2010	Impact of Radian Non-Performance Risk December 31, 2010	Fair Value Liability Recorded December 31, 2010
Product			
Corporate CDOs	\$(387.1)	) \$281.5	\$(105.6)
Non-Corporate CDO-related (1)	(1,696.2)	) 934.1	(762.1)
NIMS-related (2)	(134.1)	) 4.8	(129.3)
Total	\$(2,217.4)	) \$1,220.4	\$(997.0)

(1) Includes the net liability recorded within derivative assets and derivative liabilities, and the net liability recorded within VIE debt and other financial statement line items for consolidated VIEs.

(2) Includes NIMS VIE debt and NIMS derivative assets.

The cumulative impact attributable to the market's perception of our non-performance risk increased by \$0.1 billion during the first three months of 2011, as presented in the table above. This increase was primarily the result of the widening of Radian Group's CDS spreads during this period.

We established a fair value hierarchy by prioritizing the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level I measurements) and the lowest priority to unobservable inputs (Level III measurements). The three levels of the fair value hierarchy under this standard are described below:

Level I—Unadjusted quoted prices or valuations in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

Level II—Quoted prices or valuations in markets that are not active or financial instruments for which all significant inputs are observable, either directly or indirectly; and

Level III—Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable.

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The level of market activity in determining the fair value hierarchy is based on the availability of observable inputs market participants would use to price an asset or a liability, including market value price observations. For markets in which inputs are not observable or limited, we use significant judgment and assumptions that a typical market participant would use to evaluate the market price of an asset or liability. These assets and liabilities are classified in Level III of our fair value hierarchy.

A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. At March 31, 2011, our total Level III assets were approximately 3.9% of total assets measured at fair value and total Level III liabilities accounted for 100% of total liabilities measured at fair value.

Available for sale securities, trading securities, VIE debt, derivative instruments, and certain other assets are recorded at fair value. All derivative instruments and contracts are recognized in our condensed consolidated balance sheets as either derivative assets or derivative liabilities. All changes in the fair value of trading securities, VIE debt, derivative instruments and certain other assets are included in our condensed consolidated statements of operations. All changes in the fair value of available for sale securities are recorded in accumulated other comprehensive income (loss).

The following is a list of those assets and liabilities that are measured at fair value by hierarchy level as of March 31, 2011:

(In millions)	Level I	Level II	Level III	Total
Assets and Liabilities at Fair Value				
Investment Portfolio:				
U.S. government and agency securities	\$707.5	\$744.8	\$—	\$1,452.3
State and municipal obligations	—	1,220.8	23.2	1,244.0
Money market instruments	365.8	—	—	365.8
Corporate bonds and notes	—	1,005.0	—	1,005.0
Residential mortgage-backed securities ("RMBS")	—	913.1	55.3	968.4
CMBS	—	193.1	24.0	217.1
CDO	—	—	4.1	4.1
Other ABS	—	120.8	4.7	125.5
Foreign government securities	—	70.1	—	70.1
Hybrid securities	—	367.6	—	367.6
Equity securities (1)	178.3	165.3	4.3	347.9
Other investments (2)	—	151.6	3.9	155.5
Total Investments at Fair Value (3)	1,251.6	4,952.2	119.5	6,323.3
Derivative Assets	—	0.5	24.1	24.6
Other Assets (4)	—	—	106.3	106.3
Total Assets at Fair Value	\$1,251.6	\$4,952.7	\$249.9	\$6,454.2
Derivative Liabilities	\$—	\$—	\$487.3	\$487.3
VIE debt (5)	—	—	373.0	373.0
Total Liabilities at Fair Value	\$—	\$—	\$860.3	\$860.3

(1) Comprised of broadly diversified domestic equity mutual funds included within Level I and various preferred and common stocks invested across numerous companies and industries included within Level II and III.

Comprised of short-term commercial paper within CPS trusts (\$150.0 million) and short-term CDs (\$1.6 million)

(2) included within Level II and lottery annuities (\$1.8 million) and TruPs held by consolidated VIEs (\$2.1 million) included within Level III.

- Does not include fixed-maturities held to maturity (\$8.7 million) and other invested assets (\$61.2 million),
- (3) primarily invested in limited partnerships, accounted for as cost-method investments and not measured at fair value.
  - (4) Comprised of manufactured housing loan collateral related to two consolidated financial guaranty VIEs.
  - (5) Comprised of consolidated debt related to NIMS VIEs (\$72.4 million) and amounts related to financial guaranty VIEs (\$300.6 million).

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The following is a list of those assets and liabilities that are measured at fair value by hierarchy level as of December 31, 2010:

(In millions)	Level I	Level II	Level III	Total
Assets and Liabilities at Fair Value				
Investment Portfolio:				
U.S. government and agency securities	\$1,075.0	\$731.4	\$—	\$1,806.4
State and municipal obligations	—	1,159.7	23.2	1,182.9
Money market instruments	310.9	—	—	310.9
Corporate bonds and notes	—	1,060.4	—	1,060.4
RMBS	—	913.5	52.5	966.0
CMBS	—	173.6	23.0	196.6
CDO	—	—	2.4	2.4
Other ABS	—	131.1	3.3	134.4
Foreign government securities	—	83.5	—	83.5
Hybrid securities	—	318.9	—	318.9
Equity securities (1)	168.4	168.6	2.9	339.9
Other investments (2)	—	150.0	4.6	154.6
Total Investments at Fair Value (3)	1,554.3	4,890.7	111.9	6,556.9
Derivative Assets	—	—	26.2	26.2
Other Assets (4)	—	—	109.7	109.7
Total Assets at Fair Value	\$1,554.3	\$4,890.7	\$247.8	\$6,692.8
Derivative Liabilities	\$—	\$—	\$723.6	\$723.6
VIE debt (5)	—	—	520.1	520.1
Total Liabilities at Fair Value	\$—	\$—	\$1,243.7	\$1,243.7

(1) Comprised of broadly diversified domestic equity mutual funds included within Level I and various preferred and common stocks invested across numerous companies and industries included within Level II and III.

(2) Comprised of short-term commercial paper within CPS trusts included within Level II and lottery annuities (\$2.6 million) and TruPs held by consolidated VIEs (\$2.0 million) included within Level III.

Does not include fixed-maturities held to maturity (\$10.8 million), certain short-term investments (\$1.6 million), (3) primarily invested in CDs and time deposits, and other invested assets (\$59.6 million), primarily invested in limited partnerships, accounted for as cost-method investments and not measured at fair value.

(4) Comprised of manufactured housing loan collateral related to two consolidated financial guaranty VIEs.

Comprised of consolidated debt related to NIMS VIEs (\$141.0 million) and amounts related to financial guaranty (5) VIEs (\$379.1 million) that required consolidation as of January 1, 2010, under the accounting standard update regarding improvements to financial reporting by enterprises involving VIEs.

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The following is a rollforward of Level III assets and liabilities measured at fair value for the quarter ended March 31, 2011:

(In millions)	Beginning Balance at January 1, 2011	Realized and Unrealized Gains (Losses) Recorded in Earnings (1)	Purchases	Sales	Issuances	Settlements	Transfers Into (Out of) Level III (2)	Ending Balance at March 31, 2011	
Investments:									
State and municipal obligations	\$23.2	\$ —	\$—	\$—	\$—	\$—	\$ —	\$23.2	
RMBS	52.5	4.0	—	—	—	(1.2	) —	55.3	
CMBS	23.0	1.0	—	—	—	—	—	24.0	
CDO	2.4	1.6	—	—	—	0.1	—	4.1	
Other ABS	3.3	1.4	—	—	—	—	—	4.7	
Hybrid securities	—	(0.7	) 0.7	—	—	—	—	—	
Equity securities	2.9	0.4	1.1	(0.1	) —	—	—	4.3	
Other investments	4.6	0.1	—	(0.5	) —	(0.3	) —	3.9	
Total Level III Investments	111.9	7.8	1.8	(0.6	) —	(1.4	) —	119.5	
NIMS derivative assets	11.7	(2.4	) 0.1	—	—	—	(0.4	) 9.0	
Other assets	109.7	3.9	—	—	—	(7.3	) —	106.3	
Total Level III Assets, net	\$233.3	\$ 9.3	\$1.9	\$(0.6	) \$—	\$(8.7	) \$ (0.4	) \$234.8	
Derivative liabilities, net	\$(709.1	) \$ 244.7	\$—	\$—	\$—	\$(7.8	) \$ —	\$(472.2	)
VIE debt	(520.1	) 72.9	—	—	—	74.2	—	(373.0	)
Total Level III liabilities, net	\$(1,229.2)	\$ 317.6	\$—	\$—	\$—	\$66.4	\$ —	\$(845.2	)

Includes unrealized gains (losses) relating to assets and liabilities still held as of March 31, 2011, as follows: \$6.8 (1) million for investments, \$(2.0) million for NIMS derivative assets, \$0.8 million for other assets, \$229.2 million for derivative liabilities, and \$0.7 million for VIE debt.

(2) Transfers are recognized at the end of the period as the availability of market observed inputs change from period to period.

There were no investment transfers between Level I and Level II during the first quarter of 2011 or 2010.





## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The following is a rollforward of Level III assets and liabilities measured at fair value for the quarter ended March 31, 2010:

(In millions)	Beginning Balance at January 1, 2010	VIE Consolidation at January 1, 2010 (1)	Realized and Unrealized Gains(Losses) Recorded in Earnings (2)	Purchases	Sales	Issuance	Settlements	Transfers Into (Out of) Level III (3)	Ending Balance at March 31, 2010
Investments:									
State and municipal obligations	\$ 24.4	\$ —	\$ —	\$—	\$—	\$—	\$—	\$ —	\$24.4
RMBS	—	44.3	12.0	—	(2.2 )	—	—	—	54.1
CMBS	—	23.8	0.5	—	—	—	—	—	24.3
CDO	—	3.8	(0.1 )	—	0.1	—	—	—	3.8
Other ABS	—	3.5	—	—	—	—	—	—	3.5
Hybrid securities	0.6	—	—	—	—	—	—	0.5	1.1
Equity securities	1.7	—	(0.3 )	0.1	—	—	—	—	1.5
Other investments	3.8	3.7	—	—	(0.8 )	—	—	—	6.7
Total Level III Investments	30.5	79.1	12.1	0.1	(2.9 )	—	—	0.5	119.4
NIMS and CPS derivative assets	44.7	—	(2.8 )	0.2	—	—	0.4	—	42.5
Other assets	—	119.7	2.0	—	—	—	(3.4 )	—	118.3
Total Level III Assets, net	\$ 75.2	\$ 198.8	\$ 11.3	\$0.3	\$(2.9 )	\$—	\$(3 )	\$ 0.5	\$280.2
Derivative liabilities, net	\$ (214.9 )	\$ 51.8	\$ (75.1 )	\$—	\$—	\$—	\$ 28	\$ —	\$(210.2 )
VIE debt	(296.1 )	(253.5 )	(107.0 )	—	—	—	60.5	—	(596.1 )
Total Level III liabilities, net	\$ (511.0 )	\$ (201.7 )	\$ (182.1 )	\$—	\$—	\$—	\$ 88.5	\$ —	\$(806.3 )

(1) Represents the impact of our adoption of the accounting standard update regarding improvements to financial reporting by enterprises involving VIEs.

Includes unrealized gains (losses) relating to assets and liabilities still held as of March 31, 2010 as follows: \$11.6 (2) million for investments, \$(0.2) million for NIMS derivative assets, \$(1.7) million for CPS derivative assets, \$2.0 million for other assets, \$(88.8) million for derivative liabilities, and \$(31.0) million for VIE debt.

(3) Transfers are recognized at the end of the period as the availability of market observed inputs change from period to period.



## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

## Other Fair Value Disclosure

The carrying value and estimated fair value of other selected assets and liabilities not carried at fair value on our condensed consolidated balance sheets were as follows:

(In millions)	March 31, 2011		December 31, 2010	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets:				
Fixed-maturities held to maturity	\$8.7	\$9.3	\$10.8	\$11.4
Short-term investments (carried at cost)	—	—	1.6	1.6
Other invested assets	61.2	62.6	59.6	58.4
Liabilities:				
Long-term debt	968.2	1,039.0	964.8	1,082.5
Non-derivative financial guaranty liabilities	407.5	520.5	406.1	531.1

## 5. VIEs

The following information provides additional detail related to our consolidated and unconsolidated VIEs.

## NIMS VIEs

We consolidate all of the assets and liabilities associated with NIMS VIEs, due to contractual provisions that allow us to purchase assets of the VIEs and thus direct the activities that most significantly impact the economic performance of each VIE. For this reason, we have concluded that we have the power to most significantly impact the economic performance of these VIEs. As the guarantor of either all or a significant portion of the debt issued by each NIMS VIE, we have the obligation to absorb losses that are significant to the VIEs. As a result, we have concluded that we are the primary beneficiary of these VIEs. The consolidated NIMS assets are accounted for as derivatives and represent assets to be used to settle the obligation of the VIEs. We elected the fair value option as it relates to the NIMS VIE debt, and therefore, the consolidated NIMS VIE debt is recorded at fair value. Our VIE debt includes amounts for which third parties do not have recourse to us.

Our continued involvement with the NIMS VIEs also includes a risk mitigation initiative, under which we purchased one NIMS bond during the first three months of 2011, with \$0.9 million face value and a purchase price approximately equal to our fair value liability at the time of purchase, which effectively eliminates the guarantee that we had issued to the VIE with respect to such bond and limits our liability to the discounted purchase price. In total, our net cash outflow related to NIMS during 2011 has been primarily as a result of claim payments. The average remaining maturity of our existing NIMS transactions is approximately two years. The following tables provide a summary of our maximum exposure to losses, and the financial impact on our condensed consolidated balance sheets, our condensed consolidated statements of operations and our condensed consolidated statements of cash flows as of and for the periods indicated, as it relates to our consolidated NIMS VIEs:

(In millions)	March 31, 2011	December 31, 2010
Balance Sheet:		
Derivative assets	\$9.0	\$10.8
VIE debt—at fair value	72.4	141.0
Maximum exposure (1)	69.3	135.8

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(1) The difference between the carrying amounts of the net asset/liability position and maximum exposure related to VIEs is primarily due to the difference between the face amount of the obligation and the recorded fair values, which includes an adjustment for our non-performance risk. The maximum exposure is based on the net par amount of our insured obligation as of the reporting date.

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

(In millions)	Three Months Ended	
	March 31, 2011	2010
Statement of Operations:		
Net investment income	\$0.1	\$—
Change in fair value of derivative instruments—loss	(1.9	) (0.2
Net gain (loss) on other financial instruments	2.4	(30.7
Net Cash Outflow	66.2	50.1

## Put Options on CPS

Radian Group and its subsidiaries have purchased by tender offer and privately negotiated transactions substantially all of the face amount of the CPS issued by the custodial trusts. Our continued involvement with these VIEs includes the payment of a put premium representing the spread between the assets of each trust and the relevant CPS, which has typically been de minimis. We eliminate the premium associated with the purchased CPS.

Based on our involvement in these trusts, combined with the put options Radian Asset Assurance Inc. ("Radian Asset Assurance") holds on these trusts (which together are considered in the determination of the primary beneficiary), we concluded that we are the party that directs the activities that most significantly influence the economic performance of these VIEs and has the right to receive benefits that would be significant to these VIEs. This determination was based on a qualitative analysis which demonstrates that we have a variable interest in each of these VIEs, and therefore, we concluded that we are the primary beneficiary. As such, the assets and liabilities of these trusts were consolidated at their respective fair values, net of liabilities to us. The assets of the consolidated trusts are reported in short-term investments. During 2011, our net cash outflow related to our involvement with these VIEs was de minimis.

The following tables provide a summary of our maximum exposure to losses, and the financial impact on our condensed consolidated balance sheets, our condensed consolidated statements of operations and our condensed consolidated statements of cash flows as of and for the periods indicated, as it relates to our consolidated and unconsolidated CPS VIEs:

(In millions)	Consolidated	
	March 31, 2011	December 31, 2010
Balance Sheet:		
Short-term investments	\$150.0	\$150.0
Maximum exposure (1)	150.0	150.0

(1) The maximum exposure is based on our carrying amounts of the investments.

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

(In millions)	Consolidated		Unconsolidated (1)	
	Three Months Ended		Three Months Ended	
	March 31,		March 31,	
	2011	2010	2011	2010
Statement of Operations:				
Net gain (loss) on investments	\$0.1	\$(0.5 )	\$—	\$—
Change in fair value of derivative instruments—loss	—	—	—	(2.1 )
Net loss on other financial instruments	—	(0.3 )	—	—
Interest expense	—	0.1	—	—
Other operating expenses	0.1	0.1	—	—
Net Cash Outflow	—	29.5	—	0.4

(1) Activity displayed reflects the impact for the periods prior to June 30, 2010, for one CPS custodial trust that was not consolidated prior to that date.

## Financial Guaranty Insurance Contracts

We consolidate the assets and liabilities associated with one CDO of ABS transaction. Due to contractual provisions that allow us to direct the collateral manager to sell the underlying assets of the transaction, we concluded that we have the power to direct the activities that most significantly impact the economic performance of this VIE. In addition, as the guarantor of certain classes of debt issued by this VIE, we have the obligation to absorb losses that are significant to this VIE. The consolidated CDO of ABS VIE assets are accounted for as trading securities and represent assets to be used to settle the obligation of this VIE. While the assets of this VIE may only be used to settle the obligations of the trust, due to our guarantee, the creditors have recourse to our general credit for this consolidated VIE debt.

We also consolidate the assets and liabilities associated with two other financial guaranty transactions, in which we provided guarantees for VIEs that own manufactured housing loans, and which had previously been accounted for as insurance contracts. Due to the contractual provisions that allow us to replace and appoint the servicer who manages the collateral underlying the assets of the transactions, we concluded that we have power to direct the activities of these VIEs. In addition, as the guarantor of certain classes of debt issued by these VIEs, we have the obligation to absorb losses that could be significant to these VIEs. The assets of these VIEs may only be used to settle the obligations of the trusts, while due to the nature of our guarantees, creditors have recourse to our general credit as it relates to the VIE debt. However, due to the seniority of our insured bonds in these transactions, we do not expect to incur a loss from our involvement with these two VIEs; as such, we did not have a reserve recorded for these transactions as of March 31, 2011.

Our interests in VIEs for which we are not the primary beneficiary may be accounted for as insurance, reinsurance or credit derivatives. For insurance contracts, we record reserves for losses and LAE, and for derivative interests, we record cumulative changes in fair value as a corresponding derivative asset or derivative liability. Our primary involvement with VIEs relates to transactions in which we provide a financial guaranty to one or more classes of beneficial interest holders in the VIE. Underlying collateral in the VIEs includes residential and commercial mortgages, manufactured housing loans, consumer receivables and other financial assets sold to a VIE and repackaged into securities or similar beneficial interests.

In continually assessing our involvement with VIEs, we consider certain events such as the VIE's failure to meet certain contractual conditions, such as performance tests and triggers, servicer termination events and events of default, that should they occur, may provide us with additional control rights over the VIE. These events would cause us to reassess our initial determination of whether we are the primary beneficiary of a VIE. In addition, changes to its governance structure that would allow us to direct the activities of a VIE or our acquisition of additional financial interests in the VIE would also cause us to reassess our determination of whether we are the primary beneficiary of a VIE. Since many of our financial guaranty contracts provide us with substantial control rights over the activities of VIEs upon the occurrence of default or other performance triggers described above, we expect that additional VIEs may be consolidated by us if these events occur.



## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The following tables provide a summary of our maximum exposure to losses, and the financial impact on our condensed consolidated balance sheets, our condensed consolidated statements of operations and our condensed consolidated statements of cash flows as of and for the periods indicated, as it relates to our consolidated and unconsolidated financial guaranty insurance contracts and credit derivative VIEs:

(In millions)	Consolidated		Unconsolidated	
	March 31, 2011	December 31, 2010	March 31, 2011	December 31, 2010
<b>Balance Sheet:</b>				
Trading securities	\$90.2	\$ 83.2	\$—	\$ —
Derivative assets	—	—	5.6	6.0
Premiums receivable	—	—	4.7	5.2
Other assets	108.1	112.4	—	—
Unearned premiums	—	—	5.5	6.0
Reserve for losses and LAE	—	—	18.4	15.0
Derivative liabilities	17.4	19.2	410.3	585.9
VIE debt—at fair value	300.6	379.1	—	—
Accounts payable and accrued expenses	0.9	0.8	—	—
Maximum exposure (1)	582.7	584.6	6,585.2	6,874.2
(In millions)	Consolidated		Unconsolidated	
	Three Months Ended March 31, 2011	2010	Three Months Ended March 31, 2011	2010
<b>Statement of Operations:</b>				
Premiums earned	\$—	\$ —	\$0.5	\$ 0.7
Net investment income	2.1	2.7	—	—
Net gains on investments	8.0	12.4	—	—
Change in fair value of derivative instruments—(loss) gain	(0.9)	(3.2)	176.7	(81.6)
Net gain (loss) on other financial instruments	74.5	(73.3)	—	—
Other income	—	3.9	—	—
Provision for losses —increase	—	—	3.4	5.7
Interest expense	—	1.2	—	—
Other operating expenses	0.8	2.0	—	—
Net Cash Inflow (Outflow)	0.2	(0.7)	2.0	(37.4)

(1) The difference between the carrying amounts of the net asset/liability position and maximum exposure related to VIEs is primarily due to the difference between the face amount of the obligation and the recorded fair values, which includes an adjustment for our non-performance risk. The maximum exposure is based on the net par amount of our insured obligation as of the reporting date.



## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

## 6. Investments

Our held to maturity and available for sale securities within our investment portfolio consisted of the following as of the dates indicated:

(In thousands)	March 31, 2011		Gross Unrealized Gains	Gross Unrealized Losses
	Amortized Cost	Fair Value		
Fixed-maturities held to maturity:				
Bonds and notes:				
State and municipal obligations	\$8,743	\$9,250	\$523	\$16
	\$8,743	\$9,250	\$523	\$16
Fixed-maturities available for sale:				
U.S. government and agency securities	\$25,202	\$27,640	\$2,438	\$—
State and municipal obligations	269,926	197,420	222	72,728
Corporate bonds and notes	19,408	19,062	295	641
RMBS	11,508	11,994	502	16
CMBS	3,042	3,051	60	51
Other ABS	1,712	1,819	113	6
Other investments	1,647	1,736	89	—
	\$332,445	\$262,722	\$3,719	\$73,442
Equity securities available for sale (1)	\$160,083	\$194,921	\$34,847	\$9
Total debt and equity securities	\$501,271	\$466,893	\$39,089	\$73,467

(1) Comprised of broadly diversified domestic equity mutual funds (\$178.3 million fair value) and various preferred and common stocks invested across numerous companies and industries (\$16.6 million fair value).

(In thousands)	December 31, 2010		Gross Unrealized Gains	Gross Unrealized Losses
	Amortized Cost	Fair Value		
Fixed-maturities held to maturity:				
Bonds and notes:				
State and municipal obligations	\$10,773	\$11,416	\$662	\$19
	\$10,773	\$11,416	\$662	\$19
Fixed-maturities available for sale:				
U.S. government and agency securities	\$25,120	\$27,742	\$2,622	\$—
State and municipal obligations	269,185	199,187	272	70,270
Corporate bonds and notes	26,748	26,206	334	876
RMBS	11,952	12,538	600	14
CMBS	3,279	3,310	70	39
Other ABS	2,104	2,226	127	5
Other investments	2,407	2,590	183	—
	\$340,795	\$273,799	\$4,208	\$71,204
Equity securities available for sale (1)	\$160,242	\$184,365	\$24,188	\$65

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Total debt and equity securities	\$511,810	\$469,580	\$29,058	\$71,288
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(1) Comprised of broadly diversified domestic equity mutual funds (\$168.4 million fair value) and various preferred and common stocks invested across numerous companies and industries (\$16.0 million fair value).

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## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The trading securities within our investment portfolio, which are recorded at fair value, consisted of the following as of the dates indicated:

(In thousands)	March 31, 2011	December 31, 2010
Trading securities:		
U.S. government and agency securities	\$717,157	\$703,636
State and municipal obligations	1,046,582	983,680
Corporate bonds and notes	985,982	1,034,206
RMBS	956,405	953,416
CMBS	214,050	193,244
CDO	4,054	2,406
Other ABS	123,681	132,149
Foreign government securities	70,078	83,508
Hybrid securities	367,633	318,940
Equity securities	152,962	155,636
Other investments	2,135	2,000
Total	\$4,640,719	\$4,562,821

The following tables show the gross unrealized losses and fair value of our investments, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, as of the dates indicated:

March 31, 2011:	Less Than 12 Months			12 Months or Greater			Total		
(\$ in thousands)	# of securities	Fair Value	Unrealized Losses	# of securities	Fair Value	Unrealized Losses	# of securities	Fair Value	Unrealized Losses
Description of Securities									
State and municipal obligations	7	\$6,692	\$1,659	25	\$184,212	\$71,085	32	\$190,904	\$72,744
Corporate bonds and notes	25	12,179	627	1	403	14	26	12,582	641
RMBS	2	2,140	16	—	—	—	2	2,140	16
CMBS	2	674	12	1	1,012	39	3	1,686	51
Other ABS	2	510	6	—	—	—	2	510	6
Equity securities	2	104	9	—	—	—	2	104	9
Total	40	\$22,299	\$2,329	27	\$185,627	\$71,138	67	\$207,926	\$73,467

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

December 31, 2010:	Less Than 12 Months			12 Months or Greater			Total		
(\$ in thousands) Description of Securities	# of securities	Fair Value	Unrealized Losses	# of securities	Fair Value	Unrealized Losses	# of securities	Fair Value	Unrealized Losses
State and municipal obligations	6	\$3,507	\$110	26	\$189,194	\$70,179	32	\$192,701	\$70,289
Corporate bonds and notes	31	16,364	852	2	604	24	33	16,968	876
RMBS	1	1,436	14	—	—	—	1	1,436	14
CMBS	3	1,885	39	—	—	—	3	1,885	39
Other ABS	2	802	5	—	—	—	2	802	5
Equity securities	2	205	65	—	—	—	2	205	65
Total	45	\$24,199	\$1,085	28	\$189,798	\$70,203	73	\$213,997	\$71,288

During the first quarters of 2011 and 2010, there were no credit losses recognized in earnings.

At March 31, 2011, we did not have the intent to sell any debt securities in an unrealized loss position, and we determined that it is more likely than not that we will not be required to sell the securities before recovery of their cost basis.

Impairments due to deterioration in credit that result in a conclusion that the present value of cash flows expected to be collected will not be sufficient to recover the amortized cost basis of the security are considered other-than-temporary. Other declines in fair value (for example, due to interest rate changes, sector credit rating changes or company-specific rating changes) that result in a conclusion that the present value of cash flows expected to be collected will not be sufficient to recover the amortized cost basis of the security, may also result in a conclusion that an OTTI has occurred. To the extent we determine that a security is deemed to be other-than-temporarily impaired, an impairment loss is recognized.

We have securities that have been in an unrealized loss position for 12 months or more that we did not consider to be other-than-temporarily impaired as of March 31, 2011, due to the qualitative factors explained below.

#### State and Municipal Obligations

The majority of the unrealized losses of 12 months or greater duration as of March 31, 2011, relate to our interests in certain bonds issued as part of securitizations collateralized by the Master Settlement Agreement ("MSA") between the domestic tobacco manufacturers and the 46 states and certain territories party thereto. In December 2010, after a review of these tobacco settlement bonds, including bonds we own, Moody's Investor Service ("Moody's") took certain ratings actions on the tobacco settlement bonds, including placing 67 classes in 19 transactions under review for possible downgrade due primarily to a decline in the most recent annual MSA payment to the trusts. Based on our review of stressed cash flow scenarios and despite the decline in cash flows to the trusts, we expect the present value of cash flows to be collected from each security to be sufficient to recover our amortized cost basis. In addition, we do not believe it is more likely than not that we will be required to sell these investments before recovery of our amortized cost basis, nor did we intend to sell these investments as of March 31, 2011. We are monitoring the Moody's review closely and will update our OTTI analysis each period as new information develops that might cause us to change our assessment of projected cash flows or our intent to sell.

The unrealized losses of 12 months or greater duration as of March 31, 2011, on the remaining securities in this category were caused by interest rate or credit spread movement. We did not consider these investments to be other-than-temporarily impaired at March 31, 2011.

#### Corporate Bonds and Notes

The unrealized losses of 12 months or greater duration as of March 31, 2011, on the security in this category were caused by credit spread widening in the sector. Corporate spreads have tightened significantly over the past 12 months, although they remain wide relative to pre-2008 levels. As of March 31, 2011, we expect the present value of cash flows to be collected from this security to be sufficient to recover the amortized cost basis of this security. As of March 31, 2011, we did not intend to sell this investment, nor did we believe that it was more likely than not that we will be required to sell this investment before recovery of our amortized cost basis, which may be at maturity; therefore, we did not consider this investment to be other-than-temporarily impaired at March 31, 2011.

Radian Group Inc.

Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

**CMBS**

The unrealized losses of 12 months or greater duration as of March 31, 2011, on the security in this category were caused by credit spread widening in the sector. As of March 31, 2011, we expect the present value of cash flows to be collected from this security to be sufficient to recover the amortized cost basis of this security. As of March 31, 2011, we did not intend to sell this investment, nor did we believe that it was more likely than not that we will be required to sell this investment before recovery of our amortized cost basis, which may be at maturity; therefore, we did not consider this investment to be other-than-temporarily impaired.

For all investment categories, unrealized losses of less than 12 months in duration were generally attributable to interest rate or credit spread movements. All securities were evaluated in accordance with our impairment recognition policy covering various time and price decline scenarios.

The contractual maturities of fixed-maturity investments are as follows:

(In thousands)	March 31, 2011		Available for Sale	
	Held to Maturity			
	Amortized	Fair	Amortized	Fair
	Cost	Value	Cost	Value
Due in one year or less (1)	\$658	\$661	\$16,981	\$17,863
Due after one year through five years (1)	4,719	4,924	16,295	16,630
Due after five years through ten years (1)	3,065	3,381	7,618	7,715
Due after ten years (1)	301	284	275,289	203,650
RMBS (2)	—	—	11,508	11,994
CMBS (2)	—	—	3,042	3,051
Other ABS (2)	—	—	1,712	1,819
Total	\$8,743	\$9,250	\$332,445	\$262,722

(1) Actual maturities may differ as a result of calls before scheduled maturity.

(2) RMBS, CMBS and Other ABS are shown separately, as they are not due at a single maturity date.

**7. Losses and LAE**

Our reserve for losses and LAE, as of the dates indicated, was comprised of:

(In thousands)	March 31, 2011	December 31, 2010
Mortgage insurance reserves	\$3,542,797	\$3,524,971
Financial guaranty reserves	84,898	71,764
Total reserve for losses and LAE	\$3,627,695	\$3,596,735



Radian Group Inc.  
Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The following table presents information relating to our mortgage insurance reserves for losses and LAE as of the dates indicated:

(In thousands)	Three Months Ended	
	March 31, 2011	2010
Mortgage Insurance		
Balance at beginning of period	\$3,524,971	\$3,450,538
Less Reinsurance recoverables (1)	(223,254 )	(621,644 )
Balance at beginning of period, net of reinsurance recoverables	3,301,717	2,828,894
Add losses and LAE incurred in respect of default notices reported and unreported in:		
Current year (2)	190,686	251,287
Prior years	223,287	277,804
Total incurred	413,973	529,091
Deduct paid claims and LAE in:		
Current year (2)	(837 )	(18,966 )
Prior years	(364,314 )	(338,309 )
Total paid	(365,151 )	(357,275 )
Balance at end of period, net of reinsurance recoverables	3,350,539	3,000,710
Add Reinsurance recoverables (1)	192,258	596,325
Balance at end of period	\$3,542,797	\$3,597,035

Related to ceded losses on captive reinsurance transactions and Smart Home. See "Management's Discussion and (1) Analysis of Financial Condition and Results of Operations—Critical Accounting Policies—Off-Balance Sheet Arrangements" for additional information regarding our Smart Home transactions.

Related to underlying defaulted loans with a most recent date of default notice in the current year. For example, if a (2) loan had defaulted in a prior year, but then subsequently cured and re-defaulted in the current year, that default would be considered a current year default.

Our loss reserves were reduced in the first quarter of 2011 as a result of a decrease in our total inventory of defaults. However, our loss reserves were negatively impacted in the quarter by new default notices received in the current year, as well as an increase in the aggregate weighted average estimated rate at which defaults move to claim ("default to claim rate"), primarily due to an increase in the weighted average age of underlying defaulted loans, and an increase in our incurred but not recorded ("IBNR") reserve estimate. The increase in our IBNR estimate was related to an increase in our estimate of future reinstatements of previously rescinded policies and denied claims. Of the \$223.3 million prior year adverse development experienced in 2011, \$77.8 million related to an increase in our IBNR reserve estimate due to an increase in our estimate of the reinstatements of previously rescinded policies and denied claims, while the balance related primarily to the unanticipated impact of aging of underlying defaulted loans on our default to claim rate. With continuing declines in home values, persistently high unemployment and delays by servicers in either modifying loans or foreclosing on properties, the ability to cure a delinquent loan within our expected timeframe has become increasingly difficult to achieve. Consequently, our default inventory has experienced an increase in aging, and we apply higher estimated default to claim rates on our more aged delinquent loans, resulting in higher reserves. The protracted amount of time it has taken for servicers to resolve certain aged loans has extended the period of uncertainty with regard to our ultimate claim liability beyond what we predicted as of the prior year end.

As a consequence, our aggregate weighted average default to claim rate assumption (net of denials and rescissions) used in estimating our reserve for losses was 43% at March 31, 2011, compared to 40% at December 31, 2010. Our default to claim rate estimate varies depending on the age of the underlying defaulted loans, as measured by the number of monthly payments missed. As of March 31, 2011, our default to claim rate estimate, net of our estimate for insurance rescissions and claims denials, ranged from 19% for insured loans that had missed two to three monthly payments, to 51% for such loans that had missed 12 or more monthly payments.

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

Our reserve for losses includes the impact of our estimated rescissions and denials, which remain elevated compared to levels experienced prior to 2009. Rescissions and denials reduced our loss reserves as of March 31, 2011, by approximately \$783 million. The amount of estimated rescissions and denials incorporated into our reserve analysis at any point in time is affected by a number of factors, including not only our estimated rate of rescissions and denials on future claims, but also the volume and attributes of our defaulted insured loans, our estimated default to claim rate, and our estimated claim severity, among other assumptions. We expect the amount of estimated rescissions and denials embedded within our reserve analysis to decrease over time, as the defaults related to the poor underwriting periods of 2005 through 2008 decline as a proportion of our total default portfolio and as we realize the results through actual rescissions and denials, or the commutations of insured loans.

Our reported rescission and denial activity in any given period is subject to future challenges by our lender customers. Our IBNR reserve estimate, which includes an estimate of the future reinstatements of previously rescinded policies and denied claims, was \$116.2 million and \$39.5 million at March 31, 2011, and December 31, 2010, respectively. The change in this estimate primarily reflects recent trends in insurance rescissions and claim denial activity as a result of lenders challenging a greater number of rescissions and denials and the overall challenges being more substantive in nature (i.e., producing new or additional information that supports a reinstatement of coverage or a claim payment). As a result, we expect that an increasingly larger portion of previously rescinded policies will be reinstated and previously denied claims will be resubmitted with the required documentation and ultimately paid. The following table illustrates the impact to our loss reserve estimates due to estimated insurance rescissions and claim denials as of the dates indicated:

(In millions)	March 31, 2011	December 31, 2010
Decrease to our loss reserve due to estimated rescissions and denials	\$(783	) \$(922

The following table illustrates the amount of first-lien claims submitted to us for payment that were rescinded or denied, for the periods indicated, net of reinstatements within each period:

(In millions)	Three Months Ended March 31,	
	2011	2010
Rescissions—first loss position	\$93.8	\$129.4
Denials—first loss position	24.6	8.0
Total first loss position (1)	118.4	137.4
Rescissions—second loss position	31.0	110.4
Denials—second loss position	2.7	3.7
Total second loss position (2)	33.7	114.1
Total first-lien claims submitted for payment that were rescinded or denied (3)	\$152.1	\$251.5

(1) Related to claims from policies in which we were in a first loss position and would have paid the claim absent the rescission or denial.

Related to claims from policies in which we were in a second loss position. These rescissions or denials may not have resulted in a claim payment obligation due to deductibles and other exposure limitations included in our policies.

(3) Includes a small amount of submitted claims that were subsequently withdrawn by the insured.



## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The following table illustrates the total amount of first-lien claims submitted to us for payment that were rescinded in the years noted, and then subsequently were challenged ("rebutted") by the lenders and policyholders, but not reinstated, as of March 31, 2011:

(In millions)	2011	2010	2009
First loss position	\$33.5	\$153.6	\$97.7
Second loss position	8.4	59.1	87.8
Total non-overturned rebuttals on rescinded first-lien claims	\$41.9	\$212.7	\$185.5

While the total potential claim amount of non-overturned rebuttals outstanding represents all challenged rescissions for which coverage has not been reinstated, our ongoing, active engagement with our lender customers typically involves a small number of these non-overturned rebuttals. Absent litigation or other legal proceedings in which we are not successful, we do not expect that these discussions are likely to result in settlements that would materially impact our liquidity or results of operations.

We also accrue for the premiums that we expect to refund to our lender customers in connection with our estimated insurance rescission activity. Our accrued liability for such refunds, which is included within accounts payable and accrued expenses on our condensed consolidated balance sheets, was \$39.0 million and \$43.5 million as of March 31, 2011, and December 31, 2010, respectively.

The following table shows the cumulative denial and rescission rates, net of reinstatements, as of March 31, 2011, on our total first-lien portfolio for each quarter in which the claims were received for the periods indicated:

Claim Received Quarter	Cumulative Rescission Rate for Each Quarter (1)		Percentage of Claims Resolved (2)	
Q1 2008	12.2	%	100	%
Q2 2008	13.2	%	100	%
Q3 2008	19.3	%	100	%
Q4 2008	21.4	%	100	%
Q1 2009	24.4	%	99	%
Q2 2009	26.0	%	99	%
Q3 2009	23.5	%	99	%
Q4 2009	21.2	%	97	%
Q1 2010	18.4	%	94	%
Q2 2010	16.1	%	88	%
Q3 2010	9.3	%	74	%

Rescission rates represent the ratio of claims rescinded or denied to claims received (by claim count) and represent (as of March 31, 2011) the cumulative rate for each quarter based on number of claims received during that (1) quarter. Until all of the claims received during the periods shown have been resolved, the rescission rates for each quarter will be subject to change. These rates are also subject to change based on reinstatements of previously rescinded policies or denied claims.

(2) The percentage of claims resolved for each quarter presented in the table above, represents the number of claims that have been internally resolved as a percentage of the total number of claims received for that specific quarter. A claim is considered internally resolved when it is either paid or it is concluded that the claim should be denied or rescinded. For the fourth quarter of 2010 and the first quarter of 2011, a significant portion of claims received for

those quarters have not been internally resolved; therefore, we do not believe the cumulative rescission rates for those periods are presently meaningful.

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

We considered the sensitivity of first-lien loss reserve estimates at March 31, 2011, by assessing the potential changes resulting from a parallel shift in severity and default to claim rate. For example, assuming all other factors remain constant, for every one percentage point change in primary claim severity (which we estimate to be 27% of unpaid principal balance at March 31, 2011), we estimated that our loss reserves would change by approximately \$102 million at March 31, 2011. For every one percentage point change in pool claim severity (which we estimate to be 47% of unpaid principal balance at March 31, 2011), we estimated that our loss reserves would change by approximately \$9 million at March 31, 2011. For every one percentage point change in our overall default to claim rate (which we estimate to be 43% at March 31, 2011, including our assumptions related to rescissions and denials), we estimated a \$73 million change in our loss reserves at March 31, 2011.

## 8. Reserve for Premium Deficiency

We perform a quarterly evaluation of the expected profitability of our existing mortgage insurance portfolio, by business line, over the remaining life of the portfolio. A premium deficiency reserve ("PDR") is established when the present value of expected losses and expenses for a particular product line exceeds the present value of expected future premiums and existing reserves for that product line. We consider our first-lien and second-lien mortgage ("second-lien") insured portfolios to be separate lines of business as they are managed separately, priced differently and have a different customer base.

Numerous factors affect our ultimate default to claim rates, including home price changes, unemployment, the impact of our loss mitigation efforts and interest rates, as well as potential benefits associated with lender and governmental initiatives to modify loans and ultimately reduce foreclosures. To assess the need for a PDR on our first-lien insurance portfolio, we develop loss projections based on modeled loan defaults related to our current risk in force ("RIF"). This projection is based on recent trends in default experience, severity, and rates of defaulted loans moving to claim (such default to claim rates are net of our estimates of rescissions and denials), as well as recent trends in the rate at which loans are prepaid. As of March 31, 2011, our modeled loan default projections for our first-lien insured portfolio assume that the rate at which current loans will default will remain consistent with those rates observed at December 31, 2010, for the next six months, and will gradually return to normal historical levels over the subsequent two years.

The following table illustrates our net projected premium excess on our first-lien portfolio as of the dates indicated:

(In millions):	March 31, 2011	December 31, 2010
First-lien portfolio		
Net present value of expected premiums	\$2,647	\$2,806
Net present value of expected losses and expenses	(4,497)	(4,537)
Reserve for premiums and losses established, net of reinsurance recoverables	3,324	3,276
Net projected premium excess	\$1,474	\$1,545

For our first-lien insurance business, because the combination of the net present value of expected premiums and already established reserves (net of reinsurance recoverables) exceeds the net present value of expected losses and expenses, a first-lien PDR was not required as of March 31, 2011. Expected losses are based on an assumed paid claim rate of approximately 12.4% on our total primary first-lien insurance portfolio, which includes both delinquent loans and performing loans, comprising 9.5% on prime, 26.1% on subprime and 25.5% on Alternative-A ("Alt-A"). New business originated since the beginning of 2009 is expected to be profitable, which has contributed to the overall expected net profitability of our first-lien portfolio. In addition, estimated rescissions and denials on insured loans are expected to partially offset the impact of expected defaults and claims.

In the third quarter of 2007, we established a reserve for premium deficiency on our second-lien business. We were required to establish a PDR because the net present value of the expected future losses and expenses exceeded our expected future premiums. Since that time, our PDR has been reduced as premiums are earned, the risk is reduced (either through attrition or terminations of transactions), claims have been paid, or changes have occurred to our initial assumptions.



## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The following table reconciles our mortgage insurance segment's beginning and ending second-lien PDR for the periods indicated:

(In thousands)	Three Months Ended March 31,	
	2011	2010
Second-lien PDR		
Balance at beginning of period	\$ 10,736	\$ 25,357
Incurred losses recognized in loss reserves	(2,805 )	(5,080 )
Premiums recognized in earned premiums	620	510
Changes in underlying assumptions	(129 )	3,486
Accretion of discount and other	931	(147 )
Balance at end of period	\$ 9,353	\$ 24,126

## 9. Financial Guaranty Insurance Contracts

The following table includes information as of March 31, 2011, regarding our financial guaranty claim liabilities, segregated by the surveillance categories that we use in monitoring the risks related to these contracts:

(\$ in millions)	Surveillance Categories				Total
	Performing	Special Mention	Intensified Surveillance	Case Reserve	
Number of policies	7	150	64	110	331
Remaining weighted-average contract period (in years)	22	20	21	26	21
Insured contractual payments outstanding:					
Principal	\$ 27.5	\$ 1,251.2	\$ 405.1	\$ 347.5	\$ 2,031.3
Interest	10.9	838.8	174.7	182.6	1,207.0
Total	\$ 38.4	\$ 2,090.0	\$ 579.8	\$ 530.1	\$ 3,238.3
Gross claim liability	\$ 0.4	\$ 20.1	\$ 148.9	\$ 103.1	\$ 272.5
Less:					
Gross potential recoveries	—	0.7	66.7	79.6	147.0
Discount, net	0.1	6.8	20.1	0.3	27.3
Net claim liability	\$ 0.3	\$ 12.6	\$ 62.1	\$ 23.2	\$ 98.2
Unearned premium revenue	\$ 0.1	\$ 33.3	\$ 9.9	\$ —	\$ 43.3
Claim liability reported in the balance sheet	\$ 0.2	\$ 3.3	\$ 53.9	\$ 23.2	\$ 80.6
Reinsurance recoverables	\$ —	\$ —	\$ —	\$ —	\$ —

Claim liabilities may be established for a performing credit if the expected losses on the credit exceed the unearned premium revenue for the contract based on the present value of the expected net cash outflows. Included in accounts and notes receivable and unearned premiums on our condensed consolidated balance sheets are the present value of premiums receivable and unearned premiums that are received on an installment basis. The premiums receivable is net of commissions on assumed reinsurance business. The present values of the premiums receivable and unearned premiums as of the dates indicated are as follows:

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(In millions)	March 31, 2011	December 31, 2010
Premiums receivable	\$43.8	\$44.0
Unearned premiums	59.0	60.5

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## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The accretion of these balances is included in premiums written and premiums earned for premiums receivable and policy acquisition costs for commissions on our condensed consolidated statement of operations. The amounts of the accretion included in premiums written, premiums earned and policy acquisition costs for the periods indicated are as follows:

(In millions)	Three Months Ended March 31,	
	2011	2010
Premiums written	\$0.3	\$0.4
Premiums earned	0.3	0.4
Policy acquisition costs	0.1	0.1

The weighted-average risk-free rate used to discount the premiums receivable and premiums to be collected was 2.6% at March 31, 2011.

The following table shows the nominal (non-discounted) premiums, net of commissions that are expected to be collected on financial guaranty contracts with installment premiums, included in premiums receivable as of March 31, 2011:

(In millions)	Future Expected Premium Payments
Second Quarter 2011	\$1.3
Third Quarter 2011	1.6
Fourth Quarter 2011	1.0
2011	3.9
2012	6.0
2013	3.8
2014	2.0
2015	3.4
2011 – 2015	19.1
2016 – 2020	12.7
2021 – 2025	8.7
2026 – 2030	5.8
After 2030	10.1
Total	\$56.4

The following table shows the rollforward of the net present value of premiums receivable for the periods indicated:

(In millions)	Three Months Ended March 31,	
	2011	2010
Balance at beginning of period	\$44.0	\$54.4
Payments received	(1.3)	(1.6)
Accretion	0.2	0.3
Adjustments to installment premiums	(0.1)	(0.3)

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Foreign exchange revaluation	1.0	(1.7	)
Balance at end of period	\$43.8	\$51.1	

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Radian Group Inc.

Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

Premiums earned were affected by the following for the periods indicated:

(In millions)	Three Months Ended March 31,	
	2011	2010
Refundings	\$4.8	\$9.5
Unearned premium acceleration upon establishment of case reserves	—	0.3
Foreign exchange revaluation, gross of commissions	1.3	(1.7)
Adjustments to installment premiums, gross of commissions	0.2	—
Total adjustment to premiums earned	\$6.3	\$8.1

The following table shows the expected contractual premium revenue from our existing financial guaranty portfolio, assuming no prepayments or refundings of any financial guaranty obligations, as of March 31, 2011:

(In millions)	Ending Net Unearned Premiums	Unearned Premium Amortization	Accretion	Total Premium Revenue
Second Quarter 2011	\$464.0	\$10.1	\$0.4	\$10.5
Third Quarter 2011	453.9	10.1	0.3	10.4
Fourth Quarter 2011	443.0	10.9	0.3	11.2
2011	443.0	31.1	1.0	32.1
2012	405.5	37.5	1.3	38.8
2013	368.7	36.8	1.2	38.0
2014	333.7	35.0	1.1	36.1
2015	302.1	31.6	1.0	32.6
2011 – 2015	302.1	172.0	5.6	177.6
2016 – 2020	175.2	126.9	4.1	131.0
2021 – 2025	89.3	85.9	2.8	88.7
2026 – 2030	39.4	49.9	1.8	51.7
After 2030	—	39.4	2.6	42.0
Total	\$—	\$474.1	\$16.9	\$491.0

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

The following table shows the significant components of the change in our financial guaranty claim liability for the periods indicated:

(In millions)	Three Months Ended	
	March 31, 2011	2010
Claim liability at beginning of period	\$67.4	\$121.8
Incurred losses and LAE:		
Increase in gross claim liability	19.3	40.1
Increase in gross potential recoveries	(3.2)	(23.4)
Increase in discount	(3.3)	(2.5)
Decrease in unearned premiums	0.6	1.0
Incurred losses and LAE	13.4	15.2
Paid losses and LAE	(0.2)	(3.6)
Claim liability at end of period	\$80.6	\$133.4
Components of incurred losses and LAE:		
Claim liability established in current period	\$—	\$0.9
Changes in existing claim liabilities	13.4	14.3
Total incurred losses and LAE	\$13.4	\$15.2
Components of increase in discount:		
Increase in discount related to claim liabilities established in current period	\$(0.1)	\$(2.1)
Increase in discount related to existing claim liabilities	(3.2)	(0.4)
Total increase in discount	\$(3.3)	\$(2.5)
The weighted-average risk-free rates used to discount the gross claim liability and gross potential recoveries were as follows as of the dates indicated:		

December 31, 2009	4.34	%
March 31, 2010	4.39	%
December 31, 2010	3.69	%
March 31, 2011	4.11	%

## 10. Income Taxes

We provide for income taxes in accordance with the provisions of the accounting standard regarding accounting for income taxes. As required under this standard, our deferred tax assets and liabilities are recognized under the balance sheet method, which recognizes the future tax effect of temporary differences between the amounts recorded in our condensed consolidated financial statements and the tax bases of these amounts. Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in the periods in which the deferred tax asset or liability is expected to be realized or settled.

In 2010, in accordance with the accounting standard regarding the accounting and disclosure of income taxes in interim periods, we used an annualized effective tax rate to compute our tax expense each quarter. We adjusted this annualized effective tax rate each quarter by the following discrete items: (i) net gains or losses resulting from the change in fair value of our derivatives and other financial instruments, (ii) investment gains or losses, (iii) the

liabilities recorded under the accounting standard regarding accounting for uncertainty in income taxes, and (iv) prior year provision-to-filed tax return adjustments. Given the impact on our pre-tax results of net gains or losses resulting from our derivative transactions and our investment portfolio, and the continued uncertainty around our ability to rely on short-term financial projections, which directly affects our ability to estimate an effective tax rate for the full year of 2011, we booked our income tax benefit based on actual results of operations as of March 31, 2011.

## Radian Group Inc.

## Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

For federal income tax purposes, we have approximately \$2.3 billion of net operating loss ("NOL") carryforwards as of March 31, 2011. To the extent not utilized, the NOL carryforwards will expire during tax years 2028 through 2031. To protect our ability to utilize our NOLs and other tax assets from an "ownership change" under U.S. federal income tax rules, we adopted certain tax benefit preservation measures, including amendments to our certificate of incorporation and by-laws and the adoption of a tax benefit preservation plan.

As of March 31, 2011, before consideration of our valuation allowance, we had deferred tax assets ("DTA"), net of deferred tax liabilities, of approximately \$845.6 million. We are required to establish a valuation allowance against our DTA when it is more likely than not that all or some portion of our DTA will not be realized. At each balance sheet date, we assess our need for a valuation allowance and this assessment is based on all available evidence, both positive and negative, and requires management to exercise judgment and make assumptions regarding whether such DTA will be realized in future periods. Future realization of our DTA will ultimately depend on the existence of sufficient taxable income of the appropriate character (ordinary income or capital gains) within the applicable carryback and carryforward periods provided under the tax law. The primary sources of negative evidence that we considered are our cumulative losses in recent years, and the continued uncertainty around our future operating results. We also considered several sources of positive evidence when assessing the need for a valuation allowance such as future reversals of existing taxable temporary differences, future projections of taxable income, taxable income within the applicable carryback periods, and potential tax planning strategies. In making our assessment of the more likely than not standard, the weight assigned to the effect of both negative and positive evidence is commensurate with the extent to which such evidence can be objectively verified.

A valuation allowance of approximately \$818.1 million and \$851.9 million was recorded against our net DTA of approximately \$845.6 million and \$879.4 million at March 31, 2011, and December 31, 2010, respectively. The remaining DTA of approximately \$27.5 million represents our NOL carryback, which we expect to utilize in the coming months as a result of our anticipated settlement with the Internal Revenue Service ("IRS") relating to tax years 2000 through 2007.

## 11. Recent Accounting Pronouncements

There were no applicable new accounting pronouncements issued during the quarter ended March 31, 2011.

## 12. Selected Financial Information of Registrant—Radian Group

The following is selected financial information for Radian Group:

(In thousands)	March 31, 2011	December 31, 2010
Investment in subsidiaries, at equity in net assets	\$1,063,814	\$947,724
Total assets	1,984,080	1,864,896
Long-term debt	968,199	964,788
Total liabilities	1,011,183	1,005,116
Total stockholders' equity	972,897	859,780
Total liabilities and stockholders' equity	1,984,080	1,864,896

## 13. Commitments and Contingencies

On June 26, 2008, we filed a complaint for declaratory judgment in the United States District Court for the Eastern District of Pennsylvania, naming IndyMac Bank ("IndyMac"), Deutsche Bank National Trust Company ("Deutsche



Bank"), Financial Guaranty Insurance Company ("FGIC"), Ambac Assurance Corporation ("Ambac") and MBIA Insurance Corporation ("MBIA") as defendants. The suit involves three of our pool policies covering second-lien mortgages, entered into in late 2006 and early 2007 with respect to loans originated by IndyMac. We are in a second loss position behind IndyMac and in front of three defendant financial guaranty companies. We alleged that the representations and warranties made to us to induce us to issue the policies were materially false, and that as a result, the policies should be void. The total amount of our claim liability for all three pool policies was approximately \$77 million and represents the aggregate RIF related to these policies.

Radian Group Inc.  
Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

In March 2009, FGIC, Ambac and MBIA served us with demands to arbitrate certain issues relating to the same three pool policies that are the subject of our declaratory judgment complaint. In July 2009, the court declined to dismiss our declaratory judgment action, but stayed the action to permit the arbitrations to proceed first. In August 2009, we settled our dispute with Ambac and Deutsche Bank with respect to one of the disputed pool policies, which policy represents approximately \$27 million of the approximately \$77 million in total claim liability. In January 2010, we settled our dispute with MBIA and Deutsche Bank with respect to another of the disputed pool policies, which policy represents approximately \$21 million of the approximately \$77 million in total claim liability. These settlements resolved the declaratory judgment action as it pertains to Ambac and MBIA, and the arbitrations commenced by Ambac and MBIA were dismissed with prejudice. We have reached agreements in principle with FGIC and with Deutsche Bank, the essential terms of which will be submitted to the noteholders. These settlements are with respect to the third disputed pool policy, which policy represents the remaining \$29 million of the approximately \$77 million in total claim liability. The arbitration with FGIC and Deutsche Bank has been stayed indefinitely pending finalization and execution of the settlement agreement with FGIC and with Deutsche Bank.

On August 13, 2010, American Home Mortgage Servicing, Inc. ("AHMSI") filed a complaint against Radian Guaranty in the United States District Court for the Central District of California, on its own behalf and as servicer for certain RMBS insured by Radian Guaranty under 27 separate bulk primary mortgage insurance policies. AHMSI contends that in 2008, it mistakenly sent cancellation notices to Radian Guaranty for certain loans covered under these policies, and that Radian Guaranty wrongfully refused to reinstate coverage for these loans after AHMSI discovered the error. We believe there are approximately 256 loans for which insurance was not reinstated. According to AHMSI, Radian Guaranty's refusal to reinstate coverage was in breach of its contractual duties under the policies and in bad faith. AHMSI is seeking money damages and injunctive relief requiring Radian Guaranty to reinstate full coverage on all loans insured under the policies. On October 18, 2010, Radian Guaranty filed a motion to dismiss this case, which the court granted on December 16, 2010, stating that AHMSI failed to establish that it is the real party of interest. On January 5, 2011, AHMSI filed an amended complaint that included the trustee of the securities as an additional plaintiff to the complaint. On February 24, 2011, we filed a motion to dismiss the amended complaint and a motion to have this case moved to the United States District Court for the Eastern District of Pennsylvania. Oral arguments on these motions are scheduled for May 16, 2011.

The elevated levels of our rate of rescissions and denials have led to an increased risk of litigation by lenders and policyholders challenging our right to rescind coverage or deny claims. Under our master insurance policy, any suit or action arising from any right of the insured under the policy must be commenced within two years after such right first arose and within three years for certain other policies, including certain pool insurance policies. Recently, we have faced an increasing number of challenges from certain lender customers regarding our insurance rescissions and claim denials, which have resulted in some reversals of our decisions regarding rescissions or denials. We are currently in discussions with these customers regarding rescissions or denials which, if not resolved, could result in arbitration or judicial proceedings. Although we believe that our rescissions and denials are justified under our policies, if we are not successful in defending the rescissions or denials in any potential legal actions, we may need to reassume the risk on, and increase loss reserves for, those policies or pay additional claims. See Note 7 for further information. In addition to the above litigation, we are involved in litigation that has arisen in the normal course of our business. We are contesting the allegations in each such pending action and believe, based on current knowledge and after consultation with counsel, that the outcome of such litigation will not have a material adverse effect on our consolidated financial position and results of operations.

Securities regulations became effective in 2005 that impose enhanced disclosure requirements on issuers of ABS (including mortgage-backed securities ("MBS")). To allow our customers to comply with these regulations,

we typically were required, depending on the amount of credit enhancement we were providing, to provide (1) audited financial statements for the insurance subsidiary participating in the transaction, or (2) a full and unconditional holding-company-level guarantee for our insurance subsidiaries' obligations in such transactions. Radian Group has guaranteed two structured transactions for Radian Guaranty involving approximately \$182.9 million of remaining credit exposure.

Under change of control agreements with certain of our officers, upon a change of control of Radian Group or Radian Asset Assurance, as the case may be, we are required to fund an irrevocable rabbi trust to the extent of our obligations under these agreements. The total maximum amount that we would be required to place in trust is approximately \$6.7 million as of March 31, 2011. In addition, in the event of a change of control of Radian Group under certain of our long term cash-based incentive plans, we would be required to pay approximately \$15.0 million to plan participants as of March 31, 2011.

Radian Group Inc.

Notes to Unaudited Condensed Consolidated Financial Statements - (Continued)

As part of the non-investment-grade allocation component of our investment program, we have committed to invest \$90.0 million in alternative investments (\$12.3 million of unfunded commitments at March 31, 2011) that are primarily private equity securities. These commitments have capital calls expected through 2015, with the possibility of additional calls through 2017, and certain fixed expiration dates or other termination clauses.

On March 1, 2011, we sold our 45% interest in the holding company of a Brazilian insurance company, which specializes in surety and agricultural insurance, to another owner for a nominal purchase price. This holding company and its subsidiaries are subject to regulation by The Superintendence of Private Insurance, the regulatory agency responsible for the supervision and control of the insurance market in Brazil. Although we wrote off our entire interest in this company in 2005 and have sold our ownership interest, under Brazilian law, it is possible that we could become liable for our proportionate share of the liabilities of the company related to the period in which we were a significant shareholder, if the company was to become insolvent and had insufficient capital to satisfy its outstanding liabilities. Our share of the liabilities of the company attributable to this period was approximately \$103.4 million as of December 31, 2010.

Our mortgage insurance business provides an outsourced underwriting service to its customers known as contract underwriting. Typically, we agree that if we make a material error in underwriting a loan, we will provide a remedy to the customer, by purchasing the loan or placing additional mortgage insurance coverage on the loan, or by indemnifying the customer against loss up to a maximum specified amount. By providing these remedies, we assume some credit risk and interest-rate risk if an error is found during the limited remedy period in the agreements governing our provision of contract underwriting services. Recently, we limited the recourse available to our contract underwriting customers to apply only to those loans that we are simultaneously underwriting for compliance with secondary market compliance and for potential mortgage insurance. In the first quarter of 2011, we paid losses related to contract underwriting remedies of approximately \$2.5 million. Rising mortgage interest rates or further economic uncertainty may expose the mortgage insurance business to an increase in such costs. In the first quarter of 2011, our provision for contract underwriting expenses was approximately \$2.1 million and our reserve for contract underwriting obligations at March 31, 2011, was \$2.1 million. We monitor this risk and negotiate our underwriting fee structure and recourse agreements on a client-by-client basis. We also routinely audit the performance of our contract underwriters.

We have incentive, retention and severance agreements with certain employees in our financial guaranty business. The total cost expected to be incurred under these agreements is \$8.7 million, of which \$5.3 million has not been recorded as of March 31, 2011. The remaining cost for these agreements is expected to be recorded over the next two years.

#### 14. Subsequent Events

In April 2011, one of our financial guaranty counterparties exercised its termination right with respect to five corporate CDO transactions. This termination reduced our financial guaranty segment's net par outstanding by approximately \$1.7 billion, and decreased the present value of expected future installment premiums by \$7.4 million. As a result of this termination, we will record credit enhancement fees of \$0.5 million and reverse \$0.9 million of unrealized losses on derivatives in the second quarter of 2011.

In April 2011, we commuted approximately \$0.5 billion of net par outstanding of reinsurance exposure from one of our primary reinsurance customers. We did not pay any amount to commute this exposure other than a refund of approximately \$3.0 million of unearned premium reserves, net of ceding commissions. This commutation will result in an estimated increase in pre-tax income of \$8.0 million in the second quarter of 2011, primarily as a result of a decrease in the derivative and net claim liabilities of \$3.1 million and \$3.3 million, respectively, which had been established for the exposure that was commuted.

In April 2011, we paid approximately \$39 million to terminate a structured mortgage insurance transaction comprising \$45 million of pool insurance RIF. This transaction had the effect of reducing our pool insurance default count by approximately 2,200 loans. This transaction will result in approximately \$6.5 million of pre-tax income in the second quarter of 2011 as a result of a reduction in reserves.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following analysis should be read in conjunction with our unaudited condensed consolidated financial statements and the notes thereto included in this report and our audited financial statements, notes thereto and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in our Form 10-K for the fiscal year ended December 31, 2010 for a more complete understanding of our financial position and results of operations. In addition, investors should review the "Forward Looking Statements—Safe Harbor Provisions" above and the "Risk Factors" detailed in Item 1A of Part I of our Annual Report on Form 10-K for the year ended December 31, 2010, and in Item 1A of Part II of this Quarterly Report on Form 10-Q for a discussion of those risks and uncertainties that have the potential to affect our business, financial condition, results of operations, cash flows or prospects in a material and adverse manner.

### Business Summary

We are a credit enhancement company with a primary strategic focus on domestic, first-lien residential mortgage insurance. Our business segments are currently mortgage insurance and financial guaranty. Prior to January 1, 2011, we also had a third segment—financial services. Our financial services segment had consisted mainly of our ownership interest in Credit-Based Asset Servicing and Securitization LLC ("C-BASS"), which was a credit-based consumer asset business. We wrote off our entire investment in C-BASS in 2007. C-BASS filed for Chapter 11 bankruptcy protection on November 12, 2010, and was subsequently liquidated. Our interest in C-BASS was extinguished pursuant to the Plan of Liquidation that was confirmed on April 25, 2011. In addition, until May 3, 2010, when we sold our remaining interest therein, our financial services segment included our interest in Sherman Financial Group LLC ("Sherman"), a consumer asset and servicing firm specializing in credit card and bankruptcy-plan consumer assets.

### Mortgage Insurance

Our mortgage insurance segment provides credit-related insurance coverage, principally through private mortgage insurance, and risk management services to mortgage lending institutions. We have provided these products and services mainly through our wholly-owned subsidiaries, Radian Guaranty Inc., Amerin Guaranty Corporation, and Radian Insurance Inc. (which we refer to as "Radian Guaranty," "Amerin Guaranty," and "Radian Insurance," respectively). Private mortgage insurance protects mortgage lenders from all or a portion of default-related losses on residential mortgage loans made to home buyers who generally make down payments of less than 20% of the home's purchase price. Private mortgage insurance also facilitates the sale of these mortgage loans in the secondary mortgage market, most of which are sold to Freddie Mac and Federal National Mortgage Association ("Fannie Mae"). We refer to Freddie Mac and Fannie Mae together as "Government Sponsored Enterprises" or "GSEs."

**Traditional Mortgage Insurance.** Our mortgage insurance segment, through Radian Guaranty, offers primary and pool mortgage insurance coverage on residential first-lien mortgages ("first-lien"). At March 31, 2011, primary insurance on first-liens made up approximately 93.0% of our total first-lien insurance risk in force ("RIF") and pool insurance comprised approximately 7.0% of our total first-lien insurance RIF.

**Non-Traditional Mortgage Credit Enhancement.** In addition to traditional mortgage insurance, in the past we have used Radian Insurance or Amerin Guaranty to provide other forms of credit enhancement on residential mortgage assets. These products include mortgage insurance on second-lien mortgages ("second-lien"), credit enhancement on net interest margin securities ("NIMS"), credit default swaps ("CDSs") on domestic and international mortgages and primary mortgage insurance on international mortgages (collectively, we refer to the risk associated with these transactions as "non-traditional" or "other risk"). We stopped writing non-traditional business in 2007, other than a small amount of international mortgage insurance, which we discontinued writing in 2008. As of March 31, 2011, the aggregate remaining risk on such non-traditional mortgage credit enhancement was \$357 million.

### Financial Guaranty

Our financial guaranty segment has mainly provided direct insurance and reinsurance on credit-based risks through Radian Asset Assurance Inc. ("Radian Asset Assurance"), a wholly-owned subsidiary of Radian Guaranty. We also wrote financial guaranty business internationally through Radian Asset Assurance Limited ("RAAL"), an insurance company licensed in the United Kingdom and a subsidiary of Radian Asset Assurance. All of our exposure written through RAAL has been novated to Radian Asset Assurance or commuted, and we placed RAAL into liquidation in

2010. We expect the liquidation of RAAL to be completed during the second half of 2011.

Financial guaranty insurance typically provides an unconditional and irrevocable guaranty to the holder of a financial obligation of full and timely payment of principal and interest when due. Financial guaranty insurance may be issued at the inception of an insured obligation or may be issued for the benefit of a holder of an obligation in the secondary market. Historically, financial guaranty insurance has been used to lower an issuer's cost of borrowing when the insurance premium is less than the value of the spread (commonly referred to as the "credit spread") between the market yield required to be paid on the insured obligation (carrying the credit rating of the insurer) and the market yield required to be paid on the obligation if sold on the basis of its uninsured credit rating. Financial guaranty insurance also has been used to increase the marketability of obligations issued by infrequent or unknown issuers or obligations with complex structures. Traditionally, investors have benefited from financial guaranty insurance through increased liquidity in the secondary market, reduced exposure to price volatility caused by changes in the credit quality of the underlying insured issue, and added protection against loss in the event of default on the obligation. Market developments, including ratings downgrades of most financial guaranty insurance companies (including Radian Asset Assurance), have significantly reduced the benefits of financial guaranty insurance, particularly certain forms of financial guaranty structured finance transactions.

We have provided direct financial guaranty credit protection either through the issuance of a financial guaranty insurance policy or CDSs. Both forms of credit enhancement can provide the purchaser of such credit protection with a guaranty of the timely payment of interest and scheduled principal when due on a covered financial obligation, and in the case of most of our financial guaranty CDSs, credit protection in excess of specified aggregate losses. By providing protection through CDSs, we were able to participate in transactions involving asset classes (such as corporate collateralized debt obligations ("CDOs")) that may not have been available to us through the issuance of a traditional financial guaranty insurance policy. Either form of credit enhancement requires similar underwriting and surveillance.

We historically offered the following financial guaranty products:

**Public Finance**—Insurance of public finance obligations, including tax-exempt and taxable indebtedness of states, counties, cities, special service districts, other political subdivisions, enterprises such as public and private higher education institutions and health care facilities and infrastructure, project finance and private finance initiative assets in sectors such as airports, education, healthcare and other infrastructure projects;

**Structured Finance**—Insurance of structured finance obligations, including CDOs and asset-backed securities ("ABS"), consisting of funded and non-funded (referred to herein as "synthetic") executions that are payable from or tied to the performance of a specific pool of assets or covered reference entities. Examples of the pools of assets that collateralize or underlie structured finance obligations include corporate loans, bonds or other borrowed money, residential and commercial mortgages, trust preferred securities ("TruPs"), diversified payment rights ("DPR"), a variety of consumer loans, equipment receivables, real and personal property leases, or a combination of asset classes or securities backed by one or more of these pools of assets. We have also guaranteed excess clearing losses of securities exchange clearinghouses;

**Reinsurance**—Reinsurance of domestic and international public finance obligations, including those issued by sovereign and sub-sovereign entities, and structured finance obligations.

In 2008, in light of market conditions and the downgrade of the financial strength ratings of our financial guaranty insurance subsidiaries, we discontinued writing any new financial guaranty business, including accepting new financial guaranty reinsurance, other than as necessary to commute, restructure, hedge or otherwise mitigate losses or reduce exposure in our existing portfolio. Following this decision, we reduced our financial guaranty operations, including a significant reduction in our financial guaranty workforce. Since 2008, we have also reduced our financial guaranty exposures through commutations in order to eliminate uncertainty, maximize the ultimate capital available for our mortgage insurance business and accelerate the potential access to that capital.



We continue to explore ways to maximize the value of our existing insured financial guaranty portfolio, including the possibility of partnering with third-parties to utilize all or a portion of the portfolio as a platform for writing new public finance and infrastructure business, as well as other possible ways to leverage the portfolio. On February 1, 2011, Radian Asset Assurance signed an agreement to purchase Municipal and Infrastructure Assurance Corporation (the "FG Insurance Shell"), a New York domiciled financial guaranty insurance company that has not written any business, but has obtained licenses to do so in 36 states and the District of Columbia. The acquisition, which remains subject to regulatory approval, will provide Radian Asset Assurance with the flexibility to consider using the FG Insurance Shell to pursue strategic alternatives in the public finance market, including possibly partnering with third-party investors to write new public finance insurance and/or reinsuring all or a portion of Radian Asset Assurance's existing public finance business. We expect that any new initiative for the FG Insurance Shell will be consistent with our ultimate goal of reducing our financial guaranty exposure. The expected purchase price of approximately \$82 million is \$7 million above the value of the statutory capital base of the FG Insurance Shell, consisting of approximately \$75 million of cash, cash equivalents and treasury securities.

**Financial Guaranty Exposure Subject to Recapture or Termination.** As a result of multiple ratings downgrades of Radian Asset Assurance, approximately \$57.1 billion of our total net par outstanding as of March 31, 2011, (representing 73.7% of our financial guaranty segment's total net par outstanding) remained subject to recapture or termination at the option of our primary reinsurance customers and credit derivative counterparties.

If all of our direct insurance that were subject to termination were terminated as of March 31, 2011, our net par outstanding would have been reduced by \$34.1 billion, and because our contracts do not require mark-to-market settlement payments in such circumstances, no cash payment would be required by either party. In addition, the present value of expected future installment premiums would decrease by \$104.6 million. Furthermore, \$7.1 million of unearned premium reserves would be earned and net unrealized losses on derivatives and variable interest entities ("VIEs") of \$493.9 million would also have been reversed had these transactions been terminated as of March 31, 2011.

In April 2011, one of our counterparties exercised its termination right with respect to five corporate CDO transactions. This termination reduced our net par outstanding by approximately \$1.7 billion, and decreased the present value of expected future installment premiums by \$7.4 million. As a result of this termination, we will record credit enhancement fees of \$0.5 million and reverse \$0.9 million of unrealized losses on derivatives in the second quarter of 2011.

If all of our reinsurance that were subject to recapture were recaptured as of March 31, 2011, our net par outstanding would have been reduced by \$23.0 billion and the pre-tax impact on our financial statements would have been as follows:

**Statement of Operations (In millions)**

Decrease in assumed premiums written	\$(244.2	)
Decrease in net premiums earned	\$(37.0	)
Increase in change in fair value of derivative instruments - gain	23.8	
Decrease in policy acquisition costs	4.9	
Decrease in provision for losses	10.6	
Increase in pre-tax income	\$2.3	

**Balance Sheet (In millions)**

Decrease in:	
Cash	\$177.3
Deferred policy acquisition costs	69.3
Accounts and notes receivable	32.7
Derivative assets	1.2
Unearned premiums	207.2
Reserves for losses and loss adjustment expenses ("LAE")	50.6
Derivative liabilities	25.0

Assuming all of this reinsurance business were recaptured as of March 31, 2011, Radian Asset Assurance's statutory surplus would have increased by approximately \$155.9 million, primarily as a result of the release of contingency reserves.

While our treaties with our primary reinsurance customers do not permit our reinsurance customers to selectively recapture business previously ceded to us under their treaties, because we have entered into multiple treaties with each customer, it is possible that a customer may choose to recapture business only under those treaties that it perceives as covering less risky portions of our reinsurance portfolio. This selective recapture, if it occurs, could potentially leave us with risk that is more concentrated in troubled asset classes. Approximately \$21.5 billion or 93.0% of Radian Asset Assurance's net par reinsurance exposure outstanding at March 31, 2011, was ceded from primary reinsurance customers that are subsidiaries of Assured Guaranty Ltd. Consequently, the credit performance of such reinsurance, as well as any decision to recapture ceded business, is dependent upon primary insurers that are subsidiaries of this one holding company and their surveillance and mitigation abilities.

In April 2011, we commuted approximately \$0.5 billion of net par outstanding of reinsurance exposure from one of our primary reinsurance customers (the "April 2011 Reinsurance Commutation"). We did not pay any amount to commute this exposure other than a refund of approximately \$3.0 million of unearned premium reserves, net of ceding commissions. This commutation will result in an estimated increase in pre-tax income of \$8.0 million in the second quarter of 2011, primarily as a result of a decrease in derivative and net claim liabilities of \$3.1 million and \$3.3 million, respectively, which had been established for the exposure that was commuted.

#### Overview of Business Results

As a seller of credit protection, our results are subject to macroeconomic conditions and specific events that impact the origination environment and credit performance of our underlying insured assets. While the improved credit quality of new mortgage insurance business has continued in 2011, the ongoing downturn in the housing and related credit markets, characterized by a decrease in mortgage originations, decline in home prices in many markets, deteriorating credit performance of mortgage and other assets and reduced liquidity for many participants in the mortgage and financial services industries, has had, and we believe will continue to have, a significant negative impact on the operating environment and results of operations for each of our businesses. There is a great deal of uncertainty regarding our ultimate loss performance. The possibility that the United States ("U.S.") economy may not fully recover from the most recent recession or may reenter a recessionary period following a brief period of stabilization or growth, the lack of meaningful liquidity in some sectors of the capital and credit markets, the potential for continued high unemployment, and limited home price appreciation or further depreciation may add further stress on the performance of our insured assets.

Our businesses have been significantly affected by, and our future success may depend upon, legislative and regulatory developments impacting the housing finance industry. The GSEs are the primary beneficiaries of the majority of our mortgage insurance policies, and the Federal Housing Authority ("FHA") remains our primary competitor outside of the private mortgage insurance industry. Federal and state efforts to support homeowners and the housing market, including through the U.S. Department of Treasury's Homeowner Affordability and Stability Plan ("HASAP"), have had a positive impact on our business. Various regulatory agencies are now in the process of developing new rules under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") that are expected to have a significant impact on the housing finance industry, and the U.S. Congress is planning for the reform of the housing finance market, including the future roles of the GSEs. See Risk Factors—"Because most of the mortgage loans that we insure are sold to Freddie Mac and Fannie Mae, changes in their charters or business practices could significantly impact our mortgage insurance business," "A decrease in the volume of home mortgage originations could result in fewer opportunities for us to write new insurance business," and "The Dodd-Frank Wall Street Reform and Consumer Protection Act may have a material effect on our mortgage insurance and financial guaranty businesses" in Part II, Item 1A of this Quarterly Report on Form 10-Q.

## Mortgage Insurance

**Defaults.** Our first-lien primary default rate at March 31, 2011, was 15.5%, compared to 16.5% at December 31, 2010. Our primary default inventory decreased by 6.8% during the first quarter of 2011 and continued to decline in April 2011. This positive trend is primarily the result of fewer new defaults compared to the number of defaults that cured ("cures"), combined with the payment of claims on defaulted loans and the number of loans for which coverage was rescinded or claims were denied. Despite this positive trend, our overall primary default rates continue to remain elevated due to high unemployment and continued weakness in the U.S. housing and mortgage credit markets.

Defaults have remained at elevated levels across all our mortgage insurance product lines, including our insured portfolio of prime, first-lien mortgages. Overall, the underlying trend of high defaults continues to be driven primarily by the poor performance of our 2005 through 2008 books of business. We believe that a return to sustained profitability in our mortgage insurance business is dependent upon both a further reduction in the number of new defaults and an increase in the number of cures, particularly coming from our older delinquent loans. While we expect new primary, first-lien defaults to continue to decrease throughout 2011, based on the current pace of this decrease, we do not expect our mortgage insurance business to be profitable for the remainder of 2011.

A slowdown in mortgage foreclosures, and consequently a slowdown in claims submitted to us, has contributed to the sustained high level of our default inventory, mainly due to the foreclosure moratoriums imposed by various government entities and lenders, and to the effect of prolonged modification programs for delinquent loans. This has resulted in more defaults remaining unresolved for a longer period of time than has historically been the case.

Recently, this slowdown in claims has been further exacerbated by additional foreclosure moratoriums imposed by certain servicers that are related to allegations that servicers and other third parties acted improperly in foreclosure proceedings.

**Provision for Losses.** Our mortgage insurance provision for losses was \$414.0 million for the three months ended March 31, 2011. While our loss provision for new default notices received in the first quarter of 2011 was less than both the first quarter and fourth quarter of 2010, this positive trend was substantially offset by (i) incurred losses related to an increase in our aggregate weighted average estimated rate at which defaults move to claim ("default to claim rate"), primarily due to an increase in the weighted average age of underlying defaulted loans, and to a lesser extent, a reduction in our estimated future rescissions and denials, and (ii) an increase in our incurred but not reported ("IBNR") reserve estimate, primarily related to an increase in our estimate of the future reinstatements of previously rescinded policies and denied claims.

Our mortgage insurance reserve for losses continues to be impacted by our loss management efforts. Our loss reserve estimate incorporates our recent experience with respect to the number of claims that we are denying and the number of insurance certificates that we are rescinding due to fraud, underwriter negligence or other factors, including our recent experience regarding reinstatements of previously rescinded policies and denied claims. Our current level of rescissions and denials remains elevated compared to historical levels, which we believe reflects the larger concentration of poorly underwritten loans (primarily originated during 2005 through 2008) that are in our default inventory, as well as our extensive efforts to examine more claims for potential rescissions or denials. While we expect the level of rescissions and denials to continue to remain elevated from historical levels as long as our 2005 through 2008 insurance policies comprise the majority of our default inventory, our weighted average estimated rescission and denial rates have decreased modestly during 2011.

**Claims paid.** Total mortgage insurance claims paid in the first quarter of 2011 were \$365.2 million. Foreclosure moratoriums and loan modification programs have reduced the number of defaults going to claim. We cannot be certain of the ultimate impact of these programs on our business or results of operations, or the timing of this impact. Some of the most recent foreclosure moratoriums related to foreclosure documentation may further delay our receipt of claims, although we expect claims to increase during the balance of 2011. We currently expect total claims paid in 2011 to be approximately \$1.7 billion.

**New Insurance Written.** We wrote \$2.6 billion of new mortgage insurance in the first quarter of 2011, compared to \$1.9 billion of insurance written in the corresponding period of 2010. This increase is mainly the result of an increase in the penetration rate of private mortgage insurance in the overall insured mortgage market and our increased sales efforts. We have been more aggressively marketing our product offerings that favorably compete with the FHA prices in order to gain market share back from the FHA. Effective April 18, 2011, the FHA reduced its upfront mortgage insurance premium and increased its annual premium. While we cannot predict what impact these premium changes will have on our new insurance written ("NIW") in the future, we believe that the new FHA pricing could allow us to be more competitive with the FHA than in the recent past. While the private mortgage insurance industry has made some progress in recapturing business from the FHA, the FHA's market share remains historically high, and this competition with the FHA, in conjunction with the other factors identified above, is likely to continue to negatively affect the volume of our NIW.

Starting in 2008, we implemented a series of changes to our underwriting guidelines aimed at improving the long-term risk profile and profitability of our business. As a result of these changes, the credit profile of our mortgage insurance portfolio has improved. Our implementation of these stricter guidelines has also contributed to the reduction in NIW as compared to historical levels. For 2010 and 2011, almost all of our new business production was prime business. In addition, Fair Isaac and Company ("FICO") scores for the borrowers of these insured mortgages have increased, while the loan-to-value ("LTV") on these mortgages has decreased, meaning that borrowers generally are making larger down payments in connection with the more recent mortgages that we are insuring.

**Terminations.** In 2009, we began pursuing opportunities to manage our legacy mortgage insurance portfolio and non-traditional mortgage insurance RIF through a series of commutations, transaction settlements and terminations, including the following notable transactions during 2011:

In February 2011, we exercised our option to terminate two of our four Smart Home transactions, which added approximately \$41.0 million of RIF to our portfolio. There was minimal impact to our financial statements, as funds received were offset by expenses paid.

In order to mitigate future expected losses, during the first quarter of 2011, we purchased one NIMS bond with approximately \$0.9 million face value, at a purchase price approximately equal to our fair value liability for such NIMS at the time of purchase.

In April 2011, we paid approximately \$39 million to terminate a structured transaction, comprising \$45 million of pool insurance RIF. This transaction had the effect of reducing our pool insurance default count by approximately 2,200 loans. This transaction will result in approximately \$6.5 million of pre-tax income in the second quarter of 2011 as a result of a reduction in reserves.

#### Financial Guaranty

**Net Par Outstanding.** Our financial guaranty segment's net par outstanding was \$77.5 billion as of March 31, 2011, compared to \$78.8 billion at December 31, 2010. The reduction in net par outstanding was primarily due to a counterparty exercising its early termination right with respect to a TruPs CDO transaction, the amortization or scheduled maturity of our insured portfolio, and prepayments ("refundings") of public finance transactions. Our financial guaranty segment's net par outstanding decreased by an additional \$2.2 billion in April 2011, primarily as a result of the April 2011 Reinsurance Commutation and the termination of five corporate CDO transactions as discussed above. In light of our decision in 2008 to discontinue writing new financial guaranty business, we expect our net par outstanding to continue to decrease as our financial guaranty portfolio matures and as we seek to proactively reduce our financial guaranty RIF.

**Credit Performance.** The overall credit quality of our financial guaranty insured portfolio improved slightly during the first quarter of 2011. The percentage of internally rated AAA credits in our portfolio increased to 45.2% of our net par outstanding at March 31, 2011, from 43.0% at December 31, 2010, primarily due to credit improvements in our insured corporate CDO portfolio, which offset some credit deterioration in our public finance portfolio.

**Public Finance.** Our public finance insured portfolio continues to experience stress from the general economic downturn and slow economic recovery. The percentage of our insured public finance portfolio rated below investment grade ("BIG") increased to 4.9% of our financial guaranty segment's net par outstanding at March 31, 2011, compared to 4.6% at December 31, 2010. The greatest level of stress continues to be in the healthcare and long-term care sectors. Although we have seen some stabilization and modest improvement in the performance of some healthcare credits in the portfolio, with no additional downgrades to BIG within the sector during the first quarter of 2011, the credit performance outlook for the healthcare sector remains challenging, particularly due to uncertainty regarding the future of healthcare reform and state and federal funding for healthcare expenditures. Although the states and municipalities included within our government-related insured credits have generally been able to withstand stresses to date, the lagging impact on municipal governments from recent economic conditions is becoming more evident. We expect the negative trend in this sector to continue at least through the remainder of 2011 due to the protracted economic downturn and slow economic recovery, the end of federal stimulus revenues and slow recoveries of tax-based revenues (in particular where tax revenues are derived from the value of real estate), which trend we expect will continue to strain the ability of government entities to maintain balanced budgets and adequate liquidity to meet near-term financial obligations. As a result, we may continue to experience further credit deterioration and municipal defaults in our government-related insured credits.

**Structured Finance.** The credit performance of our structured finance portfolio continued to improve in the first quarter of 2011, with no structured finance credits being downgraded to BIG and no new defaults occurring in the collateral underlying our corporate CDOs in 2011. The percentage of internally rated AAA credits in our structured finance portfolio increased to 78.9% of our financial guaranty segment's net par outstanding at March 31, 2011, from 75.8% of our net par outstanding at December 31, 2010. With respect to our directly insured TruPs CDOs, we experienced both deterioration (due mainly to interest deferrals) and some stabilization in the TruPs collateral (due to cures of previous interest deferrals). In addition, during the first quarter of 2011, one counterparty exercised its right to terminate a TruPs CDO with \$84.9 million of net par outstanding. See "Results of Operations—Financial Guaranty—Financial Guaranty Exposure Information" below for additional information regarding material changes in the credit performance of our insured TruPs CDO portfolio.

With respect to our CDOs of commercial mortgage-backed securities ("CMBS") transactions, despite signs of improvement within the commercial real estate sector, delinquencies and cumulative losses continued to increase across many of the CMBS backing these CDOs. Despite this deterioration, our internal ratings for these transactions remained unchanged, and we continue to expect no claim payments on these transactions. We increased reserves on several of our insured domestic, non-CDO, residential mortgage-backed securities ("RMBS") due to the estimated impact that the combination of prolonged foreclosures and declining home values may have on these transactions.

#### Results of Operations

Our results for the quarter ended March 31, 2011, were positively impacted by the change in fair value of derivative instruments and VIE liabilities, which occurred primarily due to the widening of Radian Group's five-year credit default swap ("CDS") spread and the corresponding decline in the fair value liability of our insured obligations, primarily TruPs CDOs. Because we have the ability to hold our financial guaranty contracts to maturity, changes in market spreads are not necessarily indicative of our ultimate net credit loss payments with respect to these obligations.

Our estimated credit loss payments presented in the table below represent our current estimate of the present value (net of estimated recoveries) that we expect to pay in claims with respect to our insured credit derivatives and net VIE liabilities. The estimated fair value of these obligations is measured as of a specific point in time and may be influenced by changes in interest rates, credit spreads, credit ratings and other market, asset-class and transaction specific conditions and factors that may be unrelated to our obligation to pay future claims. Other factors that may cause a difference between the fair value of these obligations and our estimated credit loss payments include the effects of our non-performance risk and differing assumptions regarding discount rate and future performance. In the absence of credit losses, unrealized losses related to changes in fair value will reverse before or at the maturity of these obligations. However, we may agree to settle some or all of these obligations prior to maturity at amounts that are greater or less than their fair values at the time of settlement, which could result in the realization of gains or losses and the corresponding reversal of unrealized gains or losses.

The following table summarizes the fair value amounts reflected on our condensed consolidated balance sheet at March 31, 2011, related to these instruments and the present value of our estimated credit loss payments on these instruments.

(In millions)	NIMS	Financial Guaranty Derivatives and VIEs	Total
Balance Sheet			
Trading securities	\$—	\$90.2	\$90.2
Derivative assets	9.0	15.1	24.1