Q2 2012 Earnings Call

Company Participants

- Anne Waleski, Chief Financial Officer
- Michael Crowley, Co-President
- Richie Whitt, Co-President
- Tom Gayner, President

Other Participants

- Adam Klauber, Analyst
- David West, Analyst
- Jay Cohen, Analyst
- Mark Hughes, Analyst
- Meyer Shields, Analyst
- Ron Bobman, Analyst
- Scott Heleniak, Analyst

Presentation

Operator

Greetings and welcome to the Markel Corporation Second Quarter 2012 earnings call. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation.

(Operator Instructions).

As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Mr. Tom Gayner, President of Markel Corporation. Thank you, Mr. Gayner, you may begin.

Tom Gayner {BIO 1896932 <GO>}

Thank you, Manny, I appreciate it. Good morning. Welcome everyone to the Markel Corporation Second Quarter conference call. We are pleased that you are joining us as we all look forward to sharing the good news of our substantial year-to-date progress in 2012 in building the value of your Company.

Over the past several years we've been telling you about the transformation underway at Markel. We've told you about the growth of our insurance operations through entry into new geographical areas, our new products, and our acquisitions. We have told you about our focus on improving the operating efficiencies in our business and how we have restructured the Company to increase our revenues from existing customers. We have also told you about our expanded investment activities through Markel Ventures, which now owns controlling interest in about a dozen profitable manufacturing and service businesses.

We've told about you how Markel has more ways and more flexibility to create value for our shareholders than ever before. And it is now delightful to begin to show you the fruits of these efforts rather than just telling you about them. As is our custom, our Chief Financial Officer, Anne Waleski, will lay out the overall numbers from the first half and then my Co-Presidents, Mike Crowley and Richie Whitt, will discuss our domestic and international insurance activities. I will then cover our investment in Markel Ventures' operations and then we will open the floor for your questions.

Before getting started with today's line-up though, the rules say we need to repeat the Safe Harbor Statement, so here goes. During our call today, we may make forward-looking statements. Additional information about factors that could cause actual results to differ materially from those projected in the forward-looking statements is described under the captions Risk Factors and Safe Harbor and Cautionary Statements in our most recent annual report on form 10-K and quarterly report on Form 10-Q.

We may also discuss certain non-GAAP financial measures in the call today. You may find a reconciliation to GAAP of these measures on our website at www.Markelcorp.com in the Investor Information section under Non-GAAP Reconciliation or in our quarterly report on Form 10-Q. With that, Anne?

Anne Waleski {BIO 16735457 <GO>}

Think you Tom and good morning everyone. Before I get to a discussion of our financial results I will point out a couple of accounting items new to the quarter and the year. First, I'm sure you have all noticed some changes in our statements for the quarter. Redeemable Noncontrolling Interest is a new-line item on the balance sheet this quarter.

For all periods presented, we have reclassified amounts previously included in the noncontrolling interest balances for relevant Markel Ventures affiliates to this new line item. This is required because some of the Markel Ventures minority shareholders have the option to sell their shares to us in the future, generally at a fixed multiple of EBITDA.

In addition to the reclassification, there is an adjustment recorded on these redeemable noncontrolling interest balances. As of the end of each reporting period, the carrying value of the redeemable noncontrolling interest is adjusted to the calculated redemption value if that price is higher than the current carrying value. The purpose of these estimates is to record the potential cash obligations we may have to the noncontrolling interest shareholders.

This quarter, redeemable noncontrolling interest balances were marked out by $8.2 million. The adjustment is reported to retained earnings and reduces net income to shareholders when calculating earnings per share. You can find the earnings-per-share calculation in Footnote 2 and additional information regarding our contingent obligations to the noncontrolling shareholders in Footnote 8.

The second item I would like to point out was previously discussed in our First Quarter conference call and filing but I'd like to remind everyone that we chose to prospectively adopt the new DAC accounting standards. As of June 30, 2012 we have recognized approximately $35 million or 3 points of expenses related to the prospective adoption of the new standards.

Now that we have covered these new items I will review the 2012 financial results. I will follow the same format in discussing results as in past quarters. I will start by discussing our underwriting operations followed by a brief discussion of our investment results and bring the two together with a discussion of our total results.

Our total operating revenues grew 12% to $1.4 billion in 2012 from $1.3 billion in 2011. The increase is due to a 10% increase in revenue from our insurance operations and a 30% increase in revenue from our non-insurance operations which we refer to as Markel Ventures.

Moving into the underwriting results, gross written premiums for the six months of 2012 were just under $1.3 billion which is an increase of 9% compared to 2011. The increase in 2012 was due to higher gross premium volume in each of our three operating segments. Net written premiums were approximately $1.1 billion, up 9% to the prior year. Retentions were up slightly in 2012 at 89%.

Earned premiums increased 9%. The increase in 2012 was due to higher earned premium volume in each of our three operating segments. Increases in gross, net, and earned premiums have all benefited from our recent insurance acquisitions in the Specialty Admitted segment. Our combined ratio was 93% for the first six months of 2012 compared to 107% in 2011. As a reminder, our 2011 combined ratio included $99 million or 10 points of underwriting losses related to the catastrophe events which occurred last year in the US, Australia, New Zealand, and Japan.

Setting aside the impact of the prospective adoption of the new DAC accounting standard in 2012 and the effects of catastrophes in 2011, the improvement in our year-to-date combined ratio was due to a lower current accident year loss ratio and to more favorable development of prior-years' loss reserve within the London Insurance Market segment compared to the same period in 2011. The improvement in the current accident year loss ratio was due to lower attritional current year losses in the Excess and Surplus Line segment and the London Insurance Market segment.

Favorable redundancies on prior-years' loss reserve increased to $191 million or 18 points of favorable development, compared to $151 million or 16 points of favorable development in 2011. The increase was primarily due to more favorable development of prior-years' losses in the London Insurance Market segment. Favorable development on prior-years' losses in 2012 was primarily on the 2008 and 2009 accident years and occurred in a variety of programs across our international division.

Now I will discuss the results of our non-insurance operations, which we call Markel Ventures. In 2012, year-to-date revenues from Markel Ventures were $191 million compared to $147 million in 2011. Year-to-date net income to shareholders from our non-insurance operations, Markel Ventures, was $400,000 in 2012 compared to $4.7 million in 2011. Revenues from Markel Ventures increased in 2012 as compared to 2011 primarily due our acquisitions of Baking Technology Systems Incorporated and WI Holdings Incorporated in late 2011, as well as Havco 2012.

Next, some information on our investment results. Investment income was up 7% in 2012 to just under $144 million. Net investment income for the six months of 2012 included a favorable change in the fair value of our credit default swap of $12 million, which compares to $600,000 in 2011. During the First Quarter of 2012, financial markets improved and credit spreads narrowed, which favorably impacted this credit default swap.

Net realized investment gains were $20 million compared to $13 million in 2011. Net realized gains for the six months of 2012 excluded $1 million of write-downs for other than temporary declines in the estimated fair value of investments as compared to $5 million in 2011.

Unrealized gains increased $194 million before taxes in 2012 driven primarily by increases in equity securities. Tom will go into further detail on investments in his comments. Looking at our total results for 2012, the effective tax rate was 23% in 2012 compared to an effective tax rate of 14% in 2011.

The increase is primarily due to anticipating a smaller tax benefit related to tax exempt investment income as a result of projecting higher pre-tax income for 2012 than in 2011. We reported net income to shareholders of $147 million compared to $39 million in 2011. Book value per share increased 8% to $380 per share at June 30, 2012 at year-end.

I will now make a few comments on cash flow and the balance sheet. Net cash provided by operating activities was approximately $105 million for the six months ended June 30, 2012. That compares to approximately $100 million for the same period as 2011.

The increase in net cash provided by operating activities was due to higher cash flows from underwriting activities as a result of higher premium volumes in each of our three operating segments. Partially offset by increased claims settlement activity during the First Quarter of 2012, primarily in the London Insurance Market segment. Investments in cash at the holding company were approximately $900 million at June 30, as compared to a little less than $1.2 billion at the end of 2011.

The decrease in invested assets is primarily the result of acquisitions made during 2012. On July 2, 2012 the Company issued $350 million of 10-year 4.9% unsecured notes for net proceeds of $347 million. A portion of the proceeds was used to redeem the Company's

7.5% unsecured senior debentures due August 22, 2046 at a redemption price of $150 million. Remaining proceeds will be used to partially refund the repayment of the Company's 6.8% unsecured notes due February 15, 2013. At this point I will turn over to Mike to further discuss operations.

Michael Crowley {BIO 1871008 <GO>}

Thanks, Anne. Good morning, everyone. I am pleased to report that the Second Quarter North American results were positive from a rate, premium, and underwriting perspective. When measured against the First Quarter, our North American underwriting segment achieved better rate results in the Second Quarter with rates increasing 4.5% on average versus 3.4% in the First Quarter. We believe that a better comparison to the progress made in our ability to increase rate is to look back at the same period in 2011.

Last year, the majority of North American business segments had rate decreases and the total book generated a minimal increase through the first six months of 2011. We are making progress. With regard to premium growth, the E&S regions grew by 4.1% bringing growth year-to-date to 6.1%. Total E&S segment grew by 1.7% for the quarter and 6% year-to-date, the difference being the growth numbers for the E&S regions in the entire segment, difference is the impact of exited lines of businesses that were booked in 2011 for the same period.

The Specialty Admitted segment grew 25.5% for the quarter; it was up 18.1% year-to-date over the same period in 2011. This growth is fueled by the addition of $26 million of THOMCO premiums and growth in the Markel FirstComp business. Our existing property and casualty businesses and our agribusiness also were up for the quarter and the year.

Markel American, our personal lines division, generated 5.9% growth for the quarter and 5% year-to-date. The combined ratios for all North American segments improved for the quarter versus the same period in 2011. The Specialty Admitted segment improved 5 points to 102 from 107; E&S segment improved 5 points as well from to 87 from 92 in 2011.

The THOMCO transition which we closed January 1 of this year continues in a very positive manner. We still believe that we will book approximately $60 million on Markel paper in this fiscal year. FirstComp is executing their plan for improved results through price increases, geographic analysis, and reallocating volume to favorable territories, plus expense reduction efforts.

Cross-selling of FirstComp is showing improvement with 145 agents completing their Markel producer agreements, bringing the total count of agents who have initiated this process to 602. In June, 89 Markel FirstComp agents requested a THOMCO producer agreement bringing that total to 325 so far this year.

In the E&S segment, binders increased at a higher rate than submissions reflecting some improvement in the market as well as some benefit from our efforts to cull non-performing agents and reduce the receipt of submissions that offer little opportunity to

Markel. We completed and released phase two of our broker portal in the E&S division, which included the addition of more than 120 property and casualty class codes in the quick quote rate function for rating, quoting, and binding. Across all E&S regions we conducted a total of 489 agency visits, hosted three producer events, and held underwriting conferences in four regions.

In addition during the quarter, we were pleased to announce several new promotions of significance. Jeff Lamb has been with Markel for 11 years serving most recently as Head of Underwriting in our Midsouth region was promoted to Executive Underwriter for the E&S division. Evans Nash who has been with Markel for 17 years has assumed the role of Managing Director, Wholesale Marketing. Evans recently was in charge of our binding business. He replaces Wendy Hauser, who is transferring back to our Midsouth region to fill the senior position left over by Jeff Lamb's promotion.

I would like to point out that Wendy just did a terrific job in her role as Managing Director, Wholesale Marketing and we expect the same results from Wendy in the Midsouth region. Each of these individuals brings a wealth of knowledge and talent to their respective positions. Our ability to promote from within is evidence of the depth of talent at Markel. In summary, we're pleased with the performance in North America in the quarter but we will not lose sight of the fact that continuous improvement is both necessary and possible. I would like to turn the call over to Richie Whitt.

Richie Whitt {BIO 7084125 <GO>}

Thanks Mike. Good morning everybody. During the first six months of 2012, Markel International's gross written premiums grew 7% to $514 million. Significant areas of growth continue to be in the marine and energy and our catastrophe-exposed property lines both 3D [ph] and open-market property. We continue to see price increases on catastrophe-exposed property and marine and energy business.

However, as the years progress, these price increases appear to be moderating to some extent. Our overall average price increase on renewal business in the first six months of the year was approximately 5%. CAT property increases have generally been between the 10% to 20% range and energy has seen low single-digit increases.

All the rest of our lines on the international side are relatively stable, maybe a point or two up, a point or two down, but pretty stable I would say. So despite solid price increases in several of the lines of business in the first half of the year, there is still a pretty competitive market and there is still quite a bit of capacity out there. International's combined ratio for the first six months of 2012 was 86%.

That includes 3 points of expense related to the adoption of the new deferred acquisition cost accounting standards that Anne mentioned. As opposed to the significant CAT losses that we experienced in the first half of 2011, our first six months of '12 results really include minimal catastrophe losses.

In addition, Markel international's 2012 combined ratio included $86 million of favorable development on prior-year reserves. This included $18 million of takedown on 2001 and prior-year reserves. We always strive to establish reserves that are more likely redundant than deficient at Markel. However the releases we experienced in the first six months are more than we would normally expect and are, as Anne said, the result of favorable development across a number of product lines including that 2001 and prior reserve release that I mentioned.

Want to congratulate William Stovin and the International team on this really strong start to the year. Our goal for the second half of the year is going to be to continue to build on this positive momentum, continue to look for opportunities to profitably grow the international franchise.

Finally, switching gears, I would also like to mention a significant accomplishment for our IT, finance, actuarial, and information management team. During the Second Quarter we went live with the first phase of a data warehouse, which includes all of our Excess and Surplus Lines business. We are already seeing the benefit of being able to better analyze our Excess and Surplus Lines data.

We'll be able to provide our underwriters and product line leaders with significantly better information about production, profitable classes, classes the need corrective action. We believe that over time, better access to this information is going to help us gain a competitive advantage. With that, I would like to turn it over to Tom.

Tom Gayner {BIO 1896932 <GO>}

Thank you, Richie. As Anne mentioned earlier, book value per share rose to a new record high of $380 as of June 30. Our comprehensive income so far in 2012 of $279 million created an increase in book value per share of roughly $28 or 8% during the first six months of the year. I'm happy with those results, and I hope you are as well. I'm also especially pleased that those results occurred even though we were not hitting on all cylinders.

Specifically, while we enjoyed excellent results from our insurance and equity investment operations, as well as positive returns from our fixed income portfolio, the results at Markel Ventures were below my expectations.

The fact that we can hit new records in book value and compound capital at the rates we did, despite not hitting on all cylinders is very encouraging to me. The reality is that it is highly unlikely that we will ever hit on every single cylinder at once. That said, look at the returns we have earned given that fact. I am encouraged by what we have built and are continuing to build at Markel.

We've got more cylinders than we used to and more chances to keep the engine going forward. We will let the politically minded of you debate whether we built that ourselves or not, but the numbers seem to indicate that somehow or another, Markel's long legacy of creating enduring value continues.

As to some details, during the first half the total return on the investment portfolio was 4.5%. Equities enjoyed a return of 9.7%, and fixed income produced a positive overall return of 2.9%. Markel Ventures consolidated results, however, as I said, were below my expectations for the first six months. On revenues of approximately $190 million, EBITDA totaled $9.4 million. This compares to revenues of $146 million a year go and EBITDA of $9.9 million. As always, a reconciliation of EBITDA to net income is available on the website.

In the equity portfolio, our focus on high-quality securities paid off. During the first six months, we earned 9.7% compared to the S&P 500 total return of 9.5%. Over the last 15 years, a longer and more meaningful timeframe, we have outperformed the S&P 500 by 170 basis points per year. We have also outperformed the Barclay's Aggregate Bond index by 220 basis points per year, which demonstrates the value we add to our shareholders by investing in stocks.

Equities now represent roughly 60% of our total shareholders' equity, up from 55% at year-end. We continue to steadily and regularly add to or equity investment portfolio and we expect to continue to do so. Revenues are going up around here, and we've got ideas for where to invest the money.

In our fixed income operations, we earned a total return of 2.9%. Interest rates moved lower yet again during the Second Quarter so we over-earned the coupon from our bond portfolio. Yet again, I continue to be amazed that this is happening and remain ever more defensively positioned with that portfolio. Duration for the overall bond portfolio is now at a record low for us of 3. The perverse good news is that the opportunity cost of holding an ever-shorter duration bond portfolio is going down.

Given the low rate at the front and long end of the curve, we couldn't stretch for yield even if we wanted to. There just isn't any worthwhile yield out there to be had. As such, we have a portfolio where the difference is between what one would call cash and equivalents and fixed income continue to diminish.

That means for all practical purposes, we have a lot of cash and all the options that go with cash, such as deploying at higher rates of return as time goes by. It also means we are protecting our balance sheet against a rise in interest rates even more than last quarter and last year, and I believe that's a good idea.

Finally, let me address Markel Ventures. As I mentioned earlier, we breathe the same air as everybody else and the continued passage of caution in the overall economy caused several sales, large ticket capital goods to be pushed out beyond original shipment schedules. There's also some undeniable pressure on our order books and sales prices. Additionally and positively, we are undertaking meaningful expansions at several of our units which means that we are incurring up-front expenses to build for the future.

That said, I am optimistic about the second half of the year. Our current shipment rates are encouraging, seasonality helps us in the second half, and we should begin to see the beginning of the pay off in both sales and earnings from some of the major expansions underway at the Markel Ventures Company. Additionally, we acquired a controlling interest in HAVCO late during the Second Quarter. Havco is the leading manufacturer of flooring for the trailers of the 18-wheelers you see out there on the highway.

Subsequent to the end of the quarter we also acquired Tromp, a Dutch baking equipment company, which will join our AMF bakery operations and IDRECO, a Dutch dredging manufacturer which joins our Ellicott Dredge operations. These additions should begin to contribute to our second half results. As we look out over the balance of 2012 and into 2013, I expect that the current run rate of revenues for the Markel Ventures companies should approximately $600 million and that they should produce double-digit EBITDA on those revenues. I look forward to reporting those sorts of results to you.

Additionally, let me take a few minutes to discuss our culture and history of being very conservative in our accounting judgment. As you've heard us say, we have a policy of reserves being more likely to be redundant than deficient You can see the evidence that we mean what we say in our history of reserve redundancy. During this quarter, new items, noncontrolling interest Anne referred to earlier in her comments, is yet another example of what I would consider to be extremely conservative accounting and financial presentation. And I would like to explain it as I see it economically.

In many of the Markel Ventures acquisitions, we buy less than 100% of the businesses on day one. In each and every case, agreements with specific valuation mechanisms have been put in place by which Markel will acquire additional ownership over time and move towards 100% ownership. When we buy 100% of a business, the price we pay logically goes directly onto our balance sheet and consolidates into Markel Corporation's financial statement.

Under accounting rules which are confusing to me, if we buy, say 80% of the business, that amount goes on the balance sheet as you would expect. When we buy the remaining 20%, that stub amount is expensed as a period expense through the income statement and doesn't get placed on the balance sheet as an asset.

We've already done this once when we bought the additional 20% interest in AMF that increased our ownership to 100%. That transaction took place in 2010. With this noncontrolling interest item, we are essentially putting up a provision against our comprehensive income and providing for our expectation of what we will pay over the next several years for the additional minority interest we expect to buy in several of the Markel Ventures entities.

I'm thankful for my accounting degree, but I never expected to use it like this. I don't think the treatment follows economic logic, but those are the accounting rules as they currently exist and we follow them conservatively. For additional discussion of this topic, I encourage you to read Page 15 of the 2011 Berkshire Hathaway annual report, where Mr. Buffett writes about this exact issue in conjunction with the ongoing acquisition of additional percentage ownership of his Marmon subsidiary.

I apologize for spending this kind of time on these subjects as well as subjecting you to my philosophy about them, and I appreciate our dedicated and hard-working accountants who spend a great deal of time and diligent effort to understand and comply with the increasing codification of accounting rules. But I think its worth covering. Unless we all understand and appreciate what goes into comprehensive income, accounting treatment, and total economic returns, we won't fully understand and be able to reasonably measure the economics occurring at Markel.

Over the years, investors have accorded Markel a premium multiple compared to many of our peers. I think this is the result of our history of producing excellent long-term returns, as measured by the total comprehensive returns for the business as well as having confidence in the conservatism and dependability of our accounting. A premium multiple also comes from the belief and faith that will continue to be able to allocate our capital well in the future and earn above-average returns from doing so as we have in the past.

What makes me so excited is that we have more process and opportunity to effectively allocate capital than ever before in our history. We have the imagination, the creativity, and the discipline of execution to make our dreams real. I like our hand. We are now all delighted to discuss our comprehensive results that we are reporting today and we hope that you share our optimism about the future.

With that, Manny, if you'd be so kind as to open the line for your questions. Thank you.

Questions And Answers

Operator

Thank you. Ladies and gentlemen, we will now be conducting a question-and-answer session.

(Operator Instructions).

Mark Hughes, SunTrust.

Q - Mark Hughes {BIO 1506147 <GO>}

In terms of the pricing, it sounds like things are getting better in North America. In talking about the Marine and Energy and Cat-exposed properties you did suggest that the pace of improvement has moderated recently, let's say. What do you think about the broader P&C environment in the US? Is it moderating as well? Or are you continuing to see progress?

A - Richie Whitt {BIO 7084125 <GO>}

Mark -- Richie; how are you doing?

The thing I think you have to recognize is, those lines of business in London, they probably started strengthening before some of the other lines, some of the US lines as an example. The price increases we're getting in energy and the price increases we're getting on the Cat-exposed stuff -- that's on top of price increases we were getting last year. So it doesn't surprise me, given that there is still a decent amount of capacity out there, that we are not going to continue to see increasing price increases, unless we start to have events or something else happens. Capacity starts to leave.

That doesn't surprise me a lot. I think what Mike would tell you and what Mike said about the Second Quarter is, actually we saw some incremental improvement in the price increases in the US.

A - Michael Crowley {BIO 1871008 <GO>}

Yes, I agree, and I don't want anybody to think that the world isn't still competitive out there, because it is. But so far we have been working hard to get rates, and we have been successful in doing it. And I think you also have to keep in mind that the way we price our products -- a lot of times we are not the cheapest guy out there, so we're starting from a different position than maybe some of our competitors are that might be reporting larger rate increases. But the market is fairly consistent; there are still some lines, like the medical malpractice, that are very competitive, but we have been making progress.

Q - Mark Hughes {BIO 1506147 <GO>}

Got you.

The systems you talked about, how broadly are those going to be implemented? Is that across most or all product lines? And how much more granular or timely is your information going to be?

A - Tom Gayner {BIO 1896932 <GO>}

Right now, it's across really the wholesale division. So it's all the systems, it aggregates all the information up there. Over time, we would love to expand that to the specialty areas as well. London has their own systems in terms of looking at their information. It's a good bit more granular than what we have had in the past, and we were having to do a lot of work to combine information.

So we're pretty excited about it. We are able to give our underwriters and product line guys a lot more to work with now to manage their portfolios. I think its a real step forward for us.

Q - Mark Hughes {BIO 1506147 <GO>}

Thank you.

Operator

Jay Cohen, Bank of America.

Q - Jay Cohen {BIO 1498813 <GO>}

Couple questions -- on the E&S business, the premium gross slowed pretty considerably from the First Quarter growth rate. I'm wondering what is behind that?

A - Tom Gayner {BIO 1896932 <GO>}

We did have an earlier close this year that we did last year. That had a little bit of an impact on it, I am not going to quantify that because we will just have to deal with that next quarter if we did. But I think the growth rate, we are comfortable with. As I pointed out, we have been working hard to reduce the number of -- I don't want to use the word useless -- but the number of submissions that we get, where in reality we have very little opportunity to write business, and we have been more focused on spending our time on stuff that we really want to write. And we're starting to make some incremental progress there.

Other than that, we feel very good about where we are in the E&S segment, we feel very good about our submission plug, we feel very good about our buying rates, and are very optimistic about the rest of the year.

Q - Jay Cohen {BIO 1498813 <GO>}

I guess it does jump around a bit quarter to quarter. If I look at the first half results, is that a better indication?

A - Tom Gayner {BIO 1896932 <GO>}

Probably.

A - Richie Whitt {BIO 7084125 <GO>}

Jay, this is Richie. As Mike mentioned, we are constantly adding products; at the same time we're constantly looking at products that aren't performing and we will discontinue those if they are not performing. We have a little bit of noise in the numbers around some of those exited lines. There is a little bit of lumpiness between the first and Second Quarter. But I think looking at the growth rate over the first six months is probably a good way to look at it.

A - Michael Crowley {BIO 1871008 <GO>}

Yes, I agree.

Q - Jay Cohen {BIO 1498813 <GO>}

Great -- and same question in London. I'm not sure if currency played a role here, but the growth rate had been double-digit and it slowed down to about 2% on a written basis.

A - Tom Gayner {BIO 1896932 <GO>}

We've got some seasonality, obviously, to the book in London. Where we're getting a lot of the price increases as well as we were writing more premium, is the Cat-exposed Business in January 1, and April 1 are big dates for that, but January 1, in particular. So there's a little bit of seasonality there. But again, I would probably look at the six-month growth rate, and that's probably a pretty good policy.

Q - Jay Cohen {BIO 1498813 <GO>}

That is helpful.

And the last question -- the tax rate, just given where you made your money, and a lot of it came in the underwriting side, obviously, given the huge reserve release -- the tax rate to me seemed a little low. And I could talk off-line about this, but is there anything in the tax rate that distorted things at all this quarter?

A - Anne Waleski {BIO 16735457 <GO>}

No, nothing unusual, and I'm happy to take it up with you off-line, but there is nothing odd in it.

Q - Jay Cohen {BIO 1498813 <GO>}

Okay, we will follow up on that than. Thank you.

A - Tom Gayner {BIO 1896932 <GO>}

Thanks, Jay.

Operator

David West, Davenport.

Q - David West {BIO 1838548 <GO>}

One for each of you -- first, Anne, on the accounting side, on the prospective adaptation of the new DAC expense accounting, I think earlier you estimated about a $43 million impact for the full-year. Is that still a good estimate?

A - Anne Waleski {BIO 16735457 <GO>}

That's correct.

Q - David West {BIO 1838548 <GO>}

Great; and that will still be primarily Third Quarter, more Third Quarter than Q4?

A - Anne Waleski {BIO 16735457 <GO>}

Right. It is front-loaded. In the first half of the year, you'll start to see the quarter number come down and the whole year should be about $43 million.

Q - David West {BIO 1838548 <GO>}

Great. And Tom, when I look at the cost basis of the portfolio, June 30 versus year-end, it looks like fixed income basis is down, short-term down, but equity up. Is that more of a conscious acceleration of monies toward the equity portfolio?

A - Tom Gayner {BIO 1896932 <GO>}

There's a mild acceleration, but I think actually if you look at that pattern, you'd find since the First Quarter of 2009 we have steadily dollar cost-averaged our way into bigger and bigger equity positions; and the way you could really track that if you wanted to, is to look at exactly that -- the cost basis. And that's a reasonable number to look at, because our turnover -- compared to the high-frequency guys at night, we are the low-frequency guys at Markel -- our turnover statistics [ph] are very low, so that would be a relatively accurate way of seeing the dollars we are putting in the equity portfolio.

Q - David West {BIO 1838548 <GO>}

I guess it's also a reflection of the alternatives with the low interest rate environment, as well.

A - Tom Gayner {BIO 1896932 <GO>}

Yes, but I would say it's really more driven by the fact that we see equity opportunities. We think that's where we get the best, long-term, total return over time when we have the balance sheet and the business will to do it.

Q - David West {BIO 1838548 <GO>}

Great. And Mike -- turning to the FirstComp, the premiums written there have increased year-over-year; the losses that have been recorded this year are also higher than last year. Are those still running within your range of expectations?

A - Michael Crowley {BIO 1871008 <GO>}

Yes, they are, David. And FirstComp, as I said, we have given FirstComp a plan and they are executing the plan right on target with our expectations. As I mentioned in my comments, they're getting rate increases. There focusing on a geographic analysis, moving to areas where there is more opportunity for better business and moving out of some areas where historically the performance has not been good.

Last year we added a couple states. We added Alaska, we added Louisiana. They're focused on their expense reductions. So we are very comfortable that they are executing exactly like we want them to.

Q - David West {BIO 1838548 <GO>}

Are you continuing to move away from California?

A - Michael Crowley {BIO 1871008 <GO>}

Parts of California, but there are parts of California that we are comfortable with. And they are restructuring their book in California.

Q - David West {BIO 1838548 <GO>}

Very good.

And Richie -- on the international side, you mentioned in the Q that 2008/2009 were the years for the favorable development. You mentioned it extended across a lot of product lines, but could you add a little bit more color to that? Where there any particular lines that made a meaningful contribution to that favorable development?

A - Richie Whitt {BIO 7084125 <GO>}

Yes, David, it really was across product lines there. I know that it sounds like a copout, but it really was. I think part of the issue is, we have been very concerned about how the market was declining in those years, so we were very cautious in how we established the reserves. And we have had some pretty darn good developments the last few quarters. It really was pretty much across.

It was Professional Liability; there was actually some in Property; it was Marine and Energy. And then, of course, there were some 2001 and prior, where we have been incredibly cautious with those reserves, because is that it is the old legacy business that came to us when we purchased Terra Nova, so we have been very cautious with those, and got to the point where we could release some of those reserves. It was a really good quarter. The only thing I would they is, it was a really good quarter, and I wouldn't take that into numbers in the third and Fourth Quarter.

Q - David West {BIO 1838548 <GO>}

Thanks very much.

Operator

Scott Heleniak, RBC.

Q - Scott Heleniak {BIO 15171212 <GO>}

I was just wondering -- the ThomCo book, you said you expect $60 million in premium this year; and was wondering if you had a target you might be able to share for next year, for 2013? Are you going to get to the $160 million?

A - Tom Gayner {BIO 1896932 <GO>}

The $60 million is a number that we feel we will book this year. Obviously ThomCo writes a lot more business than that, but we are also transitioning the business to Markel paper from other carriers, and so the ability to forecast exactly what the slippage might be there or something is not something we want to do at this point. But their volume was considerably more than $60 million.

Q - Scott Heleniak {BIO 15171212 <GO>}

Okay. And just want to touch on the Markel Ventures, Tom, you mentioned some investments that you're making there. Just wondering if you could elaborate on some of the areas. Is that across the board, or was there a few specific divisions you can talk about?

A - Tom Gayner {BIO 1896932 <GO>}

It's across-the-board. In each of the companies, there's some pretty dramatic opportunities to expand. There are competitors who have more leveraged balance sheets and are having competitive difficulties and give us the opportunity to pick up some business. We are undergoing fairly dramatic physical expansions in a lot of the different business units.

Q - Scott Heleniak {BIO 15171212 <GO>}

Okay. And just one other one on Markel Ventures -- you acquired two Dutch companies in the quarter. Was that a one off? Or should we continue to expect to see international acquisitions at Markel Ventures?

A - Tom Gayner {BIO 1896932 <GO>}

My insurance colleagues were hanging around Holland, so we were in the neighborhood. That just happened to be the case. The Markel Ventures Company, in fact -- Ellicott is the most dramatic example -- but they do 80% of their revenue outside of the US. It's a global company and has been so for decades. AMF, at the time we purchased it back in 2005, might have been 10% or 15% international. Probably that's more like 35% or 40% these days. A lot of these businesses are seeing international expansion opportunities, and we don't plan on geographies; what we plan on is trying to find what the best business opportunities are and going there.

Q - Scott Heleniak {BIO 15171212 <GO>}

Okay, that is helpful. Explained that correlation there.

The other one is -- just wanted to ask about the foreign government exposure you have. Can you remind us what exactly you have most concentrated, which countries; and whether you have reduced exposure to any of those countries at all this year or whether that has changed much this year?

A - Richie Whitt {BIO 7084125 <GO>}

The good news is that the traders haven't really changed, because we did not have too much in the way of countries where we didn't want to have exposure that you read about in the headlines now. What we do is, we try to match the liability of our insurance policies, and we take in premiums in euros or sterling, and we are going to make a claims payment in one of those currencies. We buy bonds in that currency to the best of our ability, to match that liability and we buy the very highest credit quality we can, and we take the results as they are. We don't try to engineer a result that would be better than the natural circumstances we create.

Q - Scott Heleniak {BIO 15171212 <GO>}

Okay, thanks a lot.

A - Tom Gayner {BIO 1896932 <GO>}

Let me come back to your ThomCo question. I'm going to give you a little more clarity. When we acquired ThomCo, the prior year, they had placed over $160 million of premium. There are a couple of programs that ThomCo wrote -- a couple of their smaller programs -- that we probably won't move to Markel paper because it's a different underwriting appetite than we have. That could give you little more clarity on ThomCo.

Q - Scott Heleniak {BIO 15171212 <GO>}

Okay, thanks.

Operator

Ron Bobman, Capital Returns.

Q - Ron Bobman

I had a question on E&S and Aspen. On the E&S front, I was wondering if -- you touched on, you're happy with your app counts and your buying rates. Would you give us some metrics of how those two stats compared Q2 this year versus Q1 this year?

A - Tom Gayner {BIO 1896932 <GO>}

Slightly better. Not a lot of difference.

Q - Ron Bobman

Okay marginally better, but not all that dramatic.

I had a question about Aspen and changes there. Will Aspen in California -- if you could share the California rate changes for Aspen of late, and --

A - Tom Gayner {BIO 1896932 <GO>}

I don't have those in front of me. We'd be happy to talk about it. It's not inconsistent with their rate increases elsewhere, which has been in the neighborhood of around 5%.

Q - Ron Bobman

Okay, and should we think of Aspen shrinking this year compared to last?

A - Tom Gayner {BIO 1896932 <GO>}

No. You mean in California?

Q - Ron Bobman

Either way. I was thinking California.

A - Tom Gayner {BIO 1896932 <GO>}

At this point, they are not shrinking, in total.

Q - Ron Bobman

Understood. Thank you, very much.

Operator

(Operator Instructions).

Meyer Shields, Stifel Nicolaus.

Q - Meyer Shields {BIO 4281064 <GO>}

Two quick questions, if I can. One, on the International or London side, we saw the expense ratio up 300 basis points or so, sequentially. Is that a consequence of the reserve releases?

A - Tom Gayner {BIO 1896932 <GO>}

It's two things. It's the deferred acquisition account -- and how many points is that?

A - Anne Waleski {BIO 16735457 <GO>}

In London?

A - Tom Gayner {BIO 1896932 <GO>}

In London. We will find that.

The other thing is with the significant reserve releases, we've got bigger bonus accruals going up. It's interesting there -- you have prior year reserve releases, but there is no such thing as prior-year bonus expense that goes against this year's expense ratio. So little bit of a mismatch when you think about it.

Q - Meyer Shields {BIO 4281064 <GO>}

Okay. And when we calculate the tax rate for the London segment, should we be using the UK corporate tax rate?

A - Tom Gayner {BIO 1896932 <GO>}

Say that one again I'm sorry?

Q - Meyer Shields {BIO 4281064 <GO>}

Yes, if we try and break up the expected tax calculation based on the geographic (technical difficulty), is that reasonable? Should we use UK corporate tax rates for the London insurance market segment?

A - Tom Gayner {BIO 1896932 <GO>}

No, the way the US works is, it taxes you at 35% on everything you make in the world. Really, the thing you should think about, probably, is, we pretty much have a 35% rate other than our union portfolio, which is not taxed.

Q - Meyer Shields {BIO 4281064 <GO>}

Okay. Great, thank you.

Operator

Adam Klauber, William Blair.

Q - Adam Klauber {BIO 1494359 <GO>}

What is your overall loss trend in workers comp for 2012? And what's that trend in California, workers comp?

A - Tom Gayner {BIO 1896932 <GO>}

I don't have those with me. I don't have that information here.

Q - Adam Klauber {BIO 1494359 <GO>}

Okay, fine. As far as ThomCo -- are those programs growing right now? The programs you're keeping, the main ones?

A - Tom Gayner {BIO 1896932 <GO>}

They're pretty stable. During the transition, we are being very careful and trying to be efficient at what we're doing, because we are transitioning from another company's paper to our paper, which requires notices and everything else. But they are very stable.

Q - Adam Klauber {BIO 1494359 <GO>}

Okay, okay. And then, finally, on the Lloyd's reserve release -- you've had significant redundancies, but this is a bigger number. Could you do some review or -- why is the number that big this quarter?

A - Michael Crowley {BIO 1871008 <GO>}

Really, we didn't do anything differently. Like I said, I think we were probably, if anything, been fairly cautious the last few years, given the decline in the market. In 2008 and 2009 have gotten to an age now where you can believe what you are seeing in terms of development. That really drove it more than anything. We are very consistent in terms of how we work with reserves, and put up the margin in safety in terms of our reserves. Nothing really changed other than just, we have gotten to a point on those two accident years where you can believe what you are seeing.

Q - Adam Klauber {BIO 1494359 <GO>}

Okay, thank you very much.

A - Tom Gayner {BIO 1896932 <GO>}

I want to just emphasize one point about the reserve discussion. We're talking about geography on the right-hand side of the balance sheet in terms of accounting, whether it's in the loss reserve or retained earnings by the time reserves are released. The good news is, that over on the left-hand side of the balance sheet -- the assets -- the number is unchanged.

The cash was collected a long time ago. It's in the investment portfolio, it's making money, no matter what geography you have it on the right-hand side of the balance sheet. I think that's a fundamentally important point that goes into the comprehensive economic thinking of the way we run things around here.

Q - Adam Klauber {BIO 1494359 <GO>}

Great, thank you.

Operator

Thank you. We have no further questions in the queue at this time. I would like to turn the floor back over to Management for any closing remarks.

A - Tom Gayner {BIO 1896932 <GO>}

Thank you, very much, we are glad you joined us. We look for to seeing you again soon. Thanks; goodbye.

Operator

Ladies and gentlemen, this concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.