

Q3 2017 Earnings Call

Company Participants

- Jay Stanley Bullock, Chief Financial Officer & Executive Vice President
- Mark E. Watson, President, Chief Executive Officer & Director
- Mark H. Rose, Chief Investment Officer & Senior Vice President
- Susan Spivak Bernstein, Senior Vice President-Investor Relations

Other Participants

- Anthony To, Analyst
- Elyse B. Greenspan, Analyst
- Matthew J. Carletti, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good day, and welcome to the Argo Group Third Quarter 2017 Earnings Conference Call. All participants will be in listen-only mode. After today's presentation, there will be an opportunity to ask questions. Please note this event is being recorded.

I would now like to turn the conference over to Susan Spivak Bernstein, Senior Vice President of Investor Relations. Please go ahead.

Susan Spivak Bernstein {BIO 1514699 <GO>}

Thank you, and good morning. Welcome to Argo Group's conference call for the third quarter 2017 results. Last night, we issued a press release on our earnings, which is available on the Investors section of our website at www.argolimited.com.

Presenting on the call today is Mark Watson, Chief Executive Officer, who will share his thoughts about the quarter, after which, Mark Rose, our Chief Investment Officer, will discuss the investment results and strategy, following by Jay Bullock, Chief Financial Officer, who will add some more color and commentary to the financial results. As the operator mentioned, this call is being recorded.

As a result of this conference call, Argo Group management may make comments that reflect their intentions, beliefs and expectations for the future. Such forward-looking statements are qualified by the inherent risks and uncertainties surrounding future expectations generally, and may materially differ from actual future results involving any one or more of such statements. Argo Group undertakes no obligation to publicly update

forward-looking statements as a result of events or developments subsequent to this conference call. For a more detailed discussion of such risks and uncertainties, please see Argo Group's filings with the SEC.

With that, I'll turn the call over to Mark Watson, Chief Executive Officer of Argo Group. Mark?

Mark E. Watson {BIO 20610831 <GO>}

Thank you, Susan. Good morning, everyone and welcome to our third quarter conference call. Despite this year's historic industry-wide catastrophe losses, Argo's strategy of building a leading specialty insurer remains our focus. Our U.S. business continues its strong growth momentum, and we're excited about the future of our International operations, including the Lloyd's business.

Overall, our risk and capital management framework protected our balance sheet during the quarter, with all of the activity that we'll go through in a minute. And with our underwriting expertise, our focused distribution strategy and expanding global platforms, we're in a great position to pursue the attractive market opportunities as long-needed price increases take shape. Having said that, even absent the effect of recent events, Argo has never been in a better position to successfully compete in International Specialty markets.

As you all know, the third quarter of 2017 was significantly impacted by the natural catastrophe losses from hurricanes, Harvey, Irma, and Maria as well as the earthquake in Mexico. Losses from these events are the worst in a quarter since 2005, which included hurricanes, Katrina, Rita, and Wilma. Back then where, we were not yet in the reinsurance business, and at the time, I remember thinking that on a risk-adjusted basis that we would be better off as a reinsurer than an insurer. And of course, shortly after that we then acquired our Bermuda platform, and as you know, we closed on our Ariel Re acquisition during the first quarter of 2017, which also gave us greater scale in the reinsurance business, but also contributed to the losses in this quarter. I mentioned this to note that on a reported basis, our adjusted net operating loss was \$57.4 million or \$1.97 per share in the third quarter. So, a little bit more volatility, but when I think about the return that we get on reinsurance versus insurance, I think it's a better use of our capital and aggregate exposure to property cap.

These results as we pre-announced last month were negatively impacted by a \$104.5 million of cat losses from various events during the quarter. We also reported \$15 billion of higher attritional losses, primarily related to the property business at Syndicate 1200. For transparency and to give you a clearer perspective of the core profitability of our book, we presented the adjusted underlying results in the tables in our press release, which if you haven't had a chance to look at, I would encourage you to do so.

One important point to consider coming out of this complex quarter is that, in 2018, our reinsurance programs will be purchased in a slightly different manner than this year. Because the Ariel Re reacquisition didn't close until the first quarter of this year and

FINAL

Bloomberg Transcript

because most reinsurance and retro programs were put in place on the first of the year, we ended up with multiple programs and that means multiple retentions in some instances. So, I think that we'll be in a much better spot going forward in 2018, as you know, we're in the middle of placing all of that right now and we can talk more about that in Q&A if you would like.

Moving on to capital management, during the quarter of 2017, we repurchased \$33.8 million or a little over 560,000 shares of stock at an average price of, I believe, just under \$60 a share. As we've talked about in the past, we will capitalize on opportunities when our stock price corrects to a level that does not in our view reflect the value of the franchise we're building. That brings our total repatriation through share purchases and dividends to nearly \$560 million since we began our share repurchase program.

We ended the quarter with book value per share of \$60.96, up approximately 3.4% from year-end 2016, inclusive of dividends paid. The risk management strategies we employed to protect our balance sheet leave us well positioned now to write more business at better returns in improving pricing environments. And I say that because I do think we'll see pricing going up across the board, mainly in places where we had losses, but I do think we'll see it in many places. Having said that, I think given the changes that we've made to our portfolios over the last few years, as you'll see in the numbers, I think that, that we will still move ahead even if market pricing doesn't change very much.

Before I talk more about the market, I want to highlight some of the positive underlying trends that continued to emerge in our results. First, we continue to generate strong profitable growth in our U.S. operations. In the third quarter of 2017, gross written premiums were up 18.9%, with the strongest growth in the liability and specialty lines. Specifically, growth was fueled by casualty and our Excess and Surplus Lines business, our surety business, Argo Pro, our professional liability business, and Rockwood, our mining business, and the specialty program business as well.

From a profitability standpoint, the adjusted ex-cat, accident year loss ratio was 57.2% for the U.S. compared with 58.5% from the prior year. This marks the 17th quarter that our loss ratio in the U.S. was below 60%, which is why I was saying a minute ago that I think we're in a really good spot even if pricing doesn't improve at the level that we think it might.

This strong growth and improved profitability in the U.S. operations reflects the benefits of our growing profitable relationship strengthened by our ongoing investments in technology. Through digitization and predictive analytics, we've built better tools for risk selection and pricing, and of course, those investments continue.

Moving on to our International operations, despite recent catastrophic losses and pricing challenges, we're confident about the future of our International operations, which include London, Bermuda, Latin America, and other emerging markets.

Third quarter 2017 gross written premium was at 67.6%, driven primarily by the acquisition of Ariel Re. Having said that, even if you exclude Ariel Re, our International business in the

FINAL

third quarter was up approximately 7%, benefiting from our growth in our Bermuda casualty business, global professional lines and Brazil.

From a profitability standpoint, the adjusted ex-cat accident year loss ratio deteriorated to 58.3% from 49.9%, due primarily to higher attritional losses on the property book that I mentioned earlier from Syndicate 1200. Fortunately, this is a short-tail business, most of which was written in 2017 and will earn out over the next few quarters. We've not renewed the porous performing accounts, have refined our risk appetite and are using new pricing models to better predict the future loss costs of the written business.

I've been talking for many quarters about the margin pressure at Lloyd's, of which property has experienced the most significant declines over recent years. Given that the Lloyd's market is expected to absorb a disproportionate share of the recent catastrophic losses, I would expect to see significant pressure in the market to raise rates to a level that produces more adequate returns. Our position as one of the larger syndicates in the market should make us a primary beneficiary of these emerging favorable pricing trends. Having said that, if we don't see that happening, then I suspect we'll reallocate our capital more towards our reinsurance business and away from the D&F property business, if pricing doesn't improve to levels we think are appropriate.

Over the last 15 years, we built a franchise strongly positioned to capitalize on opportunities in the U.S. – in the U.S., mainly our Excess and Surplus Lines business, commercial lines, our Bermuda insurance and reinsurance markets, Lloyds, and most recently in Latin America. While the timing of our Ariel Re acquisition led to additional third quarter losses, and again, I'm referring to having multiple retentions in our reinsurance and retro program, the transaction gives us greater scale to position the company to benefit from the improvement in global property reinsurance rates and our other lines of business at Lloyds.

And I think that when you look at all the risks that we've added to the books through the Ariel Re transaction, I know there was some concern at the beginning of the year of how this would play out. And while it would have been nice if maybe this happened a year from now, I feel pretty comfortable that our risk management of our balance sheet is sound. And I think we just had a number of incidents where we had a chance to prove that to ourselves and to everyone else.

In conclusion, while the wind blew and our results reflected its effects, our strategy of growing as a specialty insurer is consistently proving to be sound. We continue to grow through our strategic acquisitions, our focused global distribution strategy, company-wide systems improvements, wise investing, product innovation, and ambitious recruitment of top-tier talent. And because results in our investment portfolio reflect our active management and total return strategy, I'm now going to ask Mark Rose, our Chief Investment Officer, to make some comments on our portfolio and current market trends.

Mark H. Rose {BIO 1557365 <GO>}

Bloomberg Transcript

FINAL

Thanks, Mark. Let's go over the Argo investment performance for the quarter. The third quarter total return was up 1.3%, which is flat to the third quarter of 2016. Year-to-date, we are up 4.4% versus 4.3% in 2016. However, with the acquisition of Ariel Re and the growth of the portfolio, our dollar return was \$20 million higher to \$194 million. From a top-down perspective, our solid portfolio growth year-to-date has been driven by our allocation in U.S. in global equities, versus 2016, which was largely driven by a rally in the credit markets.

As you can see in Argo's Investor Presentations, we invest 10% to 11% of our portfolio in equities with a U.S. to global split of around 70/30. We track allocation in our risk portfolio. For the quarter, our risk portfolio was up 3.3% and year-to-date 9.8%. This compares favorably to the risk portfolios' performance last year of 2.8% and 9.1% for the year - nine months into 2016.

Year-to-date, Argo's risk portfolio especially benefited from the U.S. equity allocation, which was up 10.3% versus 6.8% in 2016, and global equities, which were up 15.7% year-to-date versus 8.1% in 2016. Given the outsized growth in equities over the last 12 months, we have trimmed the portfolio to maintain our targeted balance in risk assets. Argo's allocation also to high-yield emerging market debt and private equity contributed to the risk portfolios' year-to-date returns; high-yield up 6.3%, EM debt 10.2%; and private equity 9.4% year-to-date.

Moving to the core bond portfolio, the core bond portfolio was up 0.8% versus 0.6% in 2016 for the third quarter. Year-to-date, our core bond portfolio was up 2.7% versus 2.9% in 2016. During the quarter and year-to-date, our core bond portfolio benefited from spread compression in the U.S., although to a lesser degree versus 2016, when the debt markets rallied into the first nine months. Our International debt portfolios, which make up approximately one-third of the core bond portfolio, benefited this year from maintaining a short duration bias, with rising sovereign rates, and benefited from a weakening U.S. dollar.

Our reported net investment income for the quarter was \$30.8 million, down \$1.9 million versus a year ago and down \$12.8 million versus the second quarter of 2017. Our second quarter benefited from the sale of SureTec, which was part of our alternatives portfolio. Year-to-date, our net investment income was \$105 million versus \$90 million in 2016. This aided from growing income from bonds and stocks, and alternatives were up mainly due to the SureTec sale this year.

With that, I will turn the call back to Jay.

Jay Stanley Bullock {BIO 3644311 <GO>}

Thanks, Mark and good morning everyone. Let me add some additional color on the financials and then open it up to questions. We recognize that there are a lot of moving pieces to the numbers and have included additional exhibits in our press release to show our underwriting margins adjusted for extraordinary items, demonstrating the true

underlying trends in the business. Of course, the majority of the unusual items in the quarter emanate from a significant catastrophe losses experienced by the industry.

As noted and consistent with our pre-announcement, we reported a \$104.5 million in losses in the current quarter. Included in this number is a catastrophe-related premium adjustment of \$14.5 million, that was a direct reduction to earned premium. This adjustment is related to an aggregate contract and represents the reversal of the expected outcome of that contract over the first nine months of the year. The contract had the effect of reducing retained losses by a much larger amount.

We got an additional impact to net earned premium due to other catastrophe and risk management purchases of \$8.1 million. During the second half of the year, we made additional purchases to align the combination of Ariel Re and our existing businesses with our risk appetites. These purchases, which totaled approximately \$20 million, were made in each case for the balance of the year and as a result will be fully recognized by year-end. We estimate the benefit from recoveries under the contract to-date to be in excess of the premiums paid.

Finally, as reported, we increased our current accident year loss pick primarily related to property business in Syndicate 1200. The net effect of this was to raise the current year non-cat loss ratio for the International segment to 56.4% or higher than we find acceptable. We expect that non-cat loss ratio to continue to the fourth quarter of 2017, and then gradually move back to a more acceptable level over the first six months of 2018, as the earned premium related to the 2017 business earns out.

The second item is the expense ratio, the reported expense ratio in the quarter of \$42.7 million reflects the lower earned premium of \$22.6 million, and a one-time charge of \$3.5 million related to a longstanding premium tax dispute that was resolved during the quarter.

Adjusting for these one-time items, the expense ratio would have been 39.5%, and reflects a modest shift to business with the higher acquisition costs, that's surety and programs, and our ongoing investments in technology and people in support of our strategic plans as evidenced by the strong growth, most notably in the U.S. business of 18.9% in the third quarter.

For the third quarter of 2017, the effective tax rate for the group was 7% versus our base assumption of 20%. The lower-than-expected rate was mainly due to more than 60% of our results attributable to our Bermuda operations, a zero tax jurisdiction. For the first nine months of 2017, the effective tax rate for the group was 22.3% or very close to our expectations.

Moving on to balance sheet and reserves, we had a favorable development in the overall loss reserves of \$1.3 million in the third quarter of 2017 compared to \$2.9 million favorable development in the comparable period of 2016. The U.S. operations reported favorable development of \$10.7 million. In addition, there was also a favorable development in International operations of \$2.6 million.

Run-off operations had unfavorable development of \$12 million in the third quarter of 2017, compared to \$11.5 million in the 2016 period. This was the net effect of unfavorable development in A&E reserves, as cases continue to stay open longer than anticipated, offset by a favorable move in our risk management run-off reserves.

We ended the quarter with a pre-tax unrealized embedded gain of \$180 million, compared to \$159 million at June 30, and a \$134 million at March 31, 2017. Majority of the gains are part of the equity - of our equity holdings. Our fixed income holdings remain very short in duration, and the carrying value approximates market value.

Operator, that concludes our prepared remarks, and we're now ready to take questions.

Q&A

Operator

We will now begin the question-and-answer session. At this time, we have no questions. So, I would like to turn the conference back to over Mark Watson for any closing remarks. Pardon me, we do have a question that just entered in.

So, the first question will come from Anthony To with KBW. Please go ahead. Anthony, your line might be muted.

Q - Anthony To {BIO 19955085 <GO>}

Hi. Thank you for taking my questions. Just a broader question, can you give us an update on your cyber initiatives, and possibly any commentary on the hurdles in respect to this line and how that has progressed, I guess, from the beginning of the year and how will you move forward?

A - Mark E. Watson {BIO 20610831 <GO>}

Are you referring to the cyber that we offer as a product or how we manage cyber for our own risk?

Q - Anthony To {BIO 19955085 <GO>}

The product?

A - Mark E. Watson {BIO 20610831 <GO>}

Okay. Well. So, we've been offering cyber as a product for over a decade. And we continue evolving the product. Most of the inforce policies (22:00) that we have are for small businesses and I suspect that will continue in the near-term, and I say that because I don't think that cyber is adequately priced for larger risks. And I think that as we've seen a number of events happen over the course of the year, I think that the market will continue to get a bit more level set. We're looking at both first-party and third-party coverage and I think that we'll continue evolving our product just as we do others over the course of the year, but it is one of many products that we offer. It is not the leading product that we're

focusing on at the moment. So, I would say that's probably a better discussion a year from now than right now.

Q - Anthony To {BIO 19955085 <GO>}

Okay. Thank you for that. And, I guess lastly what's your current appetite in writing private flood given the recent storm activity?

A - Mark E. Watson {BIO 20610831 <GO>}

Well. It depends on the product. I mean, there's some programs that we offer that includes flood and some that don't. As long as it's properly priced, we offer it. But given that in the United States, you have the National Flood Insurance Program, and other markets for flood, I don't really see us changing our product mix too much, to be honest.

Q - Anthony To {BIO 19955085 <GO>}

Got it. Thank you so much for your answers.

A - Mark E. Watson {BIO 20610831 <GO>}

Okay

Operator

The next question comes from Matt Carletti with JMP. Please go ahead.

Q - Matthew J. Carletti {BIO 5249827 <GO>}

Hey thanks. Good morning.

A - Mark E. Watson {BIO 20610831 <GO>}

Good morning.

Q - Matthew J. Carletti {BIO 5249827 <GO>}

Just a couple of questions. Mark, you touched on, in your opening comments, a bit about consolidating the two reinsurance programs, Ariel and the legacy Argo next year. Can you expand on that a little bit? And what sort of follow-on impacts you see that having on how you're looking to structure it in terms of how it may impact earnings volatility and capital needs?

A - Mark E. Watson {BIO 20610831 <GO>}

Sure. So, going forward, obviously, we'll have a lot more to say about this on the next call, because then we'll have finished what we're working on placing in the marketplace right now. So, I can tell you what we expect to do, but we'll see exactly how it plays out over the next, well, gosh, now we're down to probably eight weeks.

FINAL

Bloomberg Transcript

FINAL

I mentioned in my remarks at the beginning that because we had acquired Ariel in the first quarter, they had already put their retro program in place and we had already put our reinsurance and retro programs in place as well, and of course, we all keep some risk net, and it varies from one event to the next, meaning in the first event you tend to have your retention at one level and depending upon how you buy reinsurance, if you structure it in a certain way, sometimes your retention will drop down for second and third events, which was certainly the case with Ariel's retro program, given some changes that we made to it over the summer. But we still ended up with two different net retentions. Going forward, our expectation is that we will combine as much of our cat exposure into one or two reinsurance and retro programs that combine at a certain point, so that has the effect of giving us one retention per event, and presumably at a lower level than the combined retentions that we had in 2017. So, assuming that's the case, then that should lead to lower volatility.

So, instead of having - and again, I'm just going to speak generally because it's very different for each event. Now, instead of having \$50 million to \$70 million of net retention in any event, it may be that we have \$40 million or \$50 million of net retention next year for each event. So, don't hold me to those numbers just yet, because it depends on price and terms, but I'm just speaking figuratively.

And then, the other thing that I didn't talk about, which I think, Jay, actually alluded to in his remarks, we also bought a bit of backup cover when we saw all of the activity happening, not because we felt we were running out of cover, in fact we've got plenty of cover left, but when you have a number of things happen, you always want to make sure you're covered, and given that we hadn't seen how the Ariel Re portfolio would perform over the year as compared to the Argo Re portfolio, particularly for earthquakes, which we haven't had one, we felt we buy a little bit more backup cover, and when you add all of that up, that was another 15-plus-million-dollars that we probably won't spend in 2018.

Q - Matthew J. Carletti {BIO 5249827 <GO>}

Okay. Really helpful. Really appreciate the color. Next question. Just you know, you guys have been busy this year, you're integrating Ariel. We've obviously seen press releases on hiring some really qualified people to help build some of the products. How should we think about kind of a go-forward view on expense ratio. We know there's some to be taken out of Ariel, how that come in over time? Where do you expect that to go and kind of over what timeframe?

A - Mark E. Watson {BIO 20610831 <GO>}

Yeah. So, Jay mentioned a few things that were impacting the expense ratio this quarter.

Q - Matthew J. Carletti {BIO 5249827 <GO>}

Right.

A - Mark E. Watson {BIO 20610831 <GO>}

So, take those as given and let me add.

Q - Matthew J. Carletti {BIO 5249827 <GO>}

Right.

A - Mark E. Watson {BIO 20610831 <GO>}

So, the other things that are really impacting it are restructuring of our operations this year, and so we've made changes in our IT. We've outsourced a substantial portion of IT, but there's a cost associated with that. We finished the outsourcing project in the first quarter of 2018. We restructured part of - Jay has restructured part of his finance and accounting shop. So that led to some expenses this quarter.

I think we're kind of through trying to see what we can do to streamline our business and take expense out that way. And of course, so we have to finish integrating Ariel, which I think also finishes in the first quarter of 2018.

So far, things have gone really well with the integration. We're very happy with what we've acquired, and again, that's people, systems, portfolio. But these things take time and that's always the challenge with an acquisition is being methodical and making sure that you can actually integrate things. And I think that everyone on the team is doing a great job of bringing that together.

So, there's a lot of moving parts this year, which creates a lot of noise in the numbers. I would expect that to start going away in the first quarter of next year a bit and then I think that we'll have a lot more visibility to the profitability of the business and the benefits of the changes that we've made this year and the benefits of acquiring Ariel in the second quarter of next year. But we've got all the people we need, now it's just a question of continuing to execute and keep pulling expense out of the business and writing more good profitable business.

Q - Matthew J. Carletti {BIO 5249827 <GO>}

Okay. Great. And then one last question kind of became a topic du jour yesterday, just the new tax bill, and obviously it's just a proposal and probably will change 20 times before anything final, but as it stands kind of the provision in there that talks a bit about kind of shifting internal quarter shares basically would be the application for P&C, what are your initial views of that in terms of what the potential impact on Argo might be?

A - Mark E. Watson {BIO 20610831 <GO>}

Well, we've expected this to happen for a decade, but we've also expected interest rates to go up for a decade too. So, we've kept our investment portfolio duration short and we've also been pretty conservative in how we've used intercompany reinsurance on average and I'll just say on average.

Q - Matthew J. Carletti {BIO 5249827 <GO>}

Sure.

FINAL

Bloomberg Transcript

FINAL

A - Mark E. Watson {BIO 20610831 <GO>}

The Bermuda company only reinsures about 50% of what's written in the U.S. So, we've always underwritten off of two pools of capital, whereas other companies that have mainly focused on their Bermuda capital have reinsurance quota shares that could be 80%, 90%. So, I don't think it really impacts us very much. If you look at our average, and again, this is only an average, effective tax rate is around 20%. So, I don't see us really changing how we operate our business very much. And as you point out, the tax if anything is enacted by Congress, and that's a big if, it will change many times between now and then.

Q - Matthew J. Carletti {BIO 5249827 <GO>}

Right. I mean, on the margins, it sounds like there could even be a scenario where there's potential for benefit in the sense that while you might start paying tax on what's offshored, you lose the excise tax and you're already paying 35% on what's cut domestically and that would drop to 20%, we'd have to shake all that math out, but it sounds like it's not far from where it is?

A - Mark E. Watson {BIO 20610831 <GO>}

That's right. I would say that in anticipation of this years ago, I think we were pretty well hedged from whatever might happen. And so, there might be a slight net benefit to us on an absolute basis. And relative to our competitors who heavily reinsure their U.S. businesses back to wherever their company is domiciled, I think we're in a much better competitive advantage to them on an after-tax basis.

Q - Matthew J. Carletti {BIO 5249827 <GO>}

Great. Thanks very much for the answers, Mark.

Operator

The next question comes from Elyse Greenspan with Wells Fargo. Please go ahead.

Q - Elyse B. Greenspan {BIO 17263315 <GO>}

Hi, good afternoon. So, I have a couple of questions. My first question, I was just hoping to get some additional color just in terms of the market outlook and how you see the pricing environment developing. What kind of - what prior cycle would you compare the one that we're heading into to, and how long do you think rates can stay from - ? And how is I guess Argo positioning itself to take advantage of firmer commercial lines pricing environment?

A - Mark E. Watson {BIO 20610831 <GO>}

Yeah, so every cycle is a little different. When you look at the aggregate amount of insured losses that the industry has incurred this year, the number that keeps being bantered around is a \$100 billion, and that's probably right, which is a pretty big number. We always muse about, well, is it going to be one big event or a series of events, which is

FINAL

of course what's happened - the latter has happened this year. Some programs have been hit pretty hard - sorry, some property programs have been hit pretty hard.

But I think that, if you - and I've said this on previous calls over the last few years, last year's results at an industry level, looked pretty good and the year before that, pretty good. But that's because there was an absence of cat activity and many companies, including ours, had a fair amount or a substantial amount, depending upon the company, of positive prior-year development coming through in their financial results. If you stripped out the prior-year development, then on an accident year basis, things were getting pretty thinly priced. And so with the wind blowing multiple times this year, and also the earthquake in Mexico, it's pretty clear that market pricing across the board, not just property pricing, is a bit thin. Okay. And that's kind of, on average, if you look at our financial results - sorry, if you look at our loss ratios and that of some of our better competitors, the margins are still pretty good. I mean, our loss ratios are still on average in the 50s. So, for us, it's just getting to scale and managing expenses, which is why I said in my opening remarks even if pricing doesn't move up, we're still in a position to do well going ahead because of the repositioning that we've had in our portfolio.

Having said that, if you're primarily exposed to property cat, particularly if it's in insurance as opposed to reinsurance, then your product is probably pretty well underpriced and it's impossible to ignore it anymore. So, I can't imagine property pricing not moving up substantially - excuse me, cat exposed properly moving up substantially, but there are other lines of business across the board that, I believe, are also underpriced and I think that there has to be a movement across the board to reset pricing to really take into consideration the risk that we're all assuming.

So, when I add all of that up, this feels a little more like 2001 than it does in 2005. In 2005, you saw property pricing move and it was mainly U.S. property pricing that moved. I think this time, you see more lines moving up than just property, because I think it's just impossible to hide it when the wind blows. I can be more specific, but I hope that gives a sense of what I think will happen.

Q - Elyse B. Greenspan {BIO 17263315 <GO>}

No, that's helpful. And do you think, (37:28) how long the kind of firm - like how long (37:31) depended upon, the re-insurance and how much kind of capital comes back in there or how do you think about how long in terms of number of years and renewals that property prices could stay - could continue to increase?

A - Mark E. Watson {BIO 20610831 <GO>}

Well, I would say that, that I have a different answer for property versus the market as a whole. I think that because we all have better risk management tools and processes, we have a better sense for where pricing ought to be, and I think that if you look at the last six or seven years, there hasn't been that much volatility at a market level in pricing. So, I don't think you'll see things shoot up like they did in 2001, nor have we really seen the declines that we saw in the late-90s from the last market cycle. I think there's a little less volatility today than there was then.

FINAL

But as for property, I think that there will be capacity, both the insurance or I should say insurance, reinsurance and retro markets. I think that there may be perhaps a bit less capital coming in to support retro, but I think there will still be a fair amount. I don't think that you'll see - I think the new capital coming in will now recognize that actually there really are assuming risk, and I think that changes their view of risk and therefore the price of risk. So, I don't see rates shooting up one year and then crashing back down the next. I think it'll be a little more disciplined.

Now, I could be wrong, because at the end of the day, market price is controlled by I would say either the most aggressive or least intelligent underwriter in the market. And fortunately, I don't think that has been us. But there will always be somebody new coming in and the only way they can differentiate themselves from the rest of us is price. But I don't see that happening this year. I don't see a whole list of new companies coming in to underwrite risk. I think if there is new capital coming in, it's on the back end in the ILS market and that's probably to support retro.

Q - Elyse B. Greenspan {BIO 17263315 <GO>}

And you see that - so you see all these capital coming in into the retro market you've seen today, so kind of do you think that the market will fully reload? I'm sorry, just to follow-up to that point?

A - Mark E. Watson {BIO 20610831 <GO>}

No, no that's okay. Yeah. So, I wouldn't say all of this capital. I think that when you look at the - let me be more precise. When you look at where capital was eroded, a substantial amount of losses that were incurred by the industry this year found their way into the retro market. So, I think that if you had to pick one place where capital needs to be refreshed, it's in the retro market. That's why I was focusing on that

So, I think that it's comes back in to replace what's gone away. And I don't think there's a new wave of capital coming in. I just think that there will be a handful of new entrants into the marketplace.

Q - Elyse B. Greenspan {BIO 17263315 <GO>}

Okay. That's very helpful.

Thanks, Mark. I appreciate all the color.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to Mark Watson, CEO, for any closing remarks.

A - Mark E. Watson {BIO 20610831 <GO>}

Thank you, everyone for joining our call today. As I mentioned in my opening remarks, and as we talked about in the Q&A, there is a lot going on in our industry right now. And I think

that we'll all have a lot to talk about at the beginning of the year in February when we report our year-end results. The thing that I am most focused on right now is getting our balance sheet set for 2018. As I mentioned in my remarks earlier, I think that all of these events did a really good job of showing ourselves that our balance sheet is very well protected, that we're well positioned in many markets where we operate to move ahead. And I look forward to talking to you all about that in more detail at the end of the fourth quarter when we talk again in February. Operator, that concludes my remarks.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.

This transcript may not be 100 percent accurate and may contain misspellings and other inaccuracies. This transcript is provided "as is", without express or implied warranties of any kind. Bloomberg retains all rights to this transcript and provides it solely for your personal, non-commercial use. Bloomberg, its suppliers and third-party agents shall have no liability for errors in this transcript or for lost profits, losses, or direct, indirect, incidental, consequential, special or punitive damages in connection with the furnishing, performance or use of such transcript. Neither the information nor any opinion expressed in this transcript constitutes a solicitation of the purchase or sale of securities or commodities. Any opinion expressed in the transcript does not necessarily reflect the views of Bloomberg LP. © COPYRIGHT 2022, BLOOMBERG LP. All rights reserved. Any reproduction, redistribution or retransmission is expressly prohibited.

FINAL

Bloomberg Transcript