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Q1 2011 Earnings Call

Company Participants

- Anne Waleski, Chief Financial Officer, VP & Treasurer
- Mike Crowley, President and Co
- Richie Whitt, President and Co
- Tom Gayner, President

Other Participants

- Beth Malone, Analyst
- Doug Mewhirter, Analyst
- Mark Hughes, Analyst
- Vincent D'Agostino, Analyst

Presentation

Operator

Greetings and welcome to the Markel Corporation First-Quarter 2011 Earnings Call. At this time, all participants are in a listen-only mode. A 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, Tom Gayner, President of Markel Corporation. Thank you, sir, you may begin.

Tom Gayner {BIO 1896932 <GO>}

Good morning. It's my pleasure to welcome you to the Markel Corporation's First Quarter conference call. Thank you, all for joining us. On today's call we will follow our normal line up, with Anne Waleski leading off with the financial results, followed by Mike Crowley and Richie Whitt with operational comments, and then I will discuss our investment and other operations. After our comments, we will all be available for your questions.

Before we begin, I'm duty bound to remind you that during today's call 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.

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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 I'll turn it over to Anne.

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Anne Waleski {BIO 16735457 <GO>}

Thank you, Tom. Good morning, everyone. I will follow the same format today as I have in past quarters. I will discuss our underwriting results followed by a brief discussion our investment results, and bring the 2 together with a discussion of our total results.

Starting with the underwriting results, First Quarter 2011 gross written premiums were just under $600 million, up 21% compared to 2010. The increase in 2011 was due to higher gross premium volume in the specialty admitted and London insurance market segments. For the quarter ended March 31, 2011, the specialty admitted segment included $58 million of gross written premiums from our FirstComp workers' compensation operations, which we acquired in late 2010.

The increase in gross written premiums in the London insurance market segment was due in part to our acquisition of Elliott Special Risks in late 2009, which has now been fully converted from an MGA to a risk-bearing operation. We also saw significant increases in premium volume within our marine and energy division, due in part to offering larger line sizes and an improved pricing environment.

Net written premiums were approximately $520 million, up 16% to the prior year. Retentions were down slightly in 2011 at 88% compared to 91% in 2010. Approximately 2 points of this decrease relates to reinstatement premiums associated with losses incurred during the First Quarter of 2011. Earned premiums increased 12%, primarily due to higher earned premiums in the specialty admitted and London market segments as a result of higher gross premium volume compared to 2010.

Our combined ratio was 112% for 2011 compared to 101% in 2010. The increase was due to a higher current accident year loss ratio, and a higher expense ratio, partially offset by more favorable development of prior year's loss reserves compared to 2010.

The combined ratio for 2011 included $69 million or 15 points of underwriting loss for natural catastrophes that occurred in the First Quarter, including the Australian floods, the earthquake in New Zealand, and the Japanese earthquake and subsequent tsunami. Favorable redundancies on prior years' loss reserves increased to $75 million or 16 points of favorable development compared to $38 million or 9 points of favorable development in 2010.

The increase was primarily due to more favorable development of prior year losses in the excess and surplus lines segment. In the First Quarter of 2010, we reported $14 million of adverse development on an errors and omissions program for mortgage servicing

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companies. In the First Quarter of 2011, we resolved a significant portion of our outstanding liabilities associated with this same program, and as a result reduced loss reserves by $16 million.

Our 2011 expense ratio increased approximately 6 points to 44%. The increase in the expense ratio is due in part to higher personnel costs. Additionally, our First Quarter 2010 expense ratio benefited 2 points from a favorable arbitration settlement and an anticipated insurance recoverable.

Now moving to our investment results, investment income was up approximately 2.5% in 2011 to $70 million due in part to higher invested assets and dividend income compared to 2010. Net realized investment gains were $11 million compared to $16 million in 2010. Realized gains in 2011 included no write-downs for other than temporary declines in the estimated fair value of investments, compared to $2 million of write-downs in 2010.

Unrealized gains increased $20 million before taxes in 2011, due to increases in equity securities. Tom will comment further on investments in his portion of the call. Looking at our total results for 2011, we reported net income to shareholders of $8 million compared to $43 million in 2010. Book value per share increased to $329 per share at March 31, 2011, from $326 per share at year end. The effective tax rate was 14% in 2011, compared to an effective tax rate of 31% in 2010. The decrease from 2010 was due in part to anticipating comparable levels of tax-exempt income while estimating lower pre-tax income in 2011 as compared to 2010.

Now, I'll make a few comments about cash flow and the balance sheet. Regarding cash flow, net cash used by operating activities was approximately $9 million for the three months ended March 31, 2011, compared to net cash provided by operating activities of approximately $4 million for the same period of 2010. Historically, First Quarter is our lowest cash-generating quarter, as we pay employee bonuses, agent incentives, pension contributions, and other items of that type in the First Quarter. We would expect the numbers to improve in the Second Quarter.

Regarding the balance sheet, investments in cash held at the holding company were approximately $800 million at March 31, as compared to a little less than $900 million as of December 31, 2010. The decrease is due in part to interest payments on debt.

At this point, I will turn it over to Mike to further discuss operations.

Mike Crowley {BIO 6836605 <GO>}

Thanks, Anne. Good morning. The First Quarter results for the North American operations were encouraging, especially admitted segment gross written premiums were up significantly, as Anne mentioned, compared to the same period last year. This was due in part to our growth in our equine and livestock, agriculture, accident and health, and the FirstComp premiums in the First Quarter.

Excluding FirstComp, the specialty premium was up 8%, which was slightly better than expectations. The combined ratio was in line with budget and prior year. The expense ratio was higher than prior year due to a one-time offset in prior year for an E&O recovery.

FirstComp's revenues for the First Quarter exceeded expectations due to strong non-California performance across the regions. Encouragingly, we are seeing stronger than anticipated audit and endorsement numbers due to better than expected payrolls. Markel products training for FirstComp sales staff was also initiated in the quarter at regional sales meetings, and all outside and inside sales staff at FirstComp have now received this cross-sale training.

In addition, 400 Markel agencies have been selected as targets for opportunities with FirstComp. This cross-sell effort has begun to produce results, and we downed our first accounts in the quarter. Expectations for the cross-sell revenue between FirstComp and Markel specialty are being developed, and will be monitored going forward.

Other highlights in the specialty admitted segment for the quarter include a new wine program, kicked off by our agriculture division that produced 75 new accounts in the quarter. Our boys and girls club program gained traction with the addition of key new accounts. And we added talent to our program division with the addition of Vicki Webb, who joined Markel with 20-plus years experience, all previously with AIG.

Our E&S segment wholesale division had a solid First Quarter. While total E&S gross written premiums for the quarter was down 5%, this decline was due primarily to a reduction in a significant book of forced-place [ph] business. Excluding the reduction in this one program, total wholesale premiums were flat to a year ago.

Our total core regional premium was up 7%. This growth occurred in 4 of our 5 regions, and across a number of our product lines. We define core regional premium as the premium underwritten directly in the regions versus the few lines that are underwritten centrally. Meetings with our national agents and advisory council were held during the quarter, and the feedback from this group continues to remain very positive regarding our One Markel strategy.

We continue to focus our operational efforts on reducing the time from receipt of submission to delivering a quote, and as a result we're moving some centralized resources back under the control of the wholesale division and the regions. Submissions for the unit segment were up 17% over prior year, and the total number of buy-ins [ph] were up 8.7%.

As a result of the increased submissions, we continue to refine our agency force by terminating poor performers and focusing our efforts on those partners who are delivering the best results. Our goals include priority quote service to our top agents, eliminating full submission entry on a targeted 20% to 30% of submissions, prescreening out those that we have little chance of writing. And also by improving overall clearance, data entry, and quote turnaround times.

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Finally, during the quarter, we were very pleased to announce the appointment of Susan Swanson to Executive Vice President, and Head of the Midwest Region. Susan has been with Markel for 29 years, and is a proven and experienced leader, and we are confident she will do a terrific job in the Midwest for us.

On the underwriting side, 3 high-profile product lines were launched in the quarter -- admitted architects and engineers professional liability, miscellaneous errors and omissions, and excess transportation. There are also currently 15 to 20 other smaller product offerings that are in various stages of development. We announced that we would no longer continue developing a crisis management product, and we repositioned our transportation product line as well.

Joining our product line leadership team was John Termini, as Managing Director of Environmental. John joined us from Aston Specialty Insurance Company with 20 years experience. He began his career in 1990 as a hydrogeologist environmental scientist. And I will give you a heads up, don't ask me what that is on the Q&A, because I don't know.

In summary, the rate environment for the most part has not improved, and competition continues to remain very aggressive. We are seeing growth in a number of our areas, and we continue to be optimistic that all of the various initiatives at Markel for the North American operations will produce positive results over time.

I'll now turn the call over to Richie Whitt.

Richie Whitt {BIO 7084125 <GO>}

Thanks, Mike. Good morning, everybody. Obviously, the headline news in our international operations for the First Quarter was the catastrophes in Australia, New Zealand, and Japan. Our international operations had losses from all 3 of these events, and we recorded approximately $67 million of losses related to them in the First Quarter. Just for good housekeeping, our consolidated number for the 3 events is $69 million. While this is a significant number, it's not outside our expectations for these types or magnitude of events, and the amount of business that we write in these countries.

At this point, we believe we have a reasonable handle on our exposures to the Australian floods and the second New Zealand quake, and we're comfortable with our reserves for these events. The Japanese quake and tsunami situation is still evolving, and the extent of the losses is still being determined. We have already seen several insurers come out and increase their initial estimates. While we have established what we believe is a conservative reserve for Japan of approximately $35 million in our international operations, that would be $37 million consolidated, this number is subject to greater volatility. We're going to be watching developments very closely over the next several weeks on the Japan situation.

The insurance market is reacting to these events, and property prices are moving up. At this point, I think I'd characterize the market as fluid, as buyers, brokers, and insurers are trying to find what the new market level is, and by new market level, I mean higher. At

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Markel, we expect prices to go up, and we're seeking increases on all of our property business.

Turning to other items, gross premium volume was up 22% in our international operations in the First Quarter. As Anne said, this is primarily due to our Elliott Special Risk acquisition in Canada. It's now fully online, and due to continued growth in our marine and energy book. We had a nice First Quarter in terms of growth in Markel International. So, we're off to a good start on that scorecard.

On the expansion front in the First Quarter, we gained approval for our representative office in Beijing, China. In addition, we held the grand opening of our new office in Hong Kong. These offices will help us continue to develop a presence and strategy in Asia. In addition, all of our branch offices continue to show slow but steady growth in the First Quarter, despite what is a very competitive market worldwide. We're very pleased with the seeds we're sowing in these markets. While relatively small today, these platforms are an important component of our international strategy and franchise.

No different than in the US, as Mike said, it's still fair to say it's still very competitive in the market in most areas of our international operation. Clearly, the recent catastrophe losses and deteriorating operating performance of the past few years require the prices go up. But at this point, prices are really only moving in the lines of business that have been affected by the previously mentioned significant losses.

To sum it up, the First Quarter was not the result we'd like to report to you. However, we do recognize that catastrophe losses are a part of our business, and our response to these types of events is why companies buy our product. At Markel, we're proud of the part that we play in helping people recover from these events.

Thank you, and I now turn it over to Tom.

Tom Gayner {BIO 1896932 <GO>}

Thank you, Richie. Pleased to report to you that we're off to a profitable start in 2011 in our investment and industrial operations, and I look forward to your questions. The strategic goals of the investment department are number 1, to protect and preserve the balance sheet through high quality fixed income investments. Two, to allocate as much as possible to higher total return equity investments, and 3, to increase the overall earning power and financial flexibility of the Markel Corporation through the ownership of a variety of profitable businesses. I'm happy to report that we touched all the bases during the First Quarter, and that we continue to be on track to meet these objectives.

As to the numbers, during the First Quarter the total return for the investment portfolio was a positive 1.8%. Equities were up 3%. Fixed income was up 1%. And foreign exchange effects added 0.4%. Additionally, other revenues at Markel, which are largely those of the Markel Ventures Company, were $77 million for the quarter versus $40 million in the prior year, an increase of 92%.

Markel's share of the associated EBITDA totaled $9.9 million versus $4.4 million, more than double the level of 2010. A reconciliation of EBITDA to net income is available on the website. The net of all of this is that even with the catastrophic events of the First Quarter, we are reporting positive comprehensive income and a new record high book value per share of $329.09.

In keeping with our first strategic objective of preserving and protecting the balance sheet with a fixed income portfolio, we continue to maintain a portfolio that is high quality and short duration. We don't think you get paid fully for taking credit risks, and we sure don't think you get paid for taking inflation and currency risks. Consequently, our portfolio reflects those beliefs.

It remains a matter of slack-jawed amazement to me that long-term interest rates are as low as they are, given current policies and circumstances. While we have been early in being cautious about these risks, we do not understand, and will not accept the current market offer for taking them. We think it is more important to protect the portfolio against higher future interest rates.

As to our second objective of allocating as much as possible to higher total return equity investments, during the quarter we continued to methodically increase the percentage of our portfolio invested in equity. This has been our consistent pattern for the last few years. At March 31, the total public equity portfolio grew to $1.78 billion or 54% of our total shareholders' equity.

At the nadir of the equity market in the First Quarter of 2009, equities comprised only 45% of shareholders' equity. Since that time, we have been methodically and continuously investing in high quality public equities, and in the First Quarter of 2011 we continue that pattern. While the returns on fixed income and equity investments have been remarkably similar in recent years, I expect that normal historical relationship to resume. And I think we will be well served by maintaining and increasing our commitment to equity as time goes by.

We think that certain high quality common stocks remain at attractive valuations, and we are adding them to the portfolio. We plan to continue to do so. We have been conservative in marching this percentage up gradually, due to the soft conditions in the insurance market. And we will remain modest in increasing this percentage until such time as we see tangible evidence of a hardening market and higher insurance pricing. If anything, we could be criticized for erring on the side of caution, as we've increased our equity commitment, but that's the sort of error we will make, safety first.

As to our third objective of building the earning power and financial flexibility of the Markel Corporation by owning a variety of profitable businesses, we continue to be very pleased with the ongoing growth of Markel Ventures. The businesses are producing results in line with our expectations, and they are adding value to Markel. During the First Quarter, the Ellicott Dredge Company acquired the Rohr Company, which expands Ellicott's product line from cutter suction and auger dredges to clam shell designs, which are particularly

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well suited for sand and gravel mining. We expect ongoing organic and acquisition opportunities within the growing framework of Markel Ventures.

Our portfolio and our acquisitions remain conservative. We believe in a fortressed balance sheet, which enabled us to withstand the sort of catastrophic weather and natural events we experienced during the First Quarter and that withstood the sort of financial catastrophe that occurred in 2008. By having the balance sheet we've built over the decades, we've been able to respond to opportunities in the insurance, investment, and industrial world to build the value of your Company. We continue to see opportunities on all fronts, and I'm pleased to report to you that we have both the financial and human capital to make the most of them.

With that, I'd like to open the floor for questions.

Questions And Answers

Operator

(Operator Instructions). Our first question comes from Vincent D'Agostino with Stifel Nicolaus. Please state your question.

Q - Vincent D'Agostino

Just in the 10-Q, and on the call this morning as well, you had mentioned, there was higher personnel costs that contributed to the expense ratio. I was just curious if you would be able to provide any additional color around those costs, and I have one follow-up. Thank you.

A - Anne Waleski {BIO 16735457 <GO>}

The additional costs were largely around incentive compensation true-ups in the First Quarter. And we had budgeted for this current year about a 42% expense ratio. So just slightly higher than what we had budgeted.

Q - Vincent D'Agostino

And then a question for Tom. Looking at Markel Ventures, there seems to be a common regional denominator of how the portfolio is structured with the Company's locations. Could you maybe talk about how you foresee broadening the acquisition target network outside of the Virginia area. And since we know your acquisition criteria, it would be interesting at least to me, to know how the opportunities at least initially pop up on your radar. Thank you.

A - Tom Gayner {BIO 1896932 <GO>}

As you correctly noted, a lot of things we bought so far have been Richmond based. There were local connections where we happened to know the people, which is obviously key in gaining comfort that we're dealing with the people and the sort of businesses that

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we have confidence in. Ellicott, by contrast, is headquartered in Baltimore, and PSI is in Temple, Texas. We will continue to expand the geography that we look at.

One of the wonderful things that's really beginning to occur, and frankly the deal flow that we're starting to work on and see now, is that the people in these industries and the companies that we've already purchased, means they know people that I don't. And they have contacts in their industry and people that they do business with, that they have personal relationships with, that are interested in the permanent capital features of Markel Ventures. We're being introduced to some really high quality people that sometimes do happen to live outside of Richmond, Virginia. And there's more outside than inside. We don't have limits on the 804 area code.

Q - Vincent D'Agostino

Thank you, very much.

Operator

Thank you. Our next question comes from Mark Hughes with SunTrust. Please state your question.

Q - Mark Hughes {BIO 1506147 <GO>}

Thank you, very much. The contribution of Elliot in the quarter, you'd described how you are shifting from MGA to risk bearing. Is there an incremental revenue number associated with that?

A - Mike Crowley {BIO 6836605 <GO>}

Yes, Elliott Special Risks run about $100 million in gross written premium a year. So it's probably about $100 million. We obviously bought some reinsurance on that. In terms of net written premium, it would be a bit less. Annual run rate about $100 million.

Q - Mark Hughes {BIO 1506147 <GO>}

And the incremental contribution in the quarter since it was closed in 2009, with that transition, did you get an extra pick up associated with that transition in this quarter?

A - Anne Waleski {BIO 16735457 <GO>}

It's about a $21 million increase over First Quarter of last year.

Q - Mark Hughes {BIO 1506147 <GO>}

Okay. How are you looking at the workers' comp segment now? Seems like there's been some volatility in there among public players. You're describing doing quite well outside of California. What's your sense now on pricing, competition in that market?

A - Mike Crowley {BIO 6836605 <GO>}

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It's still rigorous. This is Mike. The competition is brutal, but we have a lot of confidence in the model at FirstComp. And keep in mind that FirstComp writes workers' compensation on very, very small risk and very small premiums. And we have no intentions of changing their method of doing business and getting into the more broader workers' comp market. The workers' comp market is tough. We're confident that they have a strong understanding of the metrics in their business. And as we said in my comments, we're shifting away from California and feel good about the growth in non-California states.

Q - Mark Hughes {BIO 1506147 <GO>}

Pricing there, if we look year over year sequentially, anything you can share?

A - Mike Crowley {BIO 6836605 <GO>}

In terms of pricing? There may be some slight changes, not a lot of changes, the market's tough. As far as FirstComp, FirstComp is raising their prices.

Q - Mark Hughes {BIO 1506147 <GO>}

Okay. And then one final question. Richie, I think you had described a fluid market looking to see where the rates will settle. Any ranges you care to share? What's your judgment about what will happen with pricing there?

A - Richie Whitt {BIO 7084125 <GO>}

I wish I knew, Mark. If you point to individual risks, you can get 25% to 300%. It just depends. I don't think you can look at individual risk and say where the overall market is going. I think it is very fluid. Customers are still trying to say -- prices should be flat, maybe even prices should be down. Brokers are working hard for them in some cases. We're sticking firm to -- there's been a lot of activity. Results have deteriorated, and we need increases. And the reality is we're getting it on a lot of accounts now.

So I think there's no question it's going higher. I think everybody probably has to process what they've seen this First Quarter, which is pretty ugly. And I think that will hopefully add fuel for them to go higher. Quite honestly, they need to.

Q - Mark Hughes {BIO 1506147 <GO>}

Thanks for that color.

Operator

Thank you. Our next question comes from Beth Malone with Wunderlich Securities. Please state your question.

Q - Beth Malone {BIO 1497932 <GO>}

I have a couple questions. How big was the California market to FirstComp when you acquired it?

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A - Mike Crowley {BIO 6836605 <GO>}

It was significant. I don't have the breakdown right in front of me. Suffice it to say we are, in our business plan for this year, have projected a significant shrinkage in our writings in California. It was significant for FirstComp.

Q - Beth Malone {BIO 1497932 <GO>}

And you talked about new products in the admitted market. Are those organically grown from your existing underwriting force? Or did you acquire talent from someplace to develop these products?

A - Mike Crowley {BIO 6836605 <GO>}

Say that again, Beth. I'm sorry, I missed it.

Q - Beth Malone {BIO 1497932 <GO>}

On the new products that you're offering in admitted, is that internal expertise that you are using to develop these products, or have you acquired groups of underwriters from elsewhere?

A - Mike Crowley {BIO 6836605 <GO>}

We've acquired groups of underwriters over the last 12 to 18 months. The products that I mentioned that we launched in the quarter, the admitted architecture and the engineers professional liability, we hired Glen Mangold last year to head that practice, replacing our head of architecture and engineers who retired. And while that's an admitted product, it will be sold all across both the Markel Specialty and the E&S segment. The miscellaneous E&O is in E&S placement, and the transportation is in E&S placement.

The talent that -- let me see if I can answer your question a little bit better. We have attracted new talent over the last year or so to head our D&O and management liability practice. Sal Palero [ph], we attracted John Termini as I said to head Environmental. We had an opening there for a while. We think he brings a lot of expertise there. Glen Mangold replaced our retiring Head of Architects and Engineers. So some of this is replacing a talent that's retiring, and some of it is coming from our existing talent.

Q - Beth Malone {BIO 1497932 <GO>}

Okay. That's helpful. Thank you. And then on the expense level overall, you mentioned that you targeted around 42%, and you made some pretty significant investments in technology over the last few years. Should we anticipate that your expense ratios should start to move lower? Or does it require a better pricing environment for you to grow the top line in order to get that expense ratio to start moving lower.

A - Richie Whitt {BIO 7084125 <GO>}

I'll take that one. This is Richie, Beth. We're scheduling to finish up the big projects we've been taking on at the end of this year. Unless we get a real shift in the market here, I don't expect our expense ratio to change too much from what we're looking at today.

And that's probably that 40% to 42% range, because we have some pretty stiff investments that we're still making through the end of the year.

Those will drop off significantly next year, and that will obviously help us. You saw that our net written is up pretty significantly in the First Quarter, and obviously, that will start to earn through, and I think those things will start to help us as we get more towards 2012.

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Q - Beth Malone {BIO 1497932 <GO>}

Okay. And then on pricing in the access and surplus lines, I know that can be one of the toughest markets in a soft market. We're hearing some noise from a lot of your competitors or re-insurers that that may be starting to improve. What do you see?

A - Mike Crowley {BIO 6836605 <GO>}

I think the declines have certainly slowed in a lot of cases. Richie mentioned the property market, which is a different environment in itself, because of the catastrophes we've had. I would be remiss to say that we're seeing significant changes in pricing right now. It's still very competitive.

Q - Beth Malone {BIO 1497932 <GO>}

What about the tornadoes in the Second Quarter? Do you think you'll have exposure to the April 27, April 28 events?

A - Mike Crowley {BIO 6836605 <GO>}

Absolutely, Beth. I don't think it's necessarily significant, but clearly we'll have exposure. And we're seeing claims come in. The nature of tornadoes is you can't really predict where they go, and they have erratic paths, and it really depends on where the properties are that you insured, and what gets hit. I'm seeing anywhere, numbers, in terms of anywhere from $2 billion to $5 billion for that string of storms. And we'll pick up something on that clearly.

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Q - Beth Malone {BIO 1497932 <GO>}

And one last question, in Japan, the losses you incurred, I assume those were on a primary basis. And what was the nature? Was it marine exposure that you had? Or is that actual just property?

A - Mike Crowley {BIO 6836605 <GO>}

Our exposure primarily comes from 2 types of risk there. It would be a reinsurance of domestic Japanese companies. So we're reinsuring their property programs and provide catastrophe cover there. We provide that type of coverage. And then the other would be what we kind of call open-market property. Basically, large, multinational property accounts. So just as an example, not necessarily that we have these accounts, but a GM or a Walmart, companies that operate internationally buy international programs, and obviously, had damage to locations in Japan. Those are the 2 areas where our exposure would come from.

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Q - Beth Malone {BIO 1497932 <GO>}

Thank you, very much for the answers.

A - Mike Crowley {BIO 6836605 <GO>}

Thanks, Beth.

Operator

Thank you. (Operator Instructions). Our next question comes from Doug Mewhirter with RBC Capital Markets. Please state your question.

Q - Doug Mewhirter {BIO 7026139 <GO>}

Hello. Good morning. Just had a couple questions. The first is the -- can you describe in the E&S sector, apart from the resolution of the one large E&O claim. Where is the approximate source of the other favorable development in the E&S segment, like accident years or lines?

A - Anne Waleski {BIO 16735457 <GO>}

Most of it is coming out of professional and products liability in the 2007 to 2009 accident years.

Q - Doug Mewhirter {BIO 7026139 <GO>}

Okay. Thanks for that. And also, I guess changing direction a bit. In your other lines, your other revenues and other costs, is there still a significant positive or negative contribution from any fee based business? Like any residual MGA type business you have, or is most of that transferred to the risk bearing subsidiaries?

A - Anne Waleski {BIO 16735457 <GO>}

Most of the fee business coming out of Elliott Special Risk has transitioned. Most of that is no longer in other. But we do still have some revenue and expenses being generated by the Aspen MGA operation.

Q - Doug Mewhirter {BIO 7026139 <GO>}

Thanks. And for my last question, could you repeat what your effective operating tax rate was for the quarter, and also what -- it seemed like there was a tax policy change. How you would expect it to even out over the year?

A - Anne Waleski {BIO 16735457 <GO>}

The effective tax rate was 14%, which compared to 31% in 2010. In my comments, the decline is in part due to anticipating lower pre-tax income, but the same amount comparable levels of tax-exempt income. Additionally, you are right, we do have a change which we talked about at year-end relative to a lower effective tax rate on our foreign operations as a result of a change in our plans regarding the amount of earnings considered permanently reinvested in our foreign subs.

Q - Doug Mewhirter {BIO 7026139 <GO>}

I guess -- go ahead.

A - Mike Crowley {BIO 6836605 <GO>}

I was just going to say, Doug, basically what that means is, if you don't plan on repatriating those earnings to the US, you don't have to layer on top a US tax rate. That provides some benefit there. And the other thing I'd just say is, obviously, with the substantial catastrophe losses in the First Quarter, we're now estimating lower pre-tax for the year, and that just makes the permanent difference on the tax exempts that much larger, so it tends to drive your effective rate down.

A - Anne Waleski {BIO 16735457 <GO>}

Right. And I would say our expectation for this year would be a mid-teens rate.

Q - Doug Mewhirter {BIO 7026139 <GO>}

Okay. Well, thanks. That's all my questions. Thanks for your answers.

A - Anne Waleski {BIO 16735457 <GO>}

Sure, thank you.

Operator

Ladies and gentlemen, there are no further requests for questions at this time. I'll turn the conference back to management for closing remarks. Thank you.

A - Mike Crowley {BIO 6836605 <GO>}

Thank you, very much for joining us. I'll remind you that our shareholders meeting is on Monday, May 9 at 4.30 PM here in Richmond. If you happen to find yourself in town, stop by. Thanks so much, we'll talk to you soon.

Operator

Thank you. This concludes today's conference. All parties may disconnect. Have a great day.

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