Q1 2017 Earnings Call

Company Participants

- Craig W. Howie, Chief Financial Officer & Executive Vice President
- Dominic James Addesso, President, Chief Executive Officer & Director
- Elizabeth B. Farrell, Vice President-Investor Relations
- John P. Doucette, Executive Vice President, President and Chief Executive Officer of the Reinsurance Division
- Jonathan M. Zaffino, Senior Vice President & President-North America Insurance Division

Other Participants

- Brian Meredith, Analyst
- Elyse B. Greenspan, Analyst
- Jay Gelb, Analyst
- Joshua D. Shanker, Analyst
- Kai Pan, Analyst
- Nicholas Mezick, Analyst
- Sarah E. DeWitt, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good day everyone, and welcome to the First Quarter 2017 Earnings Call of Everest Re Group. Today's conference is being recorded. At this time for opening remarks and introductions, I will turn the conference over to Ms. Beth Farrell, Vice President of Investor Relations. Beth, please go ahead.

Elizabeth B. Farrell {BIO 1986541 <GO>}

Thank you, Debbie. Good morning and welcome to Everest Re Group's first quarter 2017 earnings conference call. On the call with me today are Dom Addesso, the company's President and Chief Executive Officer; Craig Howie, our Chief Financial Officer; John Doucette, our President and CEO of Reinsurance Operations; and Jon Zaffino, our President of North American Insurance Operations.

Before we begin, I will preface our comments by noting that our SEC filings include extensive disclosures with respect to forward-looking statements. In that regard, I note that statements made during today's call, which are forward-looking in nature, such as statements about projections, estimates, expectations and the like are subject to various risks. As you know, actual results could differ materially from current projections or expectations. Our SEC filings have a full listing of the risks that investors should consider in connection with such statements.

Now, let me turn the call over to Dom.

Dominic James Addesso {BIO 1428096 <GO>}

Thanks, Beth. Good morning to all, and welcome to our first quarter earnings call, and we have a positive report for you today. Before we dive into the quarterly results, I would like to touch briefly on the characteristics that have helped the Everest Re Group deliver above average returns. Certainly our size and scope are important differentiators, but more critical to our success is the entrepreneurial and decisive culture that permeates our organization. We are not satisfied with the status quo, but instead, continually seek to expand our horizons for new opportunities as well as increase our penetration to existing clients.

Examples of this would be our expansion into credit opportunities in both our reinsurance and insurance businesses. And just this quarter, we participated on the new National Flood Reinsurance Program which represents new business to the market. As governments seek to privatize certain markets, we could see similar additional opportunity. So why is this important? These new market segments allow us to continue to diversify our portfolio away from the more competitive markets and sustain underwriting profitability. This and a constant focus on expenses, and our expanding use of capital market tools explains why we continue to outperform the market. This now leads me to our discussion on results, which again were quite positive for the quarter.

Operating income increased 17% in the quarter to $260 million, giving rise to $6.29 in earnings per share, and a 13% operating ROE for the quarter. The increase in earnings is a result of an increase in both the underwriting and investment income. Furthermore, the underwriting result improved in both the reinsurance and insurance division. While our reinsurance combined ratio was up slightly over the prior year, due to a relatively minor increase in cash, the increase in earned premium propelled us to a higher underwriting result.

Increase in earned premium is a continuing result of broadening our reinsurance product set over the last several quarters into crop, mortgage, and other credit related opportunity. Entering (03:50) into credit related business has contributed to the almost 1 point improvement in quarter's attritional combined ratio, 80%. John Doucette will discuss this in greater detail in his Reinsurance Operations.

The insurance segment results improved year-over-year to an underwriting gain position. This was in part a result of the drag in a prior year from the crop operation that we sold late last year. Excluding the Heartland crop business, the attritional combined ratio of 98.1 for the quarter reflects a stable loss ratio, but an uptick in the commission and operating expense ratio. The commission ratio was up on a changing business mix, while operating expenses are trending as planned.

We continue to build out the North America and European platforms, and have had great success with gross premiums written up 21% in the quarter excluding crop. Expenses are still outpacing earned premium thereby putting pressure on the expense ratio. But we would expect this to stabilize as the operation matures. However, despite this more elevated expense ratio, you will find that by comparison, we are still quite efficient relative to the market. We are pleased with what the team has accomplished in a relatively short timeframe, which was aided in part by the market dislocation created by a few large players. In fact, given the opportunities presented by this market turmoil, we (05:28) actually accelerated our investment in the operation. You'll hear more details on all this later in Jon Zaffino's Operations report.

Another strong spot this quarter was investment income, which increased approximately $20 million. Our alternative portfolio accounted for some of that improvement, along with a higher asset base. Our strategy here is not much different than the fundamentals principles we use in our total business, conservative yet look for differentiated opportunities that provide good margins relative to risk. As a result, our overall portfolio has a beta of less than one, but yet our returns have been in the upper quartile relative to our peer group. Overall, we continue our optimism in our ability to not only outperform, but also provide above market returns through the cycle.

I maintain that optimism because of, as I referenced earlier, the well diversified platform we have built, but perhaps more importantly because of our adaptability to market changes and opportunities. That comes from a corporate culture that embraces new opportunities, and that has the skilled talent to execute. You will hear more about our newest initiatives from my colleagues and how we continue to build our franchise for the future. Thank you and I look forward to your questions later on.

Now to Craig, for the financial report.

Craig W. Howie {BIO 17579923 <GO>}

Thank you, Dom, and good morning everyone. Everest had another solid quarter of earnings, with net income of $292 million for the first quarter of 2017. This compares to net income of $172 million for the first quarter of 2016. The 2017 result represents an annualized net income return on equity of over 14%.

Net income included $32 million of net after tax realized capital gains compared to $51 million of capital losses in the first quarter of last year. 2017 capital gains were primarily attributable to fair value adjustments on the equity portfolio. After tax operating income for the first quarter was $260 million compared to $223 million in 2016. The overall underwriting gain for the group was $183 million for the quarter compared to an underwriting gain of $171 million in the same period last year all segments reported underwriting gains for the quarter.

In the first quarter of 2017, Everest saw $20 million of current year catastrophe losses related to Cyclone Debbie in Australia compared to $10 million of catastrophe losses during the first quarter of 2016. The overall current year attritional combined ratio was

84.5%, down from 85.3% in the first quarter of 2016 primarily due to a lower commission ratio in 2017. Our overall expense ratio of 5.8% was down slightly from the first quarter of 2016.

Our reported combined ratio of 86% was flat compared to the first quarter last year. For investments, pre-tax investment income was $122 million for the quarter on our $18 billion investment portfolio. Investment income was 19% above last year. This result was primarily driven by an increase in limited partnership income which was up $17 million from the first quarter of 2016 primarily due to the turnaround in energy related investments compared to last year. Pre-tax yield on the overall portfolio was 2.8% with the duration of just over three years.

Foreign exchanges reported another income. For the first quarter of 2017, foreign exchange losses were $4 million similar to the first quarter of 2016. Other income also included $2 million of earnings and fees from Mt. Logan Re compared to $3 million of income in the first quarter of last year.

On income taxes, the 9% effective tax rate on operating income was on the low end of our expected range for the year. First quarter of 2017 tax rate is slightly lower than the 10% tax rate for the full year of 2016 due to a $5 million tax benefit for a FASB tax accounting change related to share based compensation. Previously these tax benefits were booked through additional paid-in capital in the balance sheet. The effective tax rate is an annualized calculation that includes planned catastrophe losses for the rest of the year. Should catastrophe losses come in lower than this estimate, it would be expected that the tax rate would go up.

Stable cash flow continues with operating cash flows of $382 million for the quarter compared with $375 million in the first quarter of 2016. Shareholders' equity for the group was $8.3 billion at the end of the first quarter, up $272 million from year-end 2016. This is after taking into account capital return through $51 million of dividends paid in the first quarter of 2017. Capital position remains very strong and continues to grow.

Thank you and now John Doucette will provide a review of the Reinsurance operation.

John P. Doucette {BIO 7178336 <GO>}

Thank you, Craig. Good morning. We are pleased to report another strong quarter with $178 million of reinsurance underwriting profit. Our earnings reflect the continued strength of our reinsurance franchise, sustained by product and geographic diversification, underwriting discipline and ultimately relevance to our clients. Everest longstanding global presence, high ratings and nimble execution underpin our outperformance through this part of the underwriting cycle.

Before discussing renewals, here's some color on the first quarter results. Total gross written premium for the first quarter was $1.2 billion an increase of 19% compared to Q1 2016, through a combination of growth on existing business and new business opportunities. This included $53 million of crop premium on the new quota share arrangement done in conjunction with the sale of Heartland, as well as new structured reinsurance business. The growth in these profitable, diversifying, and strategic lines, fortifies our competitive strength in an otherwise difficult market.

Additionally, these customized transactions require a differentiating breadth of skills from a sizeable and strong partner. Our agility in executing these bespoke transactions is highly valued by our clients, and accomplished to attracting best-in-class underwriting actuarial and analytical talent and providing them appropriate resources within a lean and responsive organization conducive to creative solution.

The Q1 loss ratio increased from 55.6% to 53.2% in Q1 2016, driven in part by an increase in the cat loss ratio with losses from Cyclone Debbie impact in the quarter. In addition, the quarter experienced lower favorable prior year loss development and an uptick in the current year attritional loss ratio. The shift in the composition of our book with a higher expected loss ratio on the new crop business accounted for the slight increase in our attritional loss ratio.

In our U.S. reinsurance segment, Q1 2017 gross written premium was up 8% to $579 million. Growth was driven by crop and credit related reinsurance writings, offset by a 9% decrease in property lines as we walked away from underpriced pro rata business. The Q1 combined ratio for the U.S. reinsurance segment was up 3.1 points, affected by the new crop writings with a higher attritional loss ratio and non-catastrophe weather related losses. This was partially offset by a lower commission ratio. Although the crop writings produced higher combined ratios, they consume relatively little capital.

Our international reinsurance segment, premium was $266 million, up 13% for the quarter and up 8% on a constant dollar basis. We saw growth across most of our territories: Middle East, Africa, Latin America, Singapore, and Canada. Increased property pro rata business and some higher cat XOL business, particularly in loss affected regions, coupled with our growth in our worldwide facultative operations provided for this growth. The combined ratio for this segment improved by 1.1 points to 86.6% despite higher cat losses and lower level of reserve release. This was due to an almost 6 point improvement in the attritional loss ratio, driven by better experience in certain regions and a lower mix of casualty pro rata business.

Our Bermuda segment written premium increased 57% to $321 million or up (15:59) 61% on a constant dollar basis. The growth was largely from new business including new credit opportunities and account true ups on financial line treaty. In addition, premium growth also came from both London and Europe, including motor quota shares and new strategic reinsurance deals with large core global clients. The combined ratio improved to 83.5% with a lower current year attritional loss ratio, no prior year reserve development, and a lower expense ratio.

Moving on to the 4/1 renewals, Everest is well-positioned in a market that appears to be stabilizing. Rate pressures continue, but are showing signs of moderating, as ample capacity is partially offset by increasing demand in some zones. In the Asia-Pacific market, renewal rates in loss-affected areas such as New Zealand were up an average of 5% with rates in a range of flat to down 10% in other areas. Japanese renewal decreases were more moderate at flat to down 5%.

In the U.S. property markets, excessive loss rates were flat to down 5% with indications that some early 6/1 renewals will be flat. We are expecting incremental Florida demand fostering some market stability, but this could be somewhat offset by decreased purchasing by citizen. As Dom mentioned, we did participate on the new National Flood Program that came to the market and we are exploring other potential opportunities around flood coverage.

In our casualty book, reinsurance rates, terms and conditions are stable but reductions on underlying business continue, put pressure on overall economics. Nevertheless, we were able to reallocate our capital to more favorable opportunities, and we see some improvement in certain facultative lines.

Internationally, some of the recent currency movements have allowed foreign-based competitors to report accounting gains, softening the otherwise weak profitability across major classes and delaying market stabilization. However, rate decreases were smaller than in prior renewals.

In the UK, Ogden rate change, which has affected the UK motor market has caused some market disruption with treaties being extended as insurers reassess their strategies. Large rate increases and program restructurings have been the norm on affected motor program.

Throughout the world, our clients demand, multi-faceted solutions commensurate with their expanding scope, complex capital requirements and unique demand. Our clients clearly want to trade with reinsurers like Everest that offers scale, expertise, and a sustainable franchise.

We just completed our latest cat bond transaction with the issuance of $1.25 billion of Kilimanjaro II catastrophe bond. That brings our total catastrophe bond capacity to $2.8 billion, which in conjunction with Mt. Logan and our balance sheet elevates Everest's total capacity and capital across both rated and unrated balance sheets to almost $13 billion. This places us among the very largest reinsurers in the industry, making us even more relevant to our clients and brokers.

Overall, Everest Reinsurance operation remain well-positioned and diversified by product, distribution, geography, client, and capital, giving us numerous levers to control our market efficiency and effectiveness. We continually enhance our strategic focus to succeed in the new reinsurance world order.

Thank you. And now, I will turn it over to Jon Zaffino to review our insurance operations.

Jonathan M. Zaffino {BIO 16652236 <GO>}

Thank you, John, and good morning. The Everest Global Insurance operations performed well and in line with our expectations in the first quarter. Many strategic actions we have taken to establish a world-class specialty diversified insurance organization by becoming increasingly evident in our results. A consistently expanding top line across a balanced portfolio is testament to the relevance we are achieving among our insurance and brokers.

We continue applying opportunities to profitably expand our business across our global platform despite a challenging market environment. As a result, Everest Insurance is firmly positioned in the market landscape as a specialty provider offering a wide breadth of product solutions and lines of business that we expect to outperform over the long-term.

As in prior quarters, due to the divestiture of Heartland in late third quarter of 2016, I will be discussing our comparative results, excluding this business.

For the first quarter of 2017, the global insurance operations registered $434 million in gross written premium, an increase of $75 million or 21% over first quarter of 2016. Another outstanding result and consistent with the growth rate we saw in 4Q 2016. This represents the ninth consecutive quarter of growth for our global insurance operation, each division within the North American segment contributed to this growth, with a notable strong performances from our Canadian in accident and health platforms, each of which grew in excess of 30%.

A further note, roughly 18% of our production in the quarter was derived from our recent new business launches and from our Lloyd's operation, which as you will recall has entered only second year of account. We remain encouraged by this balanced contribution across the diversity of our growing underwriting platform.

Net written premiums for the quarter were $346 million, an increase of $37 million or 12% over 2016. As we've shared in the past, net written premium growth slightly lags gross written premium growth due to the marginally more conservative reinsurance position we have taken to support our many new underwriting divisions.

There were some notable transactions in the quarter, particularly within our A&H group that also contributed to a slightly lower net-to-gross ratio. We expect this to normalize throughout the year. Net earned premium in the quarter increased more in line with our gross written premium on a percentage basis producing $323 million, which represents 17% growth from the first quarter of 2016.

Turning to the combined ratio, the GAAP combined ratio for the first quarter was 98.4%. While we are pleased to have produce some underwriting profit of more than $5 million in the segment, we expect to show continued improvement as earned premium develops in future quarters. The overall loss and loss adjustment expense ratio for the global insurance operations remained essentially flat year-over-year registering a 68.2% in the first quarter of 2017 versus 68.1% in the first quarter of 2016. On an attritional basis, these ratios improved to 67.8% and are flat period-over-period.

Let me offer a couple of additional comments to further amplify our performance. First, both 1Q 2016 and 1Q 2017 had unprecedented levels of cat activity in the U.S. with 12 PCS events declared in the first quarter of this year. Despite this, our book is performing well. Our conservative loss estimates for our U.S. property lines coupled with a series of deliberate underwriting actions taken over the past several quarters had largely mitigated the impact of these events to us.

Second, as earned premium comes in on several of our new business launches referenced earlier, which have historically generated better combined ratios, we expect the shipping portfolio mix will result in improved overall profitability. Again, the bottom line, we expect improvement in the underlying loss ratios as we move through the year.

Our expense ratio in the first quarter was 30.3%, up when compared to 28.2% in the first quarter of 2016, but essentially in line with the full-year 2016 results of 29.9%. The change to first quarter 2016 represents roughly a one-point increase in our commission in premium tax expenses and a one-point increase in our operating expenses.

There remains moderate pressure on our expense ratio due to the continued organic build of our operation along with the impact from the lag of earned premium. We anticipate the expense ratio to moderate and stabilize as we continue on our growth path. As Dom mentioned an expense ratio of roughly 30% remains very competitive in the specialty insurance segment.

I'll now turn to the performance of our major insurance portfolios starting with the North America P&C book, which is our largest business. In the first quarter, the core P&C portfolio grew 15% to $353 million over the prior year period. They continue to gain momentum across the breadth of our specialty P&C operation, headlining in the quarter were a continued steady growth from our new business initiatives, which represented 17% of our total premium production in the quarter, a highest level we have experienced to-date.

The continued addition of outstanding talent supports our strategy across underwriting, claims, technology, actuarial and several support areas. And the announcement of a portfolio transaction, we consummated to effectively acquire renewal rates to a direct and facultative book of property business. This book of business closely aligned with our own appetite and fits neatly into our property expansion strategy, and we are pleased to welcome several new talented underwriters to the Everest family.

Our accident and health group also delivered an excellent quarter of growth, with a 38% increase over the prior year comparable quarter. Our continued efforts to thoughtfully diversify and grow our product lines, including Medical Stop Loss continues to prove successful. Notably in the quarter, several of our new A&H products, particularly our sports disability offering also contributed meaningfully to growth. We expect we will continue to find opportunities across the balance book of A&H business as the year progresses.

Our Lloyd's operation also continued its expansion. The Syndicate contributed $21 million to the insurance growth in the quarter, nearly doubled the contribution from 4Q 2016. All lines of business ranging from our property through our professional indemnity books experienced growth, despite a challenging rate environment. We remain deliberate in our growth pursuits and are finding opportunities for continued expansion.

Turning to the operating environment, the first quarter represented a predictably mixed picture from a rate perspective. The overall level of rate change varies meaningfully by major line of business. As a general statement across the entirety of the North American portfolio, I would say that rate pressures are somewhat mitigating. In fact, we have many lines of business that are gaining rates across our book.

Let's take a look at this by a major line of business. Commercial auto again headline our rate change results in the first quarter, as it has in several prior quarters. We continued to achieve high-single to low double-digit rate changes for this line of business. Again, our exposure to this line is limited as it continues to represent less than 5% of our overall writings.

Also, as in prior quarters, the primarily general liability and umbrella markets continue to remain in the tight range and are basically flat year-over-year. The professional liability markets remain competitive with continued rate pressures in the mid single-digit range across various lines. We continue to take a conservative posture in this market. Of particular interest to us is the broader attention to rate in terms being exhibited in the U.S. property market, while capacity remains plentiful, the market continues to find the bottom.

Directional price changes month-by-month are recognizing this reality. 12 PCS convective storm cat events in the first quarter, a record for insured losses, on top of last year's prior record quarter should add momentum to this price action. As we noted last quarter, we feel there is a larger positive story emerging that will allow us to selectively expand our portfolio.

Finally, workers' compensation, our largest line of business, continue to experience moderate rate pressure in the low to mid single-digit range on the back of continued favorable underwriting results. While not an unexpected result, there is still an opportunity to consider new business in certain select territories as we closely monitor the many trends across this line. While the rate environment is trending predictably line by line, the overall rate picture is improving across the entirety of our portfolio.

In conclusion, we are pleased with our start to the year. Our team continues to execute very well against the major strategic objectives within our organic growth plan. As a result, our market brand and capabilities continue to grow. The Annual RIMS Conference, which is underway as we speak, is reaffirming our belief in the Everest Insurance value proposition. Based on the client interaction and meeting schedules of our colleagues in attendance, it is clear we are being embraced by a growing range of brokers and insurers alike. We look forward to continuing our momentum and reporting back to you on our progress next quarter.

With that, let me turn it back over to Beth for Q&A.

Elizabeth B. Farrell {BIO 1986541 <GO>}

Thank you, Jon. That ends our prepared remarks. I'd like to open up for the Q&A session.

Q&A

Operator

Thank you. We'll take our first question today from Elyse Greenspan with Wells Fargo.

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

Hi, good morning. My first question, I was hoping just to get a little bit more color. You guys saw exceptional growth in your reinsurance business to start the year. I know lots of moving parts with the crop, some growth in credit, and then also in other geographies outside of the U.S., but when you kind of blend your market outlook together, how do you really see the growth trajectory over the remaining three quarters? And just a question in relation to the Q1, is any of the premium growth that you saw kind of one-time in nature or are there any multi-year covers included within the strong growth you saw in the first quarter?

A - John P. Doucette {BIO 7178336 <GO>}

Good morning, Elyse, it's John, and thanks for the question. So, I think there were some one-off parts to the growth in the reinsurance operation. As we mentioned, there were some true-ups, but there is also a combination of growth in the mortgage and credit lines. Some of those are new deals, and some of those are multi-year deals, where we're continuing to get premium from prior quarters. So, we would think a normalized growth rate would be high single-digits.

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

And do you think that high single-digit is something that's sustainable over the balance of 2017 based on how you see the market right now?

A - John P. Doucette {BIO 7178336 <GO>}

We do. We do think that – I mean, there's a lot of gives and takes in that, but we continue to see new opportunities. There's places where we're coming off of business that we don't think is attractive, but at the same time we continue to find new opportunities, both – we talked about the motor quota shares in Europe tied to Solvency II. Also, in the UK motor market, there's opportunity. But then also in the mortgage and the credit and one-off structured deals that we have in the pipeline now.

A - Dominic James Addesso {BIO 1428096 <GO>}

And this is Dom. I mean, it's also highly dependent upon June 1. So, while we have had lots of new opportunities and growth in new areas, new types of products that we're offering, in particular credit, but depending on what happens with rates is just one (33:31), but still yet to be determined. So hard to predict some sustainability to our growth rate, and we don't yet know what June 1 will be offering us.

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

Okay, great. You guys did collide (33:47) an Ogden loss, did you guys have any adverse development associated with the change in the rate there?

A - Dominic James Addesso {BIO 1428096 <GO>}

The Ogden loss, the prior period event, and that was covered in our prior year-end reserve position. And it's a kind of thing that though not specifically known at prior years, the kind of thing our reserve analysis contemplates for things that can go wrong. So, it's completely covered in that reserve position. We estimate that with the current discount rate that they're applying up to a $30 million was the impact.

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

And that's included in how your reserves are set today?

A - Dominic James Addesso {BIO 1428096 <GO>}

Yes, absolutely.

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

Okay. And then in terms of capital return, there was no share repurchase in the quarter. I know we also saw a slowdown at the end of 2016. When you guys are thinking through capital return right now, how do you kind of balance just the growth opportunities that you're seeing in reinsurance as well as insurance? And then just also where – your stock is obviously trading at a higher valuation, so can you just update us on your thought process for the first quarter, as well as when you think about capital return over the balance of 2017.

A - Dominic James Addesso {BIO 1428096 <GO>}

Sometimes I feel like a broken record on this one. As you know, we do not give any predictions as to what we will be doing in terms of share repurchases. But relative to the first quarter how we were thinking about it was that, as you did see, we had significant growth. So we remained a little bit more cautious on capital return, to the point of not buying in any shares. This coupled with the fact that we had a number of cat events that were potentially swirling out, surround out there. So that was part of our deliberations.

And then the third item that you made reference to, of course, was our rise in stock price. While in and of itself and by itself not a sole determinant, but along with the other factors will led us to not be purchasing any shares back in the first quarter. And none of that means that we won't be back into the market throughout the year, but again, it has to be balanced up against events that are occurring in the marketplace as well as our premium growth trajectory.

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

Okay. Thanks so much, and congrats on a great start to the year.

A - Dominic James Addesso {BIO 1428096 <GO>}

Thank you, Elyse.

Operator

We'll take our next question from Kai Pan with Morgan Stanley.

Q - Kai Pan {BIO 18669701 <GO>}

Thank you and good morning. So first question on the insurance side. What do you think are your sort of competitive advantages that you can grow in this – like a more challenging market condition, at the same time improving your core or your combined ratio towards your 95%, like maybe long-term target? How soon do you think you can get there?

A - Jonathan M. Zaffino {BIO 16652236 <GO>}

Good morning, Kai, this is Jon. I think our competitive position in the market is quite strong. I think sits on the backs of (37:17) we are obviously trading with the benefit of a significant balance sheet from the Everest Group, which credentials exceedingly well in a number of our chosen markets.

We have been able to amass what we feel is very distinguished talent, taking advantage of the dislocation in the market over the past couple of years. And remember, our insurance platform has been around for a while, so we have a pretty good reach in terms of different market segments, different product lines, et cetera. So as we refined our strategy and focus on the areas that we thought would contribute more to our bottom line and also help us increase our relevance with clients by providing solutions, we're now starting to see the momentum of all those actions take hold. So that's been very encouraging.

As for why we feel that's going to produce better results, there's a lot of changes. So, to borrow John's comment earlier, there's a lot of ins and outs here, lots of different mixed scenarios coming in. Our new businesses tend to trend at a lower ELR, expected loss ratios than we've had in the past. So as those gain more scale, as we exit certain lines, such as our crop operation, which is better handled than (38:58) our reinsurance side, as we deemphasize a couple of other areas that had higher loss ratios, we expect that combination and mix to produce better performance that we've seen historically.

A - Dominic James Addesso {BIO 1428096 <GO>}

And I think in part, Kai, to answer that, a little bit of market disruption along with, as Jonathan pointed out, the significant capital base that's attractive to clients and brokers, but that market disruption again allowed us to get very capable people, but also as other competitors were reevaluating their strategies, that enabled us to grow certain segments faster than we might otherwise would've been able to do.

Q - Kai Pan {BIO 18669701 <GO>}

And do you see yourself can get down to the mid-90's combined ratio next couple of years?

A - Dominic James Addesso {BIO 1428096 <GO>}

Well, one interesting point that we shouldn't gloss over is that the first quarter, while none of the events – the weather events, catastrophes if you will, PCI events that Jonathan referenced, while none of them reached our threshold for declaring them to be cats, nonetheless, we had $15 million of weather losses in the first quarter of the insurance operation, which amounts to 4.5 points in the combined ratio for the insurance results. So as you can see, we're pretty much already where you're referencing.

Q - Kai Pan {BIO 18669701 <GO>}

Okay, that's great. My second question is on the reinsurance side. So, I just wonder, is there any seasonality, because now you have the crop reinsurance in the U.S. reinsurance book. That would impact your kind of second quarter and third quarter year-over-year comparison in terms of the core combined ratio?

A - John P. Doucette {BIO 7178336 <GO>}

Hi, Kai, it's John. There isn't that much seasonality. And crop, while it's a new piece given the move from the insurance to the reinsurance, in the grand scheme of things it's relatively small across the overall global portfolio for the reinsurance operations. So I would say, no, there's not really much seasonality.

Q - Kai Pan {BIO 18669701 <GO>}

So the fourth quarter and the first quarter results should be a good indication for the coming two quarters?

A - Dominic James Addesso {BIO 1428096 <GO>}

You're talking in terms of loss ratio?

Q - Kai Pan {BIO 18669701 <GO>}

Yeah, just with the overall the core combined ratio – attritional combined ratio, because there're probably different mix between loss and like commission expenses?

A - Dominic James Addesso {BIO 1428096 <GO>}

Yeah, that doesn't move around all that much, because from quarter-to-quarter based on our pegged loss ratios. Obviously, when we get to the fourth quarter we have our reserves review which could impact the attritional in that quarter. I don't know that you'd refer to that as a seasonality, but our earned premium is earned ratably through the year, and we book a consistent estimated loss ratio absent any zeitgeist (41:48) type of events.

Q - Kai Pan {BIO 18669701 <GO>}

Great. Just quick number clarification, there it's $30 million Ogden rate impact, is that including in this quarter reserve development or in the fourth quarter one? You said year-end [Technical Difficulty] (42:03) reserve study?

A - Dominic James Addesso {BIO 1428096 <GO>}

What I was referencing was that the impact of Ogden in terms of a dollar amount wasn't made known of course until the first quarter. But what I was referencing was that we consider that to be a prior-year event which was more than covered in our year-end reserve review. While not specifically of course an item in the year-end reserve review, just like many other discrete events that occur many quarters or years later frankly when you look at reserves (42:38) is that our reserve review contemplates the fact that things can go wrong, things can happen, but you cannot specifically identify what they might be.

So, our reserve review has a certain amount of conservatism built into it or what I would describe as a fact that the point of the reserve review as an unknown event and the Ogden situation it was a prior year event for us and well within the balance of being covered in our year-end reserve review contemplations.

Q - Kai Pan {BIO 18669701 <GO>}

Great. Well, thank you so much for all the answers.

A - Dominic James Addesso {BIO 1428096 <GO>}

Thank you, Kai.

Operator

We will take our next question from Sarah DeWitt with JPMorgan.

Q - Sarah E. DeWitt {BIO 18946247 <GO>}

Hi, good morning. In the reinsurance segment, I was surprised with the underlying combined ratio improved year-over-year and what's still a competitive market. Can you talk about how you're achieving this and how sustainable is that going forward?

A - Dominic James Addesso {BIO 1428096 <GO>}

The simple answer, Sarah, is just the changing mix. So as for example as mortgage and other credit related opportunities as that premium begins to flow into the books that carriers a lower loss ratio, combined ratio than which you would think about as the more traditional lines. That's frankly the simplest example or explanation. We will also have a little less quota share coming into the reinsurance book, which also helps maintain that ratio.

Q - Sarah E. DeWitt {BIO 18946247 <GO>}

Okay, great. And then just a couple of numbers questions, how much did the crop reinsurance transaction contribute to the top line, and then how much is your mortgage and credit business?

A - Dominic James Addesso {BIO 1428096 <GO>}

Crop was about $50 million.

A - John P. Doucette {BIO 7178336 <GO>}

Yeah.

A - Craig W. Howie {BIO 17579923 <GO>}

$53 million

A - Dominic James Addesso {BIO 1428096 <GO>}

$53 million in the first quarter.

Q - Sarah E. DeWitt {BIO 18946247 <GO>}

Okay. And how big is the mortgage and credit business?

A - Dominic James Addesso {BIO 1428096 <GO>}

And the total mortgage gross written premium in...

A - Craig W. Howie {BIO 17579923 <GO>}

It's about $150 million to $200 million.

Q - Sarah E. DeWitt {BIO 18946247 <GO>}

Annually or in the quarter?

A - Craig W. Howie {BIO 17579923 <GO>}

Sorry, could you say that again?

Q - Sarah E. DeWitt {BIO 18946247 <GO>}

That's an annual number or in the quarter?

A - Craig W. Howie {BIO 17579923 <GO>}

Yeah, that's annual.

Q - Sarah E. DeWitt {BIO 18946247 <GO>}

Okay, great thank you.

Operator

We'll take our next question from Jay Gelb with Barclays.

Q - Jay Gelb {BIO 21247396 <GO>}

Thanks and good morning. My first question is on the outlook for the, the mid-year Florida renewals, where I believe you said hoping for flat rates. I think it's pretty well understood that citizens insurance capacities can be down midyear in terms of demand for reinsurance protection, but I just wanted understand if I heard you correctly, are you saying demand from other primary writers of Florida is going to be enough to offset that?

A - Dominic James Addesso {BIO 1428096 <GO>}

Well citizens is down because the private market has assumed much of that exposure, so capacity will be soft from the private market.

Q - Jay Gelb {BIO 21247396 <GO>}

Okay, is there any influence, do you think midyear as a result of Matthew?

A - Dominic James Addesso {BIO 1428096 <GO>}

We hope, we think that there could be some influence, but that all depends on how much capital has been go (46:16) into the market. So look, based on the returns that the industry is producing on overall capital. We do you think it, it suggest that that rates should be in flat, but there's no way for us to know what that might be right now.

Q - Jay Gelb {BIO 21247396 <GO>}

Right.

A - John P. Doucette {BIO 7178336 <GO>}

This is John. There's also other contributing factors with the AOB issue that's out there and that impacted people in 2016 including their capital position.

Q - Jay Gelb {BIO 21247396 <GO>}

What's that John.

A - John P. Doucette {BIO 7178336 <GO>}

The assignment of benefits. So the assignment of benefits issue that happened in – that has been happening that has resulted in an increase in the attritional loss ratio for many of the Florida citizens. And so some of them had to go get more capital or in the process of getting more capital or raising more capital and as you know reinsurance is the form of capital.

And so a lot of them are potentially looking to increase their buys whether it comes – whether that's on a quota share or on an excess loss basis, as well as some of the larger Florida citizens have also been diversifying outside the state, so as they've been growing, they have had natural exposure growth for their overall books of business, their reinsurance demands to protect that book have also been increasing, and we would see that to directionally to continue.

Q - Jay Gelb {BIO 21247396 <GO>}

That's helpful, thanks very much. And then my separate question, Dom, in this year's annual shareholder letter, you talked about the decision to build in the insurance segment as opposed to buy and I'm kind of glad you brought that up in the letter, hopefully it's pretty good jumping off point just to touch on it in a bit more detail.

A - Dominic James Addesso {BIO 1428096 <GO>}

That was specific question there, I mean...

Q - Jay Gelb {BIO 21247396 <GO>}

Yeah, just in terms of – in terms of that decision, kind of where you see the insurance segment going forward?

A - Dominic James Addesso {BIO 1428096 <GO>}

Well, we have had this view for long time, and it's not because we haven't considered opportunities that are out there. And our view has been based on the fact that integration – since we had an existing operation as contrasted (48:42) with not having one at all, we felt it was easier for us to grow our existing franchise.

In the phase of acquisitions are tough, because integration issues are challenged, in addition, you're not quite sure talent that you're getting, the legacy issues that you might be attaining, there is a whole different face to the market in terms of how a particular company might be presenting itself to the distribution partners, they will have any ability to kind of build our message, our culture, our products, our appetite, all those things from the ground up was more attractive to us.

And then, of course, coupled with many of these acquisitions as you know are occurring at tremendous multiples creating a lot of goodwill, but that set aside we are potentially buying business that have mid single-digit ROEs, that's not – and I'm paying a premium for that. That's not all that attractive. And what we think we have done here in short years has been to of course dealing with the legacy issues that we've had, but we think the current enforce portfolio as I mentioned before. Absent the weather losses as already that we had in the first quarter is already in the low to mid single 90s combined ratio, so I think our strategy there is proving to be so far a good one.

Q - Jay Gelb {BIO 21247396 <GO>}

And a final one, if I can, the reinsurance performance in the first quarter was incredibly strong especially taking into account that it was a worst first quarter for catastrophe losses in the U.S. in over 20 years, is that – can you talk a little about whether that's risk management program structure primary companies just retaining more exposure, how come we didn't see more that impact on Everest results on the reinsurance side?

A - Dominic James Addesso {BIO 1428096 <GO>}

That wasn't one event right, it was many events which for the most part has fallen on within company retentions. Along with the fact that as we've mentioned each quarter – for many quarters now we keep – we tend to keep moving up our attachment point, because the most competitive part of the market has been down low and so – and we've been spreading our aggregate. So we've been diversifying our cat portfolio slightly moving up an attachment point coupled with the fact that many seasons (51:36) as their capital bases grow continue to retain more, so it's all of those things, it's not any one of them, but it's all of those things come into play.

Q - Jay Gelb {BIO 21247396 <GO>}

Thank you again.

A - Dominic James Addesso {BIO 1428096 <GO>}

Thank you, Jay.

Operator

We'll go next to Josh Shanker with Deutsche Bank.

Q - Joshua D. Shanker {BIO 5292022 <GO>}

Yeah, thank you. Can I start with mortgage reinsurance for a second? I want to know how you think about catastrophe risk versus mortgage reinsurance risk, is it similar and what Everest Re's modeling in terms of its exposure to a mortgage catastrophe. And two, how much business is there to be written out there, what's going to cause mortgage insurers want to see that risk in the future?

A - John P. Doucette {BIO 7178336 <GO>}

Good morning, Josh. It's John. So, couple of things, so we have been as we've talked about on the last several calls, focused on the mortgage opportunity within a broader credit play that we're doing, but mortgage is a meaningful part of that. And we do see – so we have focused on that both in the underwriting side, but also and arguably more importantly building out underwriting capabilities, analytical capabilities, ERM risk and very technical capabilities for us to be able to think about that really to get it – to bring it up to the level of, which it has, we have done to the level of how have been moved to best-in-class over the last several years in the property side.

So, in terms of how we think about to model it, we look at it from at the macro-macro level and how it overlaps in intersection correlates with our asset portfolio. We think about it on an overall economic capital model to the group. If we look at it on a realistic disaster scenario. We look at it as total limits that we deploy. We think about across years the correlation and the aggregation that can happen and really try to focus on what the economic situation is today and where we think it will be in the future so to determine how we want to play, where, what attachment points we want to play at, how that would impact if something like the financial crisis of 2008 happened again, how our book would perform.

Q - Joshua D. Shanker {BIO 5292022 <GO>}

So, along those lines, is it normal to think that sometime in next decade, there will be a mortgage cat event? And is there a way to have that occur and avoid the loss via underwriting?

A - John P. Doucette {BIO 7178336 <GO>}

Well, we have no idea if a loss is going to happen just like we don't know if catastrophe loss is going to happen. We...

Q - Joshua D. Shanker {BIO 5292022 <GO>}

I can promise you catastrophe loss will happen in the next 10 years. I'm certain of that.

A - John P. Doucette {BIO 7178336 <GO>}

All right, I'm going to write that down. So - but we - we're going to build a book and have an underwriting strategy that we think will succeed based on underwriting conditions, macroeconomic conditions, pricing conditions, and we're going to adjust the book. And that's our job. That's Dom and mine and the rest of the team's job to do that to react and how we think the book will best move going forward. But we do - we certainly manage to idea that a loss could happen and try to think of limits deployed and capital required in that context.

A - Dominic James Addesso {BIO 1428096 <GO>}

And it's also - keep in mind that it's - we tend to agree with you that you have to consider the fact that a loss can happen, but it's also where you attach, how diversified you are. There is many factors which go into what the level of loss might be. And from a realistic disaster scenario perspective, the exposure that we have to the mortgage space is relative to property cat risk is much less and of course relative to our capital, it's pretty small.

Q - Joshua D. Shanker {BIO 5292022 <GO>}

And then I guess one more, can we expect that if you've done your homework correctly, a well run mortgage rebook should outperform primary mortgage book?

A - John P. Doucette {BIO 7178336 <GO>}

I think the strengths - advantages and disadvantages of both are clearly from a - we have decided to make a reinsurance bet on it. And that gives us the benefit of hard dollar limits, that gives us the benefit of retentions, that gives us the benefit of having a compared to running an insurance operation far less resources, both capital and people wise. So, it gives us more ability to navigate the underwriting market, the market cycle that could happen. So we feel like - we feel pretty good about how we're deploying capacity and capital and our underwriting strategy and will be able to hopefully expand it if the market – the pricing and the market conditions allow, but also be in a position to dial it back if we don't think we're getting paid a good risk adjusted return.

Q - Joshua D. Shanker {BIO 5292022 <GO>}

And then quickly for Jon Zaffino, I want to know how he thinks about one, three, five year plan? When you started like at the beginning of 2015, did you have a three year plan? Do you have a five year plan? Wouldn't you sort of as the check points to note that the insurance business is performing in line with sort of the predicted plan on how to get this be important part of Everest Re?

A - Jonathan M. Zaffino {BIO 16652236 <GO>}

Sure, Josh. Yeah, we have very much phased out a deliberate roadmap that aligns with what Dom mentioned before about an organic growth plan. What does that look like? What are the key milestones along that journey and how do we get there? So, certainly for us there was a few prominent themes in that process. Number one was sort of foundationally preparing the organization for that journey which is an ongoing everyday type of exercise. Certainly looking to enhance our market relevance in the form of people and products and distribution connectivity has also been very much a part of that. And then certainly along the path we are going to make portfolio selections along the way.

A lot of that work has been at the forefront of our activity in the last several quarters if not year and a half or so. But remember, we're still adding talent as we go here to make sure that we continue to keep up with our growth and aspiration. So that's an ongoing work. So I would say that we're very much on track. We're going to follow market opportunity where it presents itself. We don't have a sort of hard dollar specific target in mind other than we certainly see a lot of growth opportunity that we want to pursue in our chosen markets. But certainly looking to foundation and prepare, refine our operations, add the talent, increase the relevance. There is a lot of work going on day-to-day which is the tactical activity that drives success on the insurance side that we're working hard at across the board.

Q - Joshua D. Shanker {BIO 5292022 <GO>}

Well, thank you for all the answers and I appreciate the extra time.

A - Dominic James Addesso {BIO 1428096 <GO>}

Thank you, Josh.

Operator

We'll go next Brian Meredith with UBS.

Q - Brian Meredith {BIO 3108204 <GO>}

Yes, thanks. Just a couple of quick questions here. First, I'm just curious in the Bermuda segment, what was the kind of dollar figure of the true-up which you had in the first quarter, just so we get a good sense of kind of what the year-over-year growth really is looking like without these true-ups, the Bermuda segment?

A - Dominic James Addesso {BIO 1428096 <GO>}

Just one second.

Q - Brian Meredith {BIO 3108204 <GO>}

Sure.

A - Dominic James Addesso {BIO 1428096 <GO>}

Yeah, it's roughly about $60 million.

Q - Brian Meredith {BIO 3108204 <GO>}

Great, that's truly helpful. And then, second question on the credit mortgage business, I'm just curious when you think about the capital allocation to that business, how do you think about it? Are you using call it rating agency models? What are you using in – and what is the risk here that perhaps as a change in way the rating agency look at the mortgage reinsurance business to get to maybe some type of capital requirements closer to PMIERs particularly with quota share, would that change your kind of view of the business?

A - John P. Doucette {BIO 7178336 <GO>}

So, Brian, it's John. I think a couple of things. I think we feel like just overall first principle that Everest given our overall capital position and diversified book business, we feel we're pretty capital efficient deploying capital in the areas like mortgage. We also know there has been conversations and some of the rating agencies have been looking at this fairly carefully about what the rating, how they should think about the capital required to support this book going forward.

More times than not when more capital is required whether it's on the PMIERs or the rating agencies that puts pressure on supply. And we view that given our strong capital position and balance sheet and ratings, we view that as positive that'll drive increases in demand and put downward pressure on supply. So, in terms of how we think about it? We think about it all of the above, rating agencies with limits deployed, realistic disaster scenarios, stochastic, pricing, reserving, looking at an overall economic capital model, thinking about the assets and the liabilities and whole balance sheet.

Q - Brian Meredith {BIO 3108204 <GO>}

Got you, great. And then another just quick question here. Given that you're moving to more call it shorter tail type businesses at least on the liability side with MI (1:02:03) and crop and stuff, is that causing any changes in your investment portfolio and kind of where you're going to invest proceeds?

A - Dominic James Addesso {BIO 1428096 <GO>}

No, it hasn't. The duration on the liability side really hasn't moved much (1:02:18) approximately three years - four years, and our asset portfolio was underneath that...

Q - Brian Meredith {BIO 3108204 <GO>}

Okay.

A - Dominic James Addesso {BIO 1428096 <GO>}

...so that has not changed significantly.

Q - Brian Meredith {BIO 3108204 <GO>}

Great, great. Thanks. And last quick question here. Workers' comp market, I know you guys did mention that there is some dislocation at the insurance market in general when you're taking advantage of opportunities there. How about the workers' comp market with some of the recent activity that we've seen there, any opportunities there?

A - Dominic James Addesso {BIO 1428096 <GO>}

In the insurance side?

Q - Brian Meredith {BIO 3108204 <GO>}

Yeah, insurance side, sorry, yeah.

A - Dominic James Addesso {BIO 1428096 <GO>}

There are a lot of select opportunities. And we have expanded slightly some of our offerings meaning expanded into some different states, but only selectively into certain states. California you know which is our biggest comp market, very profitable for us, rates are off a little bit, but we're still very bullish on the sector given where rates are. And we will use comp frankly as a competitive advantage. There is a lot of markets we compete against that don't have the comp capability and that gives us an edge to get into some other - some of the other lines of business. So that's how we're thinking about it.

Q - Brian Meredith {BIO 3108204 <GO>}

Got you. Thank you.

Operator

We'll take our final question today from Nicholas Mezick with KBW.

Q - Nicholas Mezick {BIO 20223149 <GO>}

Hi, good morning everyone.

A - Dominic James Addesso {BIO 1428096 <GO>}

Good morning.

A - Craig W. Howie {BIO 17579923 <GO>}

Good morning.

Q - Nicholas Mezick {BIO 20223149 <GO>}

Thanks for fitting me in. A year ago, you mentioned that you're not done hiring in the insurance division. And in the prepared remarks today, you mentioned due to market turmoil, you've accelerated those investments. Ex-Heartland, I see other underwriting expenses up about $9 million quarter-over-quarter. Where do you see the notional dollar amount is going in 2017 and 2018 or the other underwriting expense?

A - Dominic James Addesso {BIO 1428096 <GO>}

I don't know that we have an answer for you on that because it's all dependent on market opportunity. So we think about it more as an operating expense ratio. And I think where we're at today, we're lower, particularly as the earned premium begins to catch up, because our rate of add (1:04:44) for resources is not necessarily plateauing but not going up at the same pace that it has been over the last 18 months as we've been building up some of these new businesses. And as these businesses have – the premium begins to earn in, the expense ratio all other things being equal, should moderate. And as Jonathan pointed out earlier, we will continue to make additions consistent with what we see as the growth opportunity. So it's a little difficult for us to give you nominal dollar amount because that will emerge as opportunity emerges.

Q - Nicholas Mezick {BIO 20223149 <GO>}

Okay. And one of the governors to that is the sort of sub 30 expense ratio target?

A - Dominic James Addesso {BIO 1428096 <GO>}

Right.

Q - Nicholas Mezick {BIO 20223149 <GO>}

Okay. Thanks.

A - Dominic James Addesso {BIO 1428096 <GO>}

And by the way, if it remained at 30 for foreseeable future, again as we pointed out before, most of our competitors aren't even close to us there. So, while everyone seems to be focused on the increase in expenses, reality is, is that where we are at today is competitive relative to the market.

Q - Nicholas Mezick {BIO 20223149 <GO>}

Just a quick follow-up on that last point, any overrides from the more conservative reinsurance program?

A - Dominic James Addesso {BIO 1428096 <GO>}

We have overrides in our reinsurance purchases, is that what you are asking?

Q - Nicholas Mezick {BIO 20223149 <GO>}

Yes, that's sort of driving the expense ratio to that sub 30 target?

A - Dominic James Addesso {BIO 1428096 <GO>}

Not to any significant degree. We do have some overrides but that's not driving.

Q - Nicholas Mezick {BIO 20223149 <GO>}

Okay. Thanks, guys.

A - Dominic James Addesso {BIO 1428096 <GO>}

Thank you.

Operator

This concludes our question-and-answer session. I'll turn it back to management for closing remarks.

A - Dominic James Addesso {BIO 1428096 <GO>}

Well, I'll conclude by just thanking everyone for participating this morning. And as you can surmise from our prepared comments as well as some of the answers to questions, we remain optimistic about our ability to deliver – continue to deliver solid returns. Conservative management of our cat exposure, solid reserve position along with expense discipline and all of that positions us to withstand what the market might bring to us. Coupled with growth into newer product areas and our reinsurance operations as well as what's proving to be a successful growth strategy for our insurance division, these things should continue to help us maintain our above average returns.

So, thank you for your interest, and I look forward to perhaps meeting with many of you in the months ahead. Thanks again for participating.

Operator

Ladies and gentlemen, thank you for your participation. This does include today's conference. You may now disconnect.