Q1 2021 Earnings Call

Company Participants

- Jeremy A. Noble, Senior Vice President and Chief Financial Officer
- Richard R. Whitt, III, Co-Chief Executive Officer
- Thomas S. Gayner, Co-Chief Executive Officer

Other Participants

- Jeffrey Schmitt, Analyst
- John Fox, Analyst
- Mark Dwelle, Analyst
- Mark Hughes, Analyst
- Philip Stefano, Analyst

Presentation

Operator

Good morning, and welcome to the Markel Corporation First Quarter 2021 Conference Call. All participants will be in listen-only mode. (Operator Instructions) After today's presentation, there will be an opportunity to ask questions. (Operator Instructions)

During the call today, we may make forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. They are based on current assumptions and opinions concerning a variety of known and unknown risks. Actual results may differ materially from those contained in or suggested by such forward-looking statements. Additional information about factors that could cause actual results to differ materially from those projected in the forward-looking statements is included under the captions Risk Factors and Safe Harbor and Cautionary Statements in our most recent Annual Report on Form 10-K and Quarterly Report on Form 10-Q.

We may also discuss certain non-GAAP financial measures in the call today. You can find the most directly comparable GAAP measures and a reconciliation to GAAP for these measures in our most recent Form 10-Q, which can be found on our website at www.markel.com in the Investor Relations section.

Please note, this event is being recorded.

I would now like to turn the conference over to Tom Gayner, Co-Chief Executive Officer. Please go ahead.

Thomas S. Gayner {BIO 1896932 <GO>}

Thank you so much. Good morning, and welcome to the Markel Corporation first quarter conference call. This is indeed Tom Gayner, and I'm joined today by my Co-CEO, Richie Whitt; and our CFO, Jeremy Noble.

The purpose of today's call is to give you a brief update on our business and answer any questions you might have about Markel.

Well, what a difference a year makes. In my opinion, the first quarter of last year ranked as the toughest 90 days in the history of the Markel Corporation. It felt more like 90 years than 90 days. This year's first quarter report is better, a lot better. A year ago, despite the very real tangible and intangible costs from the shock of COVID-19, we pressed on, we persisted. The people of Markel demonstrated their resilience, skills and adaptability, and they produced significant rebounds in every aspect of our business as the year went on.

Today, we're pleased to report to you another milestone of progress. Each of our three engines of Insurance, Investments and Markel Ventures produced positive results in the first quarter, and we're optimistic about their prospects.

We know we've got more work to do. There is always more work to do. We're excited to be able to report to you results from our Insurance operations that are in line with our stated goals of growth and profitability that we outlined in our 1051 [ph] initiative. We're pleased with the improved profitability and risk reductions in our reinsurance business. We're earning appropriate and disciplined returns from our Investments. Markel Ventures continues to earn excellent returns, which increases the durability and value of the Markel Corporation and we're optimistic that we'll achieve meaningfully better results in our Insurance Linked Securities operations.

Jeremy will review the headline numbers from the quarter and then Richie will cover the Insurance, ILS and State National operations, I'll come back to chat about Investments in Markel Ventures, and then we will open the floor for questions. With that, Jeremy?

Jeremy A. Noble {BIO 20687803 <GO>}

Thank you, Tom; and good morning, everyone. As Tom said, what a difference a year makes. Our first quarter 2021 results showcased the benefits that come from operating our diverse three engine model with our Insurance, Investments and Ventures operations each performing well and adding value in the quarter.

Looking at our operating (technical difficulty) results, gross written premiums were $2.2 billion for the first quarter of 2021 compared to $1.9 billion in 2020, an increase of 13%. This increase was largely attributable to our Insurance segment, which reported gross written premiums of $1.6 billion, an increase of 16% compared to the same period of 2020. Our increased premium volume reflects both strong growth in new business as well as ongoing favorable pricing trends, both of which are most prominent within our professional liability and general liability product lines, but also experienced within our personal lines and marine and energy product lines.

Within our Reinsurance segment, gross written premiums increased 4% to $533 million, also reflecting growth in our general liability and professional liability product lines, partially offset by lower premium volume on our property product lines given our decision to transfer this portfolio to Nephila late last year. Retention of gross written premiums was 87% in 2021, which is up 2 points from the same period last year, primarily driven by changes in the mix of business within our Reinsurance segment. Earned premiums increased 13% to $1.5 billion in the first quarter of 2021 versus the same period last year, primarily due to higher written premium volume in our Insurance segment.

Our consolidated combined ratio for the first quarter of 2021 was a 94%, which included $64 million or 4 points of losses attributable to winter storm Uri and $19 million or 1 point of adverse development arising from a change in our estimates of the COVID-19 ultimate losses. This compares to a 118% combined ratio for the same period last year, which included 24 points of losses attributed to COVID-19. Excluding the loss impacts of the winter storm Uri and COVID-19 in both years, our consolidated combined ratio for the first quarter of 2021 was an 88% compared to a 94% in the same period in 2020. This improvement reflects a 4 point improvement in our attritional loss ratio and a 2 point improvement in our expense ratio.

With regards to prior year loss reserve development, prior year loss reserves developed favorably by $91 million in the first quarter of 2021 compared to $104 million in the first quarter of 2020. Favorable development of prior last year loss reserves in the first quarter of 2021 was net of the $19 million of adverse development related to COVID-19 that I just mentioned. All of which was within our Reinsurance segment on our property product line arising from updated in new loss information from cedents.

Turning to our Investment results. Net investment gains included in net income were $527 million in the first quarter of 2021 and were primarily attributable to an increase in the fair value of our equity portfolio driven by favorable market value movements. This compares to net investment losses of $1.7 billion in the first quarter of 2020, attributable to a decrease in the fair value of our equity portfolio driven by unfavorable market value movements resulting from the onset of the pandemic.

As I've mentioned in prior calls, given our long-term focus, variability in the timing of investment gains and losses is to be expected. We may continue to see volatility in the equity markets.

With regards to net investment income, we've reported $97 million in the first quarter of 2021 compared to $88 million in the same period last year. The increase this quarter reflects the impact of losses recognized on equity method investments in the first quarter of last year, partially offset by lower short-term investment income due to lower short-term interest rates during the first quarter of 2021 compared to the first quarter of 2020.

Net unrealized investment gains decreased $214 million net of taxes during the first quarter of 2021, reflecting a decline in the fair value of our fixed maturity portfolio resulting from increases in interest rates during the first quarter of 2021.

Now, I'll cover the results of our Markel Ventures segment. Revenues from Markel Ventures increased $707 million in the first quarter of 2021 compared to $511 million for the comparable quarter last year. This increase reflects the contributions of revenues from our April 2020 acquisition of Lansing Building Products. Excluding the contributions of Lansing in the first quarter of 2021, operating revenues in our Markel Ventures operations decreased compared to 2020 as a result of lower sales volumes, primarily in our transportation related and consulting services businesses.

EBITDA from Markel Ventures was $81 million in the first quarter of 2021 compared to $67 million during the same period last year. The year-over-year increase is attributed to a gain recognized in connection with the sale of a portion of one of our healthcare businesses. EBITDA from our other Markel Ventures operations decreased due to the impact of lower operating revenues at our transportation related and consulting services businesses in this quarter compared to the first quarter of 2020.

Looking at our consolidated results for the quarter, our effective tax rate for the first quarter of 2021 was 20% compared to 21% in the first quarter a year ago. We've reported net income to common shareholders of $574 million for the first quarter of this year compared to a net loss to common shareholders of $1.4 billion in the same period a year ago. Comprehensive income to shareholders in the first quarter this year was $359 million compared to a comprehensive loss to shareholders of $1.4 billion for the first quarter a year ago.

Finally, I'll make a few comments on cash flows, capital and our balance sheet. Net cash provided by operating activities was $318 million for the first quarter of 2021 compared to $66 million for the first quarter last year. Operating cash flows in the first quarter of 2021 refer to the impact of higher premium volume as we continue to see strong growth in our Insurance segment. Invested assets at the holding company were $4 billion at the end of March compared to $4.1 billion at the end of the year.

Total shareholders' equity stood at $13.2 billion at the end of March, up from $12.8 billion at the end of the year. During the quarter, we've repurchased just under 20,000 shares of our stock under our outstanding share repurchase program.

Overall, a very pleasing quarter from both the top and bottom line within each of our three engines. Financial condition of the company remains strong and we are well positioned to take advantage of opportunities in the marketplace.

And, with that, I'll turn it over to Richie to talk more about our Insurance businesses.

Richard R. Whitt {BIO 7084125 <GO>}

Thank you, Jeremy; and good morning, everyone. A strong momentum from the last half of 2020 continued in the first quarter of '21 as we achieved a combined ratio of 94%, which includes 4 points of cat losses from winter storm Uri and 1 point of loss is attributable to adverse development related to COVID-19. Obviously, compared to the unprecedented impacts of COVID-19 on our operations and results in the first quarter of 2020, we are pleased to be able to report a solid start to the year.

There is one golf saying that you can't win the tournament on the first day, but you certainly can lose it. Despite starting the year with a slightly higher combined ratio due to the unprecedented winter storms, we believe we are still well positioned to win the tournament and achieve our previously stated underwriting profitability goals for the full year. Sure, I absolutely would have loved to start the year on the right side of 90% combined, but I feel like we're in a striking distance.

Many of the tailwinds we've discussed on our last call remain in play with our ability to achieve meaningful rate increases across almost all Insurance and Reinsurance product lines, resulting in reductions in our first quarter 2021 attritional loss ratios. We continue to find areas to add new business and program opportunities and take full advantage of the current market environment, while also engaging in continuous portfolio management aimed at improving profitability and reducing overall volatility.

Now, I'll discuss our Insurance operations, which include our underwriting operations, State National program services operations and Insurance Linked Securities' operations.

So let's get started with the Insurance segment. Gross written premiums for the quarter in our Insurance segment were up $224 million or 16% and earned premiums were up $137 million or 12% compared to 2020. Premium growth was driven by continued strong new business growth along with the impact from rate increases across several product lines, most notably our professional liability, general liability, marine and energy, and personal lines' products. Virtually all of our growth continues to be in our preferred product offerings. We continue to see favorable rating environments within several of our product lines with the exception of workers' compensation. And we look to continue to take advantage of these market opportunities.

The combined ratio for the Insurance segment for the first quarter was 91% versus 119% in the same period last year. The 28 point combined ratio decrease was primarily driven by the impact of COVID-19 losses in 2020 compared to much smaller cat losses in 2021. We've recognized $39 million or 3 points of losses in the first quarter of '21 related to winter storm Uri versus $293 million or 27 points related to losses from COVID-19 last year.

Besides the impact from COVID and cat loss events within our ongoing operations, we also reported a 3 point reduction in our 2021 current accident year attritional loss ratio. This decrease was driven primarily by the impact of premium rate increases across several of the product lines I previously mentioned. In addition, we benefited from a 2 point reduction in our expense ratio due to the impact of higher earned premiums, efficiency efforts and expense control.

Turning to the Reinsurance segment, gross written premiums for the quarter were up $19 million or 4% and earned premiums were up $28 million or 12% compared to last year. Premium growth was driven by new business due to significant new treaties in our general liability and professional liability lines, where we see attractive opportunities.

As we've said in the past, individual contracts can have significant impacts on our premium writings. The growth that we saw in general liability and professional liability really related to three new contracts that we thought were good opportunities in the first quarter. This was partially offset by lower premiums in our property product line. As a reminder, during the first quarter of this year, we executed on our planned transition of our Reinsurance property lines from our Reinsurance underwriting operations to be managed by our Nephila ILS operations as part of our ongoing strategy to match risk to the most appropriate capital. We will continue to see impacts from the Reinsurance treaty transition throughout the remainder of the year within the results of our Reinsurance segment.

The combined ratio for the Reinsurance segment for the first quarter was -- of 2021 was 109% compared to 115% last year. The 2021 combined ratio was primarily driven by the impact of cat and COVID-19 losses where we've recognized $25 million or 10 points of losses related to winter storm Uri and $19 million or 7 points of adverse prior accident year development related to COVID-19. The 2020 combined ratio included $32 million or 14 points related to losses from COVID-19.

In addition, the 2021 combined ratio was favorably impacted by a decrease in our current accident year, attritional loss ratio primarily within our product -- property product lines and from a lower expense ratio due to the impact of higher earned premiums.

While our Reinsurance segment results are still not where they need to be, we achieved significant growth in our more profitable general liability and professional liability product lines this quarter and saw favorable trends in both our current accident year attritional loss ratio and expense ratio compared to the same period a year ago. We are working hard to price all 2021 business to a 90% combined ratio or lower. The difference between the 2021 reported current accident year combined ratio and that the pricing target is a result of earnings on business written in previous years and our consistent application of Markel's reserving philosophy, which is to set reserves at all levels that are more likely redundant than deficient.

Next, I'll touch on our program services and ILS operations, both of which are reported as part of our other operations. Gross written premium volume for our State National program services operation increased by 56% to $612 million versus $393 million a year ago. Premium growth was due to the expansion of existing programs and the addition of new programs. Premium in the first quarter of 2020 were impacted by one-time unfavorable adjustment of $55 million related to the in-force cancellation of the particular program.

The overall increase in premiums under management also favorably impacted our operating revenues and margin in the quarter. As a reminder, almost all of the gross written premium within our program services operations is ceded. We continue to see a strong pipeline of program services opportunities in the current market.

Next, I'll discuss our ILS operations. Our ILS operations consist of the results of Nephila plus startup expenses related to Lodgepine. For the quarter, operating revenues within our ILS operations decreased due to lower investment management fees related to having lower assets under management versus the same period a year ago. Assets under management at Nephila were $9.5 billion as of March 31, 2021. Earnings also continued to be impacted by cost associated with building and supporting the growth of Nephila's two MGA platforms as well as preparing for the launch of additional fund investment vehicles. Nephila continues to build and identify new areas of opportunity to deploy capital and launch new investment opportunities.

Finally, I'd like to point out that we made a change in our disclosures this quarter to recognize the runoff nature of the CATCo operations by moving those results out of the ILS operating revenues and expenses and into other for all periods presented. CATCo continues to make solid progress to the orderly winddown of its operations and currently have approximately $900 million in AUM.

I'll finish up with some market commentary. Trends in the first quarter were very similar to trends we discussed on our last call. We see continued pricing momentum in almost all lines. The glaring exception, I guess, is workers' comp. Our Insurance and Reinsurance rate increases averaged over -- averaged double digits in the first quarter. Reinsurance pricing, which as we've previously discussed, has lagged primary Insurance pricing closed the gap some more during the first quarter during the January 1 renewals. But it's still not as strong as rates being achieved in the primary market. This continuing dynamic obviously explains our continued double-digit growth in Insurance versus roughly flat in Reinsurance.

As we've discussed, while new entrants and incremental capital raise is certainly have impacted the market around the edges, we believe that this pricing momentum will continue due to a multitude of factors such as low interest rates, the continued elevated cat activity, social inflation, further COVID-19 impacts and economic uncertainties that are likely to persist throughout 2021.

We do note that there seems to be much discussion recently of a moderation of rate increases. While it certainly does appear to us that rates are not going up at the same pace that they have over the last several quarters, we really do not view this as a cause for alarm. We are in the third year of meaningful rate increases, which creates a compounding impact. It would be unrealistic to think that rates could continue to accelerate indefinitely. Also it's worth pointing out the dynamics of all lines are not the same, while D&O price increases are beginning to stabilize, cyber prices around the way up given recent loss events and as Insurance and Reinsurance capacity has decreased.

In our view, the overall market picture remains extremely healthy. We're also starting to see the benefit to our business as the economy recovers from the impacts of COVID-19. People probably obviously saw first quarter GDP increasing at 6.4%. Small businesses, which is a meaningful part of our portfolio is starting to show signs of recovery and it is showing up in our premium writings.

To sum up the first quarter, we're off to a solid start and are excited to continue to move our business steadily forward over the rest of the year. Thanks for your time today. And, now, I'll turn it over to Tom.

Thomas S. Gayner {BIO 1896932 <GO>}

Thank you, Richie. In our Ventures operations, the headline numbers show revenues of $707 million compared to $511 million a year ago and EBITDA of $81 million compared to $67 million. As is usually the case though, there is more going on than what spotlighted in headlines.

As to revenues, the biggest reason for the increase is the inclusion of Lansing. Typically the first quarter is seasonally the lightest for Lansing as well as several other of our businesses, and I would expect normal seasonal increases and profitability as the year progresses. As to the increase in EBITDA, we've recognized a gain from the sale of a facility within one of our healthcare operations. I would point out that transaction should give you some insight into the conservatism of the accounting in place at Markel Ventures. We've struggled a bit with our healthcare operations and the fact that we could sell a facility in an underperforming business and that that would yield a gain should give you some comfort that we're not raggy when it comes to how we're reporting our results to you.

For years, we've publicly stated and committed to conservatism in the presentation of our insurance results. We've operated with a goal of being more likely redundant than deficient when setting insurance reserves and I hope you take some comfort from that spirit and that spirit and culture of conservatism exist at Markel Ventures as well.

For the entirety of Markel Ventures, this year's first quarter was a COVID quarter to use a phrase, while our first quarter of last year was pre-COVID. We've had BC and AD has conventions to describe dates for a few millennia; for at least a little while longer, I think, we'll distinguish the current era as PC, DC and AC. Tom Hanks was the first person I heard breakup time into those categories and he is a firsthand veteran of the path. Personally, I'm looking forward to the AC period, but it's not here yet.

I continue to be grateful and amazed for the performance throughout the Markel Ventures organization. The results are excellent. They also require more work per unit of output compared to pre-COVID circumstances. Economic activity and order books are very good. There is plenty of business to be had and we're getting our fair share of it. Fulfilling orders and producing goods and services is getting harder. Our Ventures' CEOs use new words like supply chain roulette when describing the daily realities of their business. Labor shortages and inflation are facts of life. Your team is doing an outstanding job of scoping and adjusting with the realities on the ground, but what I see in real time from real businesses seems different than many news reports and comments from officials about inflation.

If current economic and financial markets conditions continue to prevail, we should enjoy record results in revenues and EBITDA this year from Markel Ventures. In the current pricing environment of very low interest rates and very high transaction price multiples, I do not expect us to make sizable acquisitions in 2021. We've got an excellent capital position, a lot of dry powder and a great network of CEOs and relationships that keep us connected to the opportunities. But I think we're better off focusing on our existing operations and organic growth opportunities at this time. We'll adjust as circumstances change and that ability to change is a fundamentally attractive feature of our overall structure at Markel.

On the Investment front, we are at 8% on our equity portfolio during the first quarter and our fixed income operations we posted a negative 1.3% return, which occurred entirely due to rises in interest rates. There were zero credit losses in the portfolio. The total portfolio after all expenses in foreign currency adjustments rose 1.4%.

In any one quarter and frankly in any one year, expect a lot of volatility from Investments. We make no efforts to dampen volatility artificially through expensive derivatives or the difference between publicly traded mark-to-market valuation practices versus private self-reported valuation marks. We just stick to the fundamental and basic task of trying to earn the best returns we can over long periods of time.

Currently, our capital position is quite strong. We have accumulated higher than normal cash positions. Fortunately, that cash supports our current growth in Insurance underwriting opportunities, which carry the expectations of meaningful returns. As time goes by and capital continues to build, we expect to be able to apply capital to all four components of our capital allocation triage ladder.

We're currently funding the organic growth of our Insurance businesses. We've got ample capital to fund growth initiatives within our Ventures operations. We're modestly adding to our publicly traded securities portfolio. We're open minded about potential acquisitions when opportunities arise. I'll add they always do eventually. And we are repurchasing our shares. We will continue to incur the small opportunity cost of carrying large cash balances until conditions change. We are not interested in locking in low long-term rates of return. We will continue to be opportunistic as we look at the Investment decisions.

To close, we are pleased with the progress we're reporting to you this morning. We've got demonstrated wonderful results in our Insurance business, improving results in our Reinsurance business, demonstrated wonderful results in our Markel Ventures operations, appropriate returns in our Investment portfolio, and gritted teeth determination to improve results in our Insurance Linked Securities operations. I love our culture and I like our hand.

With that, we welcome the opportunity to answer your questions.

Questions And Answers

Operator

We will now begin the question-and-answer session. (Operator Instructions) Our first question today comes from Jeff Schmitt with William Blair.

Q - Jeffrey Schmitt

Hi. Good morning. A question on the rate levels in the Insurance segment. I think in both Insurance and Reinsurance, you kind of referenced there is still the double-digit levels, but you're kind of seeing a stabilization there. How much of that, I guess, could you maybe speak to the environment? Are you seeing higher competitive levels at this point or is there maybe just sort of a pause in social inflation with the courts being closed, what do you see kind of driving that stabilization?

A - Richard R. Whitt {BIO 7084125 <GO>}

Hey, Jeff, it's Richie. I think it's a number of factors. I pointed out we're in the third year of rate increases. It gets harder to sell continued double-digit rate increases after you do that a couple of times, so I mean there is a point at which things have to level off. So I think that is part of it. We've been through a couple of renewal cycles and continued double-digit rate increases get harder and harder to sell. There is certainly competition, always is, and certainly as rates -- as people start to see rates go up and they have their opinion as to where those are versus rate adequacy. Obviously, the higher they go, the more people feel like, hey, that's a good risk and I should maybe jump in on it. So, I think, it's just the signs of a healthy market. I mean that is what's going to happen.

As I said, I mean, we really did not see -- I mean, we were pretty flat quite honestly in the first quarter looking at rate increases versus fourth quarter. I know some people talked about being down a bit. We were sort of flattish and that growth, maybe we'll see that growth dip below flat in the second quarter, but still double-digits in both Insurance and Reinsurance.

Q - Jeffrey Schmitt

Okay. And then in the Reinsurance segment, just looking at that underlying loss ratio down a fair amount, high-50s, I think it's 58%, historically mid-60s, and I think you referenced a lot of that is just a mix shift as you exit the property cat business. Is that the case? I mean, should we think of kind of high-50s being more of the run rate there versus mid-60s? I guess, the same with the expense ratio is down at 30%. I think that looks to be mix shift related, is that -- I'm just trying to think of the run rates in these items with that property cat business out?

A - Richard R. Whitt {BIO 7084125 <GO>}

Sure. Sure. Yeah. I think both of those are a little abnormal just as a result of what we're doing in terms of property and some of the -- yeah, just some of the other issues that happened in the quarter. I think the low-60s is probably about the right place in terms of an attritional loss ratio and maybe a tick higher on the expense ratio. We are pricing -- I did say this in my comments, the team is trying to price everything at a 90% or lower that they're putting on the books. But we're not going to see that show up in our results for a while.

And two reasons, we're still earning premium that was put on the books in prior years and maybe didn't have a stronger rate increases. And, secondly, just our conservatism. We want to be more likely redundant than deficient. We're coming off of few years of tough performance in Reinsurance. We're going to be from Missouri in terms of the results for a while. So while we're pricing it less than 90%, my goal would be something in the mid-90s in terms of what we can do this year.

Q - Jeffrey Schmitt

Right, okay. And then just one kind of broad comment. Just looking at the compound annual growth rate of book value, I think over the last five years to 9%, stock prices increased to about 5%, do you any general kind of thoughts or comments on that in? And, I mean, is there an opportunity there to maybe increase share buybacks at all to help the stock price?

A - Richard R. Whitt {BIO 7084125 <GO>}

Yes, there is, and we are doing that.

Q - Jeffrey Schmitt

Okay. Thanks for the answers.

A - Richard R. Whitt {BIO 7084125 <GO>}

Absolutely.

Operator

Our next question comes from Mark Hughes with Truist.

Q - Mark Hughes {BIO 1506147 <GO>}

Yeah. Thank you. Good morning. On the Reinsurance business, you've got the positive growth despite the trimming of your property exposure, I think you've mentioned three programs in particular, when we think about the balance of the year, are those programs going to continue to make a contribution? Are we looking at the positive topline for Reinsurance?

A - Richard R. Whitt {BIO 7084125 <GO>}

The rest of the year is going to -- we're going to have to see how it plays out. The issue in Reinsurance given our relatively small portfolio, roughly $1 billion is individual deals can really move the numbers around. And so, as I said, we did three deals and they add up to around $90 million. I mean, so your -- in Reinsurance individual deals can be elephant hunting. So we found three deals that we've really liked in the first quarter. I can't be certain we will find three deals in the second quarter or any deals in the third or fourth quarter. So we are going to be very opportunistic for the rest of the year and if we think there is good deals out there that we want to write, we'll put them on the books. But if not, we could be down quarter-to-quarter. So this year is all about profitability and being opportunistic. So it's going to be a little hard to give you guidance on how the next three quarters play out in terms of premium volume.

Q - Mark Hughes {BIO 1506147 <GO>}

Understood. On the retention within Reinsurance, it was up this quarter, I think you talked about mix, depending on what comes in the door, is the retention likely to stay more elevated?

A - Richard R. Whitt {BIO 7084125 <GO>}

Yes, it is. Our retentions on our property business were lower because of the cat protection that we bought, the Reinsurance protection that we bought. We tend to keep much more of our casualty, professional and specialty business net. So those retention should go up.

Q - Mark Hughes {BIO 1506147 <GO>}

And in Nephila, you talked about investments that you're making, assets were slightly down a little bit in the quarter, when do we start to see more forward progress with Nephila at the bottom line?

A - Richard R. Whitt {BIO 7084125 <GO>}

That's a great question. I can tell you we've been frustrated. We feel like we make two steps forward and then there is a step backwards. Uri in the first quarter and we have losses and that obviously reduces AUM, reduces fees. It's been a tough four years in the ILS business with the cats. But we can't make excuses. We have to figure out a way to get our business moving forward. So, certainly, we project the business moving forward the rest of the year and certainly wanted to move forward in '22 and onward, but we've got work to do and there is just no other way to say them. We've got work to do to get where we wanted to be in ILS and part of that is, hopefully, fewer cats, but the bigger part of it is getting the right price for the exposure. So I and a lot of other people believe prices need to continue to go up for cat risk.

Q - Mark Hughes {BIO 1506147 <GO>}

If I might ask one more question, Tom you mentioned inflation, I just wonder how you feel like the Ventures business is positioned for inflation? And what you might be doing in the equity portfolio? Are you resisting [ph] on the assumption that inflation will be worse than the broader market assumes?

A - Thomas S. Gayner {BIO 1896932 <GO>}

It would be my expectation that the actual inflation is really taking place on the ground. It's more than what the headlines would report. So all of the managers who live and eat and sleep and dream these businesses every day, they're doing the best they can to control their cost, get their supply chains on and then working and making sure that they're charging appropriate prices to earn a good margin of whatever product or service they're providing. That's true every day. That's true in the public securities portfolio of the companies we look at and we're really looking for the same kind of behavior from the managers of our businesses at Markel Ventures as we expect from the managers of the publicly traded companies that we're investing in and that really doesn't change whether inflation is low or high, but I don't want to be caught asleep in the wheel and not aware of the heightened sensitivity and focus that I think should be applied to that line of thought these days.

And just to sum it up, and I think I mentioned it in the comments, we think the dumbest thing you could do right now is to lock-in low long-term rates of return. So we aren't kind of geniuses or smartest people in the room, but we try not to be the dumbest. So as long as we don't do stupid things, good things compound.

Q - Mark Hughes {BIO 1506147 <GO>}

Thank you.

Operator

Our next question comes from John Fox with Fenimore Asset Management.

Q - John Fox {BIO 1796608 <GO>}

Yeah. Good morning, everyone. I have a number of questions. First for Richie on the COVID losses in Reinsurance. I'm just curious -- I mean, that's to be expected, it's obviously, as Tom said, still an ongoing situation, but I'm just curious on the logistics of that? Is that some loss that pops us, you get notified from one of your carriers that you're reinsuring and is that new information for them? And just -- could you just talk about the logistics of how that comes about?

A - Richard R. Whitt {BIO 7084125 <GO>}

Well, certainly, as a reinsurer, there is a bit of a delay in reporting and obviously COVID is a situation that's developing and indeed it's the first half people have really seen the situation. So it is taking a while for people to get their heads around how the losses might flow through the system. So, I mean, what we are seeing is notifications that -- and mostly what we're seeing is notifications that people may be sending losses to us. I think there are very few instances of actual hard, this is a loss that we're going to be putting to the tree. So the great majority of what we have up today at the Reinsurance operations is the IBNR and --

Q - John Fox {BIO 1796608 <GO>}

Okay.

A - Richard R. Whitt {BIO 7084125 <GO>}

My sense is, it's going to take quite a while for it all to play out, all the language has to be reviewed, there is probably going to be some negotiation between the cedings and the reinsurers. I wouldn't expect this to be resolved quickly and it's just prudent to hold the IBNR at this point.

Q - John Fox {BIO 1796608 <GO>}

Okay, great. Thank you. And then by my calculations, which may not be correct, but I've been looking at your accident year every quarter, which, at least by my quotes, has been running 105% plus for a lot of quarters historically. Now it's closer to a 100% or maybe even 98%, 99%, and I'd just like you to comment is that observation accurate? And if so, what's the reason for that? I'm assuming three years of good price increases probably helps, but if you could just comment on that. Thank you.

A - Richard R. Whitt {BIO 7084125 <GO>}

Yeah. I can't comment on your numbers, John, and maybe we can sync up later and get on the same page, we would actually say the current accident year combined ratio was lower than that. But the directions, the trends you're talking about is absolutely true. On the loss side, it is, as you said, three years of price increases and term improvements and then there is -- don't forget the expense ratio component. Over the last few years, it's probably approaching 3 points off the expense ratio. So --

Q - John Fox {BIO 1796608 <GO>}

Yes.

A - Richard R. Whitt {BIO 7084125 <GO>}

So your trend is absolutely correct. I can't confirm your numbers and we may be catch up later and try to get that sorted.

Q - John Fox {BIO 1796608 <GO>}

No, that's fine. The trend is correct, which is fine. And then I have to admit I'm struggling with Ventures with Page 35, the disclosure on the gain, so is the Ventures EBITDA $81 million minus $22 million, and that has also -- has come in other revenue or I didn't understand the -- it's included in services and other expenses?

A - Richard R. Whitt {BIO 7084125 <GO>}

Yeah. The gain would be at the EBITDA line. It would not be in the revenue line. It was just -- within the business, that was underperforming, we sold something and added $22 million gain on it.

Q - John Fox {BIO 1796608 <GO>}

Thank you.

A - Richard R. Whitt {BIO 7084125 <GO>}

So you might be confused, but I hope you're at least happy.

Q - John Fox {BIO 1796608 <GO>}

I'm happy with the results, I am confused on some of the disclosure.

A - Richard R. Whitt {BIO 7084125 <GO>}

The results are better.

Operator

Our next question comes from Mark Dwelle with RBC Capital Markets.

Q - Mark Dwelle {BIO 4211726 <GO>}

Yeah, good morning. Several of my questions have been covered, but on the reserve addition, was that related to -- most of the Reinsurance book was contingency related, was it primarily related to that -- the reserve addition?

A - Richard R. Whitt {BIO 7084125 <GO>}

Yeah. It is related to business interruption, where I'd tell you the language, there is a lot of different languages out there and there's going to be a lot of negotiation on what is actually covered and what is not, but it would be instances where cedings believe they have an element of coverage for business interruption through their property reinsurance. And as I said, at this point, it's mostly notifications that we may have a loss to it, but we're going to cede to you, very, very few hard and fast law -- actual laws notifications. And so the great majority of the reserve is IBNR and I do believe it's going to take quite a while for that all to be sorted out.

Q - Mark Dwelle {BIO 4211726 <GO>}

Was it the US cedent or is it non-US?

A - Richard R. Whitt {BIO 7084125 <GO>}

I don't know, Mark, whether it's US or international, it's probably some of both. I'm sure it is more than one just reviewing notifications that have come in.

Q - Mark Dwelle {BIO 4211726 <GO>}

Okay. Fair enough. Second question, you mentioned and it was also mentioned for the first time in a little while in the 10-Q about kind of the ramp-up of Lodgepine. I'll admit I kind of lost track of that thing, I think it was first established back in 2019 and maybe just an update of what's happening there and what you're hoping to accomplish in '21 with it?

A - Richard R. Whitt {BIO 7084125 <GO>}

Sure. Well, in terms of the underwriting side of Lodgepine, that got off the ground immediately and had a great year in 2020. So they were in the market, wrote business and from a retro standpoint, retro writers, I think, had a really good year in 2020. Most of the losses were contained in the Insurance -- with -- but retained by the insurance companies or made it into reinsurance, but not to retro. The difficulty has been, and I think we've talked about this just in terms of the ILS market in general, raising capital. It has been with COVID, with recent results in ILS, it has been a very long ramp-up to raise the capital. We feel like we are within a whisker of raising that capital and sort of launching the fund side of things, but it has taken considerably longer than we ever would have guessed.

Q - Mark Dwelle {BIO 4211726 <GO>}

Okay. That's helpful. And then the last question, mainly -- or actually two questions. One related to the insurance business, when you characterize the growth, I mean you talked about the rate increases, so I think you've covered that. Within the balance of the growth, is that more associated with exposure unit growth within your insureds or is it more associated with kind of new business wins or gaining policy count?

A - Richard R. Whitt {BIO 7084125 <GO>}

Yeah. And I don't have details right in front of me, right now, Mark, but if anything we have been trying to shorten limits in a number of areas in the hardening market. It just makes sense. Try to get paid more for less exposure, if possible. So I would say -- I believe, most of the growth that is out there besides rate increases is going to be new policy count. Because as I said in a number of areas where possible we're asking underwriters to be very judicious with the amount of limit they're willing to put out.

Q - Mark Dwelle {BIO 4211726 <GO>}

Okay. Helpful on that. And then the last question, maybe for Tom. I mean, you sounded particularly for your own conservative self relatively bullish about Markel Ventures for the upcoming year. And I guess the one question I wanted to maybe push back on just a little bit was, is it seem like as a group of businesses, they were relatively less pandemic affected in the first place during last year. So is the growth simply just a recovery in those lines -- in those underlying businesses that were impacted or is it a more broad general inflation of the economy that you feel like you're capitalizing on.

A - Thomas S. Gayner {BIO 1896932 <GO>}

Yeah. No, I think, first off, I want to say last year in the pandemic effect, this business just got warped [ph] by the pandemic and set aside whatever journal entries or accounting you want. The human dimension of what was involved in those businesses and the effects on the people that were running them, have been there, just never been anything like it. And I'll remind you that it's over 15,000 people mainly who work in factories, doing field service, distributed all around the country, those are the frontline workers, they never missed a day of work. They were in the factory, in the field every single day and the scrambling that took place to just keep everything on the rails where you had to keep doing business in the way that you were doing it in many regards. And for instance, one of the CEOs of Havco that makes the flooring in the back of a dry van trailer on the tractor trailer truck, he said, we can't make wood floors from home.

So the impact of that business was immense and unprecedented. Clearly, at the instant, where March 13th shutdown orders took place, a lot of order books collapsed and you had shocks to the system and again I keep using the same two words, amazed and grateful, at how quickly both the management teams responded and figured out how to conduct and operate businesses, and how fast the order books came back and in fact started to top up and go further.

So last year's results were very good. I think they represent sort of a phased shift and a change in the maturity and size and scale of what Markel Ventures is relative to the total company, but it's not something that -- that's sort of a new baseline and as we look in 2021 and 2022, we would expect the profitability that we saw last year to continue and to grow and what gives me excitement is just to see that the quality of the people that are running those businesses, how well they've done at a time of great testing and what kind of results they're putting in the board and how they're taking care of their customers and their people off. It's just exciting to be part of it. So you pick up the right tone in terms of optimism and bullishness, and this is no longer a lab experiment, it's a big business and matters.

Q - Mark Dwelle {BIO 4211726 <GO>}

Okay. I appreciate the additional color. Thanks. And that's all of my questions.

Operator

Our next question comes from Josh Shanker with Deutsche Bank.

Q - Philip Stefano {BIO 20346322 <GO>}

Yeah. Hi. This is Phil Stefano. Thanks for taking the question. So -- can you hear me okay?

A - Thomas S. Gayner {BIO 1896932 <GO>}

Yeah.

A - Richard R. Whitt {BIO 7084125 <GO>}

We hear you.

A - Thomas S. Gayner {BIO 1896932 <GO>}

We got you

Q - Philip Stefano {BIO 20346322 <GO>}

Perfect. Just wanted to ensure that that was me. So, Richie, I appreciate the -- you showed me [ph] state reference. As we think about the evolution and the earn-through of price and business mix changes, is there an acceleration in the improvements of the underlying loss ratios as we look through this year or does the conservatism kind of hold? I mean, I understand that you talked about Reinsurance first quarter was a bit quirky and that -- how that was reported, but just been thinking about the sequential changes in this as we look ahead?

A - Richard R. Whitt {BIO 7084125 <GO>}

Yeah. That's a great question, and I'm trying to think about how to answer it. I think it's fair to say -- start with more likely redundant than deficient. We are going to try always to be more likely redundant than deficient, and we are going to be slow to recognize good news, fast to recognize bad news. That's what we've always tried to do in terms of running our insurance businesses. I do not believe -- just because of how we think, I do not believe all of the rate increases that have been received in excess of claims inflation. I do not believe they're all baked into our combined ratio at this point.

I can't tell you -- I think it's 20% in there and 80% to come. 50:50. I don't know exactly. In good markets, things tend to get better than you expected; in bad markets things to get worse than you expected. I do -- I guess, the best thing I can tell you is, I do not believe we have baked into our attritional loss ratios at this point all of the rate that we've been achieving.

Q - Philip Stefano {BIO 20346322 <GO>}

Okay. No, that's fair enough. And just looking at Reinsurance, I would have assumed that pulling out the cat business would have been a headwind for the attritional loss ratio. It probably would benefit -- I mean, absolutely volatility in the long run, but it feels like the commentary around the low-60s makes the list from pricing all that more impressive. Is the -- am I thinking about this right that the cat business coming out would have been a headwind, the pricing is helping to offset?

A - Richard R. Whitt {BIO 7084125 <GO>}

Yeah. I'd tell you, the first quarter is difficult to parse, it really is, because of the -- well, the current accident year loss ratio -- we still had earned premiums from cat in the first quarter that had Uri in it. The thing I can tell you, we can go away and try to kind of think through pulling apart the numbers. The thing I can tell you is, on a go-forward basis, we think the specialty casualty professional book should be somewhere in the 60s and I won't give a specific number, but that's what we're shooting for in terms of how we're pricing that business. So the first quarter had some anomalies in it with the transfer of the business -- some of the business over to Nephila, the underwriting results of Lodgepine being in there and just Uri, the losses on Uri being in there. So it is a little hard to pull apart.

A - Jeremy A. Noble {BIO 20687803 <GO>}

Hey, Phil, it's Jeremy. I'll just maybe jump in there as well. I think that's an important point that Richie has made. It's going to take a little while for the earnings tail to run off. So our earned premium in property lines was somewhat comparable year-over-year and some of that is because we are purchasing less reinsurance. So that benefits as well. So when you take the actual cat experience out and you look at that attritional loss ratio, it's very low on the property lines that still has earned premium. That's going to fade away as we get into the year. And, importantly, as we approach to midyear, we really start cutting off risk in property as well, so we should have less exposure and less volatility. And you will start seeing the blended result in the reinsurance segment, really being the combination of our casualty, professional and specialty lines. And that will blend to be -- as Richie was talking -- commenting earlier, slightly higher than what we see on an attritional basis in the first quarter.

Q - Philip Stefano {BIO 20346322 <GO>}

Okay. And switching gears to the Venture business. I guess, when I try to tease out the Lansing impact, it feels like the first quarter underlying revenue was still down high single digits, and I think that's the pace that we saw in the back half of 2020 as well. Tom, how economically sensitive is this business to the go-forward rebound in the economy or is -- do you feel like this underlying growth, there is kind of hidden nature and we pivot as we look forward?

A - Thomas S. Gayner {BIO 1896932 <GO>}

Well, I think directionally your number is in the sensation of the portfolio prior to Lansing topline revenue numbers are correct and I would describe a lot of that happened because of the shock that would have happened on March 13th when you shut the economy down. Through 2020 all of the businesses recovered thankfully [ph]. They got better as the year went on.

To answer your second question, how cyclical are they? There are a lot of cyclical businesses in there that are highly exposed to things like transportation, freight volumes, new car sales, things of that nature. And I want to harking back to look at the language that we have put in the annual report, where we put those five-year buckets, because that's really how we think about things and look at what has happened. We've got 15 years. So there's three five-year buckets. And if you look at the results of the cash flows, EBITDA, the net income, however you want to categorize it or look at it and you look at it in those five-year bucket terms, that's a very up into the right chart that we're looking at.

Secondly, I want to pick up on a point that Richie made in answering to some of the questions about the reporting with the pace of things being apparently getting better at. He said, we are quick to recognize bad news and slow to recognize good news. That's true for Ventures as well. We don't have a different philosophy or a different culture when it comes to reporting the Ventures' results as opposed to the Insurance results.

And one of the points I was trying to make about the culture and the size and scale of being large now is in the early years of any deal where you have purchase accounting and the amortization of goodwill and customer lists and all of those sorts of things, proportionally they would tend to be the heaviest at the beginning and diminish over time. Now if we were interested in sort of managing earnings per share, we would work a little harder about trying to smooth that out and make it painting a prettier picture on day one. We don't care about that. We care about the cash returns and the earnings that the businesses have themselves produced and we want that to be sustainable over an indefinite long-term period of time.

So it's only after a couple of years that they are part of the family and part of the company that the accounting conservatism sort of burns off and you start to be able to discern the true underlying economic performance of the business. And so that is reality, that is what is happening, you want to see hard physical visual evidence of it, look at the annual report letter and look at the five-year buckets and see how do you feel.

Q - Philip Stefano {BIO 20346322 <GO>}

Just one more and then I'll go back in line. I guess, in my mind, on the Insurance business, one of the things that allows you to be slow to recognize the good news and quick to recognize the bad news is the cost of goods sold is much less transparent than, in my mind, it is in the Ventures business. I guess, what flexibility do you have in the Ventures reporting to allow enough flexibility, maybe that's not the good word, but what optionality do you have in the Ventures reporting that allows you to have that mindset?

A - Thomas S. Gayner {BIO 1896932 <GO>}

Well, not as much as I would like, quite frankly. So the purchase accounting rules which change from time to time and these are GAAP under the auspices of PCAOB imposed things and I do remind people that I was formerly trained as an accountant. I am a CPA non-practicing and I look at some of the accounting rules, shall we call them, and I try to think of them with my financial hat on and economic hat on and cash hat on as opposed to GAAP hat on and the accountants around here get tired of my lectures on these sorts of things, but it doesn't matter and I don't care. What we care about is the cash, earnings of the business and the growth and the returns on capital and those are up into the right.

So we're slow, it's painful and in the current year's and the freshness of the deal, because from the inside perspective where I know the business and I see what's happening, it's better than it looks and it just takes a period of time before it looks as good as it is. And the size and scale absent a large deal, we're starting to get to the point where it's starting to look as good as it is. Now if we do a big deal, we'll start that clock all over again, but the denominator and the size and scale of the market [ph], which in is entirety right now means that the incremental effect of any new deal is probably a lot less than what it used to be. And, again, I'd just keep getting back to that notion, if you really want to be able to draw hard lines and reconciled of them to GAAP accounting, look at those five-year charts.

All right. Maybe, Phil is up there looking at them. I think we've lost him. We might be having some technical difficulties. I'll ask our operator --

Operator

Looks like this is going to -- to go ahead and conclude our question-and-answer session here, I'd like to turn the call back over to Tom Gayner for any closing remarks.

A - Thomas S. Gayner {BIO 1896932 <GO>}

All right. Perfect. Thank you so much for joining us. We're happy to report the kind of news when we were able to do. We look forward to continuing to do so as time goes by and before we do see you at our Annual Meeting on May 10th in Richmond, Virginia, we will be live and in person and anybody who can join us, we'd love to see you. Thank you so much.

Operator

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