Q4 2015 Earnings Call

Company Participants

- David Andrew Horton
- Martin Lindsay Bride
- Neil Patrick Maidment

Other Participants

- Barrie Cornes
- Joanna T. Parsons
- Kamran Hossain
- Nick Johnson
- Thomas Seidl

MANAGEMENT DISCUSSION SECTION

David Andrew Horton {BIO 5697110 <GO>}

Good morning and welcome to our Results Presentation for our results for the year ended 31st of December 2015. So, if we look briefly at the agenda, I'm going to give you an overview of 2015. I'm going to hand over to Martin who'll take you through the financials. Then hand over to Neil who's going to go through what's been going on in the underwriting in 2015 and a view of 2016. I'm going to come back and briefly look at our vision and strategy again and then the outlook for next year.

So, if we look at the overview of 2015 we've got the headline of increasing premiums, profits and dividends. And as you can see, our profit before tax was up 8% year-on-year at $284 million. We're pleased with the growth we've managed to get to low 73%. As you may all be aware, the market is very competitive, and rates are falling in many of the areas of business we are in. So it's great to show some growth with premiums up to $2.081 billion is good.

Prior reserve releases are slightly up on the last year. Martin will be taking you through those in a bit more detail. But we all know it's a relatively quiet claims environment not only for catastrophes, but across most of our lines of business. So profit is somewhat flatted by that claims environment.

Again, we all know the investment world's been quite volatile, and it was volatile really after Q1. So most of our investment income is made in Q1, and then we did pretty well in Q2, Q3, and Q4 despite spreads growing and shrinking and growing again and the equity markets showing quite a lot of volatility.

And on the back of our profitability, our growth expectations for 2016 of around 5% and our business mix which generates our capital that we need for 2016, we've announced a growth in base dividend in line with normal, I think, 5.10% to 6% (1:48) growth in base dividend. And on the back of having more surplus capital, we've been able to announce a special dividend of £0.184.

If I look at what we've actually been doing in the business on the next slide. Continue to invest in people. So, we've gone from two people about 30 years ago to just over 1,000 people in 2015. We continue to recruit high-quality individuals who generally stay here, retain them and do incredibly well for the company. I think there are going to be more opportunities, there were in 2015 with more stress in the insurance system than has been historically, and we expect that to continue into 2016 as we expect to continue to attract talent.

The U.S., it's fantastic. It's growing by 20% for the third year in a row. And we've added a new office in Los Angeles in spring last year. So, the last part of our U.S. footprint is in place in the Los Angeles office. We are excellent at filling up offices. We've opened an office and are great at recruiting people and fill them up and look to move to a larger space relatively quickly. And we've done that – and doing that with LA.

We announced I think at the (02:53), we've got the Korean Re partnership which we, I think, started in about April last year. It's going to be relatively small for us. It has several elements the first was just purely this insurance swap. We are ceding about 1% of our premiums to a sidecar syndicate 60-50 which ultimately they will take offers, and they're giving us about $20 million of growth premiums back which we can't easily access. The exciting part is working on initiatives where we work together on developing product that we could help them launch within Korea. And we have a number of initiatives underway, but it is going to start small.

Strong balance sheet and active capital management continues. We have a good buffer. As we will see when Martin starts talking and we continue to maintain this idea of distributing capital if we have excess. Fantastic work over many years means we eventually got our Solvency II model approval from the CBI in December. Add to the (34:47) fantastic work from the teams within the company. And we announced this morning and Martin and I have been talking about it over the past couple of years, our aim is to move the management back to the UK, which should happen from the end of April.

Quickly looking at the charts, top left, as I mentioned, growth is tough, but we have shown for the past four years or five years, we can continue to grow top-line premiums, which is great. Rates have been going down across our portfolio for the past couple of years. Combined ratio on the right somewhat flatted by the quiet claims environment and you can see for the past three years we're under our expected long-term average of 90%.

Bottom left, slightly concerned, but special dividends are supposed to be special, and yet we've had special dividends for four of the past five years. Worried when the fifth one drops off, depending on what happens in 2016. Our aim is to wean people off special dividends, to some extent because we would like to grow more than we're currently growing and, that opportunity may arise at some point in the future.

And of course it's a combination of underwriting margins and underwriting profitability versus expected growth which is generally driving whether we can return surplus capital and that balance may change going forward. And return on equity, again, we're really pleased with the excellent ROE of 19% in 2015. But these are under pressure from the ratcheting (5:09) environment, potential uptick in claims and competition.

This chart we've been showing for a few years now. And briefly to explain it again, the grey triangle is where our long-term incentive plan kicks in and tops out. So, to get anything from a long-term incentive plan, we have to deliver just under 100% growth in net asset value over the six-year period and to top out 150%, the red diamond shows what we've achieved. We've shown we've achieved 164% I think growth in net asset value over the past six years.

And our belief was if we manage to achieve this, we would be one of the market's leaders in terms of ROE, which means the share price would be rerated and the share price would rise. What we have found is we have been rerated over the six-year period which is good and of course the market has been relatively buoyant for insurance stocks and the redline shows what the total shareholder return has been since the end of December 2009. On that note, I will hand over to Martin.

Martin Lindsay Bride {BIO 15458196 <GO>}

Thank you, Andrew. Good morning, everyone. I'm Martin Bride, the Finance Director. I'm going to talk very briefly about one or two of the key financial metrics and then go through my habitual three subjects sort of investments, reserves and capital. So in terms of the key financial metrics, we continue to grow net earned premiums as well as the top line so that was pleasing in the current environment. And then one or two of the per share metrics and in particular, there is a tailwind from FX. But even though we've distributed £0.214 to shareholders since last year-end, net tangible assets per share were up 10% at £1.748 so that really underlines quite a successful year Beazley's had in 2015.

So the investment picture really a tale of two halves, 2015 started out very strongly in the first half. And in my view, our teams did extremely well to nevertheless return slightly positive performances in Q2, Q3 and Q4. So overall it's a very low interest rate environment. And in absolute terms, 1.3% is not that much but we consider it a very acceptable investment return given our level of risk budget which is moderate in the current financial environment.

We did of course see the first raise in U.S. interest rates at the very end of the year that in the short-term has an exit impact. The investment portfolio has been pretty stable for the last two years or three years. The only point at the end of 2015, we have more than cash than normal. There are a couple of very specific reasons for that. It's a temporary effect, a split of 15% capital growth assets, 85% in a core portfolio of sovereign and corporate credit remains our target, and you should expect to see that as we go forward.

Turning to reserve releases, the overall reserve release is very much in line with our five-year average. Pleasing to see all the parts of the business contributing to that release. As Andrew's highlighted, we have, once again, enjoyed a, what we consider to be a below-average catastrophe claims environment. And that does boost reserve releases in the classes of business such as property, reinsurance, and marine over their normal levels. And you can see that in the chart. Pleasingly also our specialty lines portfolio delivering an increased reserve release for the first time for quite a period, so that was encouraging. So that's the past on reserve releases.

This chart here is our attempt to look into the future of reserve releases which is difficult. But what this chart's telling you is that our view of the reserves in our balance sheet is that they have a very consistent margin in them compared to the internal actuary's estimates of what's required. And you can see at the end of 2015, we're at 8.2%, which is in the corridor we're targeting. So, all other things being equal, we would expect reserve releases to continue in the future at the same levels that we've seen over the last five years.

On capital, our capital management discipline has been continuing over six years. The cumulative effect of that is quite significant. We have now returned $952 million to shareholders over the past seven years. That represents nearly 1.5 times the market cap of the company at the point of which we asked shareholders for additional funds in early 2009. So, we're very proud of that track record. We hope to continue a very positive performance possibly not quite at those levels every single year but it's a very encouraging long-term achievement.

So, our actual capital at the year-end is – this table shows you our capital requirements, how much do we require to support our business. As you can see, it's actually down 2%. We are growing but as Neil would explain there is some shifting of the portfolio across different classes and that's generating this effect that despite the fact we're growing, our regulatory capital is actually – requirement is actually reducing slightly.

So at December, even after the special dividend, we project having a surplus buffer of 35%. We haven't changed our views that 15% to 25% is the level we should really target as an appropriate buffer, but it insulates us against unexpected events and allows us to fund growth opportunities, which is slightly above that this year-end.

So Andrew announced the fact that we are going to move to run the strategy of the group from the United Kingdom, so just a couple of bullet points on that, to give you a little bit more information. So that will – needs to go through a shareholder vote because it involves the creation of a new top co. And that shareholder vote is scheduled for March. There is going to be no change in our operating platforms and structure, our expected profits and figures or our projected tax rates.

So it is a move that allows us to direct the group from the United Kingdom but doesn't change any of the day-to-day operations at Beazley. And then finally, I'm sure you'll be pleased to hear, we will be retaining the name Beazley Plc for the new top company.

So I shall hand over to Neil Maidment.

Neil Patrick Maidment {BIO 5232207 <GO>}

Thank you, Martin, and good morning ladies and gentlemen. In the next part of the presentation, I'm going to be looking at our underwriting performance and causes to the underwriting performance which is the main driver of the results that we're talking about today.

So 2015 highlights combined ratio of 87%, as Andrew mentioned. That's an improvement on our five-year average of 90% and some improvement on our prior-year performance. Also very pleased with the growth of 3%. There were a number of drivers for that growth. But the main contributors were 13% growth in our largest division specialty lines, and the continued very positive development of our business onshore in the U.S., which grew over 20% to managed premiums of just under $650 million.

Now, all of that was achieved despite an increasingly competitive market background. I'm going to talk in a moment a little bit more about market conditions. But what I would observe is our ability to reach an increasing amount of SME, a mid-market business that's a more stable market environment that's helped offset the more competitive environment that we experience here in the wholesale market in London.

As Andrew also mentioned, the results have benefited from a relatively benign claims environment. We've had the second consecutive year with the abnormally low claims at catastrophe activity, plus the tenth consecutive year without a land-falling hurricane affecting the East Coast of the United States, something that I would predict will not go on forever.

Also, on claims, as Martin mentioned, the reserves have continued to develop favorably in 2015. And our consistent approach to setting those reserves means that we finished the year with our surplus over our own actuarial within the target range of 5% to 10%.

So by if I turn to look at the numbers, gross written premiums, plus 3%. Net written premiums actually declined by 1%. That's because we bought some more reinsurance. There were two main elements of that. The first was the partnership with Korean Re, is established through a swap arrangements, and the outgoing premium contributes to that increased reinsurance spend. The second element was we bought more protection in two areas of the accounts. Firstly, within the large lawyers and architects and engineers within specialty lines, and second within property catastrophe reinsurance in our treaty team. Those are two areas where pricing has been under pressure for a number of years.

Unpacking the combined ratio, we're having expense ratio improvement of 1%. That was largely a rate of exchange effect. And if I took that FX effect out, expense ratio is in fact flat. That shows that we're continuing to invest in the business in line with the element of our revenue growth. Claims ratio also improved by a point, reflecting that relatively that benign claims environment and as you can see at the bottom, pricing reduced by 2% overall.

And let's turn to look now at market conditions. This chart shows the risk adjusted rate change on each of our products going back to 2008. We measure pricing on a risk adjusted basis to take account of changes in terms of conditions and changes in exposures where there's changes in premiums. The first thing I had observed about this chart is the dotted red line, which shows the composite, the overall rate change on the portfolio is relatively consistent going back to 2008, which obviously underscores the benefit of a more diversified portfolio.

Looking at the individual divisions, life, accident and health, which is that black line near the top, goes up 1% and finished the year close to flat. Four of the other divisions: property group, political contingency group, marine and reinsurance, all experienced more competitive market conditions through greater or lesser degree with the largest reductions coming in the marine team, minus 8%, and the reinsurance team, minus 7%.

That was somewhat offset by our largest division, specialty lines, which saw a continuation of the positive rating trend that we've experienced since 2012 and actually prices improved by 2% in specialty lines. That was driven by Cyber where prices improved following a number of high profile breaches that occurred for the backend of 2014 and into 2015, and that drove increased demand and stronger pricing.

If we turn to the outlook for this year, broadly, we're expecting similar market conditions to continue into this year that we have relatively benign claims experience is fuelling competition. Also supply of capital into the insurance industry continues to grow at a faster rate than demand for insurance products. So those two drivers mean that we should anticipate overall pricing reductions and indeed at January 1 treaty renewals in the reinsurance market, which is often seen as a bellwether for the rating conditions for the rest of the year. Prices continue to drop in our portfolio by 5%.

Now, with overall pricing reduction and any return or return to a more normalized claims environment, we'll put up with pressure on our combined ratio and we should anticipate reduced margins. Against that background and that expectation, we do, however, continue to plan for moderate growth in 2016. Our planning process every year is around cycle management. That's pushing forward in the areas where we see more opportunity, pulling back in areas that are under pressure.

In 2016, we will continue to reduce our commitment to the markets such as energy, insurance and property reinsurance where prices are under pressure and we will focus on underwriting the (19:39) tax margin. In line with that, as Martin alluded to earlier, we will continue to reduce our catastrophe risk budget this year as prices have declined.

At the same time, as those more negative environments, we do see opportunities for growth, four I want to highlight. The first one is the continued opportunity to build in the U.S. We have the first full year of operation for Los Angeles office, which as Andrew mentioned is already growing strongly. We expect to see the continued benefit of our more focused distribution strategy, which has been a strong driver for growth in 2015, as well as the initiative to put more of our products in more of the offices across the nation.

One of the products that we saw develop positively in 2015 was our gap medical products within life, accident, and health. We've seen the first influx of demand in that area, and we expect to build on that in 2016. We also expect demand for cyber to continue to grow. We have our market-leading flagship Beazley Breach Response product. That's the service-lead product that's targeted at mid-market and smaller customer. That continues to grow.

In addition to that, we've seen increased demand for large risk customers following those high profile breaches that I referred to earlier. And finally, we are also seeing the first signs of demand in international market. So, markets outside of the U.S. as there is the prospect of the adoption of stronger regulation around privacy.

Last (21:24) that I want to highlight is the SME part of our portfolio. We've been growing the number of customers that we have in this segment in both property and specialty lines and marine over the last several years. We see opportunities both in the U.S. where we can focus in 2016 on automation to drive higher levels of productivity, and in Europe where we've launched myBeazley. That's the online platform that helps us sell standardized product to retail brokers in the UK and France and other countries. And we also have the first full year of operation of our new media team.

Now, Beazley is fortunate, I think, to have these opportunities for growth in what is otherwise a low-growth environment, and one of the benefits is that it does enable us to focus on underwriting discipline in the areas of our portfolio where prices and margins are most under pressure. So with those thoughts for the environment of 2016, let me hand you back to Andrew.

David Andrew Horton {BIO 5697110 <GO>}

Thanks, Neil. I just want to remind people of our vision and the strategic priorities that we talked about. One certain change. So we got the vision to become and be recognized as the highest-performing specialist insurer. That hasn't changed, and the six pillars underneath that, our strategic initiatives we have real focus on.

So we've got three geographic growth initiatives, growth in the U.S., which we just talked about, growing at about 20% per annum. We talked less about growth in Europe, which is our Paris office, mainly, and our UK regional business, but that's also grown 20% in 2015 from a much smaller base, of course, than the U.S. And similarly, Singapore, which is a cornerstone of our Asia-Pacific strategic initiative, also grew about 20% in 2015. So it's obviously a good number to focus on as we go forward into 2016.

Innovation and product development. We come up with our market-leading cyber product and the gap medical (23:27) and other products we continue to launch and think about. Some have been a lot more successful than others, and our aim is to continue to innovate in an industry that is not generally that innovative.

Two new ones, Neil has mentioned one focusing on SME where we've been growing this profitably over many years and Adrian Cox is now going to focus on bringing those together to see whether we can grow that better going forwards than we have done historically.

Sales and services, also important in a low growth environment. We're trying to get our underwriters to be more proactive, looking for opportunities and ensure we maintain high levels of service on both underwriting and claims. As I mentioned, (24:07) in the insurance system is the pricing and margins are coming down and many insurance companies we're seeing are reducing their levels of service. And we think it's a great opportunity to show we can maintain and improve our levels of service. It's amazing how much business you get by just being responsive.

Finally, outlook for 2016. (24:29) our 30th year we're obviously founded (24:30), as many of you know, back in 1986. So it's celebratory year for us in our 30th year, continue to grow with our organic strategy. Opportunities to recruit. I think, we're going through many opportunities to recruit this year and we're going to continue to build out in almost everywhere we are in. I started listing out, we're going to grow in the U.S. and Singapore and Paris and the UK, and then I realized that this could have everywhere we're actually present. Our aim is to look for good quality people and we think there will be many of them around this year.

I think we've covered enough, but we think markets (25:01) are going forward, and I've been already pointed out by one you that I've said exactly the same thing last year. So apologies to that, that I'm so repetitive. But I can't think of anything new to say. But there is plenty of capacity and plenty of competition around in 2016.

Targeting growth in the States, 20% per annum, (25:20) great, pursue our initiatives, real focus on ensuring levels of service are maintained. Final comment from me before I hand over to questions. You may have seen in the press release. After seven-and-half years in this job, I'm going to take a couple of months off in March and April. And I'm going to hand over the CEO role. Neil is going to be acting CEO. I'm sure he's going to do an excellent job, hopefully not too excellent job.

Please get a microphone.

Q&A

Q - David Andrew Horton {BIO 5697110 <GO>}

Good morning, just a few questions on capital, if I may. A big surprise on your capital buffer at the end of the year. Both capital requirements were lower than expected. And your available capital including the Solvency II adjustments were much higher. Can you give a bit more detail on your available capital and what the Solvency II adjustments are, and what makes it higher?

And secondly, the outlook for the requirement in 2016, how much more can it decline on the back of the declining risk appetite? How far (26:32) is going to come down and what does that mean for the capital requirements?

A - Martin Lindsay Bride {BIO 15458196 <GO>}

Right. I think going forward, the appropriate benchmark for capital requirements is to think of capital requirements growing with premium. So what you're seeing there is a flat to reducing requirement, and as Neil has identified, again in 2016, our risk budget is reduced, which is probably the driver of that. So big picture, I think capital growing with top line mid-single digit is the expectation.

In terms of - in the Solvency II world, our capital (27:11) using Solvency II balance sheet, which is not - is a private balance sheet, rather than a public balance sheet. And on that private balance sheet technical provisions of discounted, best estimates and there are a number of other changes. So I think you're slightly surprised at the high level of the capital buffer at the end of the year in 2015.

Whilst it's been an excellent year for Beazley in the IFRS world, it's actually been an even better year for Beazley in the Solvency II best estimate world. Notably, there have been no catastrophes, and that goes straight into Solvency II adjustment much earlier than you see the benefit of it in IFRS results, for example. So that is why the buffer at the end of this year is a bit higher than usual.

Solvency II world is more volatile. So we framed this idea of a 15% to 25% buffer, which was higher than the 10% buffer we used to use. And the reason for that is there is some volatility in the Solvency II world. So I think it's probably nice that I'm explaining. The Solvency II balance sheet is more volatile in the first year when things have been more volatile, good.

There will occasionally be years where things are more volatile, bad. And as I say, that's why we, as a board, judge to go to a slightly higher capital buffer. The idea of that is that we - we're confident that we can continue to operate and grow the company and have enough money for moderate growth opportunities without needing to ask shareholders to support us.

A - David Andrew Horton {BIO 5697110 <GO>}

Yeah. The catastrophe with budget in managed premiums, just reducing (29:04) from $560 million to $500 million, so the group share of that is about 83%. So it reduces to about $415 million.

Q - Kamran Hossain {BIO 17666412 <GO>}

All right. So it's Kamran Hossain from RBC. Two questions. The first one, just coming back to your points in capital. So you mentioned that it's a particularly good year. Solvency to balance sheet, especially stronger. But obviously in 2015, 15% to 25% surplus. And with that, (29:36) 35%. So can you just talk us through why you didn't take that down further? And the second question, just on investment positioning at the moment, are you considering taking down the proportion of risk assets in the current environment or are you happy with the allocation? Thanks.

A - Martin Lindsay Bride {BIO 15458196 <GO>}

Right. So, on the - there's no - I think there's no right answer to capital management. I was expecting someone to be disappointed with 25 (30:08), buy you've got 35% buffer (30:12). I think - what I would say overall is for our capital management discipline, I think has proven over a long period of time. And if it transpire that we haven't done quite enough this year. Well then, that will correct it in the (30:28) of time.

We felt that a 25 fee total second payment is substantially the best payment we've ever made. It was already a pretty strong message when the backdrop is one of more competitive rights and you - perhaps, you would come out with an even larger dividend with impossibly confuse people. And the management staff, they are saying the world is getting slightly more challenging and yet - but anyway. So, I think the board considered the options and that was the right level.

On the investment risks side, I think that big picture, 15% risk assets, 85% co-portfolio were changed. We are implementing changes within those two portfolios currently in function of what we see in the investment markets. So we have been selling some non-investment grade credit bonds we started out in December. And we have happy to selling (31:26) equity, so no change in the portfolio and tight percentages in my view. But yes, definitely tactical adjustment within those according to how the investment team see markets.

Q - David Andrew Horton {BIO 5697110 <GO>}

Thanks. I had two questions on the specialty business. Firstly, could you say a bit more in terms of how sensitive you think our performance would be to different levels of competition in the U.S.? I mean, do you see fallout from, for example, (32:00) base merger or that is there other M&A that will impact or is it really more about your distribution and the teams that you have there. And secondly, in terms of the claims ratio, that the last ratio looks like the last ratio that the first year pick was very flat this year given, I guess the volatility that has been in the past. Are you now at a level which you see as sort of sustainable going forward, given the claims trends in those markets? Thanks.

A - Martin Lindsay Bride {BIO 15458196 <GO>}

(32:32) pick up the first one. I mean, at this point in time, where we feel very positive about growing our specialty business in the U.S. based on what's going on in the environment. And that can be the excitement's going on AIG and Zurich where that's generally pulling back a bit, which gives us an opportunity to show a more consistent approach, which we've been trying to do at the past 12 years we've been there. And similarly with the (32:52) where they could be more internally focused rather than externally focused and they will have overlaps.

So I think Adrian who is sitting in the audience is very excited about the - at this point in time. Of course, things change. And certainly at the edge of the cyber market, there's more competition coming in. As the market tends to grow, the bigger carriers then notice it. When it's a small market, they don't notice it as much. Margins are relatively good. So you have a mixed bag. But generally, I think we feel positive 2016 should be a good growth year in the U.S. for our specialty business.

A - David Andrew Horton {BIO 5697110 <GO>}

(33:26) last pick for the specialty account, I would expect to be relatively stable reflecting the relatively stable pricing environment that we've seen. It does also changes as the mix of the business changes because the short tail cyber element has a different aspect to the traditional specialty line accounts. So if the mix changes, it will (33:53) the margin.

But I would expect given the current pricing environment modulating by 0.2 on the EBIT side, it would be relatively stable.

Q - Joanna T. Parsons {BIO 1558226 <GO>}

Thank you. Joanna Parsons from Stockdale. Could you give us a little bit more color on your expectations then for cyber, and obviously it's been in the press a lot and it's grown quite (34:24) as part of your own portfolio. And I know you talked about expansion and potential opportunities in Europe and internationally. Could you talk a little bit more about that and how you see that developing over the next couple of years?

A - Martin Lindsay Bride {BIO 15458196 <GO>}

I'd see continued potential for growth just in the three buckets. I'll describe the Breach Response products which is targeted to the mid-market and smaller customers. That continues to grow at the marketplace, so with more and more people are buying, it remains a blue water opportunity (34:55) new customers. And we're continuing to enjoy a very distinctive profile with that product set and our brand in that marketplace and the reputations that we have for service delivery.

On top of that, we've seen more opportunity in 2015 for large cyber customers. Previously we had less appetite for those risks because we didn't believe pricing the risk reward dynamic was quite right. We've seen pricing adjust as those high profile breaches reported, and we've seen more opportunities. And we expect that to continue to build in 2016.

So we expect people to be repeat buyers of the more consistent side of program, risk transfer program. And that will give us opportunities to pay more overall.

And the third area is international. Most of our business remains U.S. at the moment. The U.S. is not the only place in the world that experiences data breach and (36:02), and we are seeing increase demand internationally. (36:08) is adopting increased regulation around privacy in 2016, it does take a couple of years for those regulations to come into force. So that will encourage demand. And partly in response that increase in demand, we put together a consortium of (36:25) to help bring relevant capacity to the European market as it continues to develop.

Q - Joanna T. Parsons {BIO 1558226 <GO>}

Thank you. Can I just follow on from that? So, there's also a lot of talk about the accumulation risk in cyber and we still don't really understand that. How do you approach it, and are you going to continue to focus on BBR, will you expand that for the cyber coverage?

A - Martin Lindsay Bride {BIO 15458196 <GO>}

So, I'll take the second one first. Most are exposure within cyber perils remains data breach rather than physical damage or business interruption or other heads of cover (37:08), so the most of the exposure is data breach. We go about assessing it just as we do any risk. So we start by adding it up. I'm always a great fan of being a TIV underwriter, a total insured value underwriter. So we start by adding it up. And then we spent a considerable amount of time, in particular over the last two years, building out a scenario set to test those aggregates in various scenarios. So we build our own scenario set, and then we have to establish a risk appetite and reinsurance to deliver that risk appetite based on that scenario testing.

Q - Barrie Cornes {BIO 2389115 <GO>}

Hello. It's Barrie Cornes, Panmure Gordon. I got three questions, if I may. First one, I wonder if you could give a bit more detail on the reinsurance spend increase that you talked about. I guess you're taking advantage of the soft market. Can you give us a sort of flavor of net retention, where you're going with that?

The second question on the rating environment. I just wondered if you could talk about post or at first of January 31/12 and 1/1 (38:18) renewal season, a bit more detail on perhaps by line, the larger lines maybe. And the third question I have is in respect of M&A, must've been a fair bit around (38:28) M&A within the London market, just wondering if you're seeing opportunities either for business or for people? Thank you.

A - Neil Patrick Maidment {BIO 5232207 <GO>}

Can we start with the last one or are we going to...

A - Martin Lindsay Bride {BIO 15458196 <GO>}

Thinking about this (38:39).

A - David Andrew Horton {BIO 5697110 <GO>}

Barrie, which way (38:42) opportunities for us to acquire?

Q - Barrie Cornes {BIO 2389115 <GO>}

I'll leave that open.

A - David Andrew Horton {BIO 5697110 <GO>}

I think at this point in time, from an acquiring point of view, prices are incredibly high and price expectations of anybody wanting to be acquired is very high. And as we're growing so well organically, adding about 100 people to our group last year, I think we'll continue to focus on that. So we're very good at picking out individuals or small teams of people, and therefore I think we should maintain focus on that. M&A is tough, as you know.

(39:16) it's much easier to see that on singles, doubles, and triples. From an M&A of being acquired point of view as we've debated before, it's quite a difficult topic to talk about. We're happy with where we are, our shareholders seem happy, the returns are good, we're relevant in the lines the business we're in. And we have such a youthful (39:34) management team that we want to continue down the path we're in at this point and time.

A - Neil Patrick Maidment {BIO 5232207 <GO>}

And then on the other two questions, Barry. Pricing, I would characterize as being very consistent with what we experienced last year. And our overall expectation for 2016 is very much in line with the minus 2% to 3% (39:57) that we experienced in 2015. And we expect the areas of the market that we're most competitive in 2015, to continue to be the most competitive areas in 2016. So, energy, aviation, marine transport, marine liabilities, the reinsurance market, all of those areas are experiencing negative trends, and balanced somewhat by the specialty lines market where we've seen a steadier pricing generally. We've seen that positive pricing trend in cyber, and in particular the mid-market and SME business that we write onshore in the U.S., tends to have less pricing volatility than the large risk business that we write here (40:51) market.

In terms of reinsurance strategy, we are long term buyers of reinsurance, and therefore, the overall picture hasn't changed very much and we have a relatively consistent reinsurance strategy. The two areas that we've just adjusted, one is the CAT retention so we were just talking about reducing our catastrophe risk budget. We're going to do that by buying more reinsurance on the catastrophe account and then the second area where we've seen some particular challenge is within the large professional indemnity market for in particular large lawyers. We bought some additional proportional reinsurance to mitigate the impact of that and allow us to continue to serve the customers that we've had for quite a long time.

Q - Barrie Cornes {BIO 2389115 <GO>}

Okay. Thank you.

Q - Nick Johnson {BIO 1774629 <GO>}

Good morning. Nick Johnson from Numis. Just a question on the cyber consortium. I just wonder if you could elaborate a bit on the rationale for signing up a consortium rather going alone and (41:55) competitors. Perhaps if you just discuss the economics and strategy behind that.

A - Neil Patrick Maidment {BIO 5232207 <GO>}

I shall (42:00). So it just reflects the early developments of the international markets, Nick. So the first flash (42:09) of that demand is for large general cyber products requiring relatively large limits. So rather than change our own retention strategy, we've partnered with some other markets to maintain our retention strategy to provide that cover.

We haven't seen the development yet of demand for breach response services type products in a large way. That's the piece of the market where we have particular IP. As regulations around privacy change in Europe and other markets, we would anticipate there'll be more demand for that product. And that part of the market, I would anticipate, we would serve by ourselves.

A - David Andrew Horton {BIO 5697110 <GO>}

Thomas is going to ask a question after eggs and breakfast (43:02).

Sorry. This is Eamonn Flanagan of Shore Capital (43:06). Just couple of things from me. Firstly, I can't find any detail about your investment expenses. I don't know if they're in there somewhere, maybe I missed them. If not, maybe you could you tell us.

A - Martin Lindsay Bride {BIO 15458196 <GO>}

(43:20) they are in there. They're $10.2 million (43:21).

Q - David Andrew Horton {BIO 5697110 <GO>}

Thank you.

A - Martin Lindsay Bride {BIO 15458196 <GO>}

(43:22) $11.8 dollars (43:23). And Stuart Simpson, who became CIO, at the start of this year, has some further ideas that we need to execute over the next couple of years that will hopefully bring it down a bit further. So work in progress.

Q - David Andrew Horton {BIO 5697110 <GO>}

Thank you. And secondly cyber claims, you indicated in your statement that you've seen an increase in the level of cyber claims within your own book. Just a wee bit more color if you know where they're coming from, the nature, the size.

And your response has been to increase rates, so what sort of rate increases you're putting through? And then, Martin, on the capital requirement, the capital requirement in U.S.A. has been stable for a long time. One of your comments earlier (44:05), an indication that now you have sufficient scale within the book that those requirements are going to go up?

A - Neil Patrick Maidment {BIO 5232207 <GO>}

So, on cyber, Eamonn (44:15) – I referred to a number of high-profile breaches that we've all seen in the press. Not all of those were insured, but that has driven the increased demand for, in particular, large risk cyber. And it's also put more caution into the insurance market. So, it's changed people's perception of the required risk-reward (44:35). That's what's driven pricing changes. In some cases, in that large risk segment, it's been a quantum shift in pricing so in the multiples of the existing price.

Our book is more focused in the midmarket, so we have had some opportunities in those large risks. In the midmarket, we've also been able to achieve some pricing strength against that background, but it will be more in the high single-digit-range overall.

A - Martin Lindsay Bride {BIO 15458196 <GO>}

And as far as the U.S. is concerned, our view is we can still support significantly more growth before we would need to alter capital in the U.S. That $107 million is really driven by rating agency requirements to achieve an (45:25) rating but the regulatory capital requirement under the current U.S. regime is much, much lower than that figure. So we're not expecting a change in the capital levels in the U.S. for the foreseeable future.

Q - Thomas Seidl {BIO 17755912 <GO>}

Okay. Thomas Seidl from Bernstein. Three questions, one also on the reserves. You seem to be more confident on reserves now. At the same time, you observed that the U.S. commercialized market is running dry on reserves in particular commercial lands, liability, properties. I wonder how comfortable are you on reserves? And maybe you can also comment on the increase in 2008. Should we expect more specialty reserve increases or is that it basically on this line of business?

Secondly, on cyber, I think you commented on the – at higher demand from large accounts. Should we expect you to engage or do you stick to your policy and not insure anyone bigger than Beazley? And the third is you changed the Chief Investment Officer, anything we should expect in terms of adjustments, strategic asset allocation and so on?

A - Martin Lindsay Bride {BIO 15458196 <GO>}

So I think our view of our reserving balance sheet is that we are setting up initial reserves just as prudently as we ever have. And reserve releases will continue. Now, I think common takes (46:47) is on the market in the U.S. I think at the level of the whole market, that's not the case. And that is certainly a phenomenon that one's observed over their past cycles that at this phase, people start to offer the level of initial reserves. We're quite confident that we haven't changed anything in the way we set our initial reserves so we will not follow that trend, as the sort of central expectation of the future, Thomas.

If I could perhaps deal with last question and then hand over on the cyber question, yeah. Stuart's been within the team for 15 months. He joined Beazley in September 2014. Yes, absolutely. He's got his own views on exactly how investments should be done as Philip Howard. So I'm sure there will be some adjustment, but our central view of our level of risk budget and our portfolio allocation of a relatively significant core portfolio. And then some risk assets alongside that I think is unlikely to change.

A - Neil Patrick Maidment {BIO 5232207 <GO>}

And if I pick up cyber Thomas, the focus in our account and where we've seen the most demand over the last several years has been in the mid-market and the SME part of the portfolio where customers need the service-led proposition that's Beazley Breach Response which is very distinctive. We've always written however some larger customers and we write it on a different policy form. And we write at a different risk reward ratio.

We've seen in 2015 more opportunities to do that and we expect that to continue as well alongside the continued growth of the Breach Response products into 2016. Some of those customers I have to say are very much larger than Beazley.

A - David Andrew Horton {BIO 5697110 <GO>}

Anything else from anybody?

Great. Thank you for joining us today.