Q2 2019 Earnings Call

Company Participants

- Albert A. Benchimol, President and Chief Executive Officer
- Matt Rohrmann, Head of Investor Relations
- Peter Vogt, Chief Financial Officer
- Unidentified Speaker

Other Participants

- Amit Kumar, Analyst
- Brian Meredith, Analyst
- Elyse Greenspan, Analyst
- Jay Cohen, Analyst
- Josh Shanker, Analyst
- Meyer Shields, Analyst

Presentation

Operator

Good day, and welcome to the Q2 2019 AXIS Capital Earnings Call and Webcast. All participants will be in listen-only mode. (Operator Instructions) After today's presentation, there will be an opportunity to ask questions. (Operator Instructions) Please note this event is being recorded.

I would now like to turn the conference over to Mr. Matt Rohrmann, Head of Investor Relations. Please go ahead.

Matt Rohrmann {BIO 15132648 <GO>}

Thank you, Allison. Good morning, ladies and gentlemen. I'm happy to welcome you to our conference call to discuss the financial results for AXIS Capital for the second quarter and period ended at June 30, 2019. Our earnings press release and financial supplement were issued yesterday evening after the market closed. If you like copies, please visit the Investor Information section of our website at axiscapital.com. We've set aside an hour for today's call, which is also available as an audio webcast at the Investor Information section of our website.

With me today on the call are Albert Benchimol, our President and CEO; and Pete Vogt, our CFO.

Before I turn the call over to Albert, I remind everyone that the statements made during this call, including the question-and-answer session, which are not historical facts, may be forward-looking statements. Forward-looking statements involve risks, uncertainties, and assumptions. Actual events or results may differ materially from those projected in the forward-looking statements due to a variety of factors, including the risk factors set forth in AXIS' most recent report on Form 10-K, as well as the additional risks identified in the cautionary note regarding forward-looking statements in our earnings press release issued yesterday evening. We undertake no obligation to update or advise publicly any forward-looking statements.

In addition, this presentation may contain non-GAAP financial measures. For the purposes of this call, we believe the best way to discuss our operating results is on ex-PGAAP basis, which is a better representation of the run rate performance of our business. Reconciliations are included in our earnings press release and financial supplement, which can be found in the Investor Information section of our website.

Now, with that, I'd like to turn the call over to Albert.

Albert A. Benchimol {BIO 2023727 <GO>}

Thank you, Matt. Good morning, everyone, and thank you for joining our call. This was a good quarter for AXIS. One in which we saw strong momentum and positive trends across many areas of our business. Our results provide further validation that we're on the right path. We're taking smart actions to strengthen our business and we're effectively positioning AXIS to be among those companies that will maximize the benefits of a firming insurance and reinsurance marketplace.

There were a number of highlights to this quarter. We, once again, recorded double-digit operating ROE ex-PGAAP. Our diluted book value per share was up 6% for the quarter and 12% year-to-date. We continue to improve our core underwriting margins and we had record net investment income. Our ex-PGAAP ROE in the quarter and in the first half of the year were both the best in the past five years. Importantly, we've improved ROE, while reducing portfolio volatility. We've made substantial reductions to our property exposures and changes to our reinsurance and retro arrangements.

For example, if the events of 2017 were to reoccur this year, our net loss across the enterprise would be lower by more than 25%. Moreover, the full benefits of the initiatives that we've already put in place have yet to be seen. We're still earning run-off premiums that are dragging on our results and we still expect to deliver additional savings between now and the end of 2020.

We're very aware that one or two quarters do not prove a trend. There is inherent volatility in our business. Nevertheless, all data points indicate that our actions are producing tangible results. And we're confident of our ability to deliver ongoing improvements. To be clear, we know that there's more work to be done and we're continuing to look for opportunities to optimize our portfolio, lower volatility, and reduce exposure to less profitable business, even while we grow in attractive lines and markets, but we're highly motivated by the progress to-date.

Encouragingly, we're also seeing an expansion and an acceleration of improved pricing and terms and conditions in our chosen markets. Indeed, AXIS is a leading or highly relevant player in those markets that are seeing the most significant price corrections, with our strong presence at Lloyd's, the US E&S markets, professional lines and global reinsurance, we're very well-positioned to capitalize on these trends.

Beyond improving our underwriting performance, our enterprise-wide transformation program, supporting our ability to implement digital capabilities and enhanced analytics is progressing well. We're confident this will help improve the customer experience including the introduction of new products. Our strategic intent is to become a stronger, faster, more innovative and more profitable customer-focused company, one that's able to deliver differentiated value to our clients and partners in distribution.

Later, during the call, I'll speak on the trends that we're seeing in the marketplace, but for now I'll pass the floor to Pete who will walk us through the second quarter results. Pete?

Peter Vogt {BIO 17059745 <GO>}

Thank you, Albert, and good morning everyone. As Albert noted, this was a good quarter with a number of positive highlights as well as some encouraging trends that speak to the actions we've taken to strengthen our portfolio. During the quarter, we generated good results featuring net income of $166 million and an annualized ROE of 14.3%. On an ex-PGAAP basis, our operating income was $143 million generating an ex-PGAAP annualized operating ROE of 12.3%.

As Albert mentioned, diluted book value per share increased by 6% in the quarter to $55.99. This was principally driven by net income and net unrealized gains partially offset by common dividends. Additional positive highlights for the quarter include the current accident year loss ratio improved 2.7 points, compared to the second quarter of 2018. As both the ex-cat and weather loss ratio and the cat loss ratio improved. In addition, the quarter benefited from record net investment income of $138 million. This included a realized gain of $13 million associated with the sale of an alternative investment.

With respect to the Novae transaction. In the quarter, the net drag on operating income from PGAAP VOBA DAC adjustments was $6 million after tax or approximately $0.07 per share. As we've previously disclosed, we expect the VOBA DAC impact to be minimal from this point forward.

As Matt mentioned, we believe the best way to discuss our results is on an ex-PGAAP basis, which is a better representation of the run rate performance of our business. Accordingly, all my remarks regarding the operating performance will be on an ex-PGAAP basis.

Moving into the details of the consolidated income statement. The current quarter consolidated ex-PGAAP combined ratio was 96.4%, this was essentially flat year-over-year with the solid improvements in the current accident year loss ratio offset by a meaningful reduction in net prior year development. The current accident year loss ratio ex-cat and weather decreased by 1.8 points.

The drivers of the decrease our improved performance driven by underwriting actions taken to strengthen the portfolios, most notably improved loss ratios in both segment property lines and then the reinsurance credit and surety lines, as well as the positive impact rate over trend. Our mid-size loss experience in the quarter was comparable to the same period last year. However, the mix did change substantially as last year our mid-size losses were predominantly in the reinsurance segment, and in this quarter they are predominantly in the insurance segment. We reported net favorable prior year reserve development of $24 million in the quarter of which $22 million came from insurance and $2 million from reinsurance. The year-over-year decrease in favorable prior year reserve development in our reinsurance segment was due largely to a couple of areas. First, we have increased our expectations for Typhoon Jebi to be approximately a $15 billion market event.

Secondly, we experienced some late claim reporting in the reinsurance property line. Notably, our reinsurance North American 2018 cat reserves were unchanged in the quarter. The consolidated ex-PGAAP acquisition cost ratio was 21.9%. The decrease of a point from last year's second quarter was primarily driven by a mix of business.

During the quarter, the consolidated G&A expense ratio of 14.7% increased by eight-tenths of a point compared to the second quarter of 2018. The increase in G&A ratio was driven by a decrease in net premiums earned. For the moment we're comfortable with the trade to a more profitable book temporarily increasing the G&A ratio. We expect this will reverse as we grow earned premiums and a strengthening market and continue with our operational transformation. Regarding the transformation. We remain on schedule to achieve our net savings of $100 million compared to our 2017 run rate by year-end 2020.

Fee income from strategic capital partners was $19 million this quarter compared to $11 million in the prior year quarter. This important part of our business continues to grow well.

Now, we'll move to the segments. Let's begin with insurance. The insurance segment reported a decrease in gross premiums written of $58 million in the second quarter. This was due to a significant increase in property and accident and health that was partially offset by increases in liability and professional lines. In the quarter, the insurance property gross premiums written decreased by $85 million or 25%. A key driver was the termination of a single program which resulted in a decline of $65 million, and as we discussed in previous quarters, we have non-renewed other property business where we continue to hold our pricing discipline.

In addition, in accident and health, we terminated a program that decreased the gross premiums written by $38 million. Offsetting the decrease in property and A&H, we saw favorable new business opportunities in liability, especially in US excess casualty and US primary casualty as well as in personal lines, most notably cyber.

From a net premium written perspective, the insurance segment is essentially flat year-over-year as the terminated property program I mentioned earlier had significant quota share reinsurance associated with it.

The insurance ex-PGAAP combined ratio was 98.3 which is more than a point higher than the same period last year. The increase in the combined ratio was due to a 0.5 point increase in the insurance segment's current accident year loss ratio ex-cat and weather to 58.7. The increase was driven by mid-size losses in marine and in credit and political risk.

This is an increase of 3.5 points from the second quarter of 2018. The increase in mid-size losses was partially offset by a 2 point improvement in the attritional loss ratio, excluding mid-size losses. This was driven by a number of factors including better attritional property loss experience and favorable rate and trend. This quarter pretax cat and weather-related losses were $14 million primarily attributable to weather-related events compared to 23 million in the same period in 2018.

The insurance segment's ex-PGAAP acquisition cost ratio was 21.3, which is a point decrease from the prior period of 22.3. The decrease was driven by changes in mix of business. During the quarter, the G&A expense ratio increased by 1.8 points compared to the second quarter of 2018. This was largely driven by the decrease in net premiums earned.

Now, let's move on to the reinsurance segment. During the quarter we saw a very solid results within our reinsurance business. The segment reported an increase in gross premiums written of $55 million. This increase principally came from catastrophe and liability lines the increase in catastrophe business was led by growth in Japan where we saw a materially improved pricing in wind exposed accounts. And we also saw growth in our North American cat book driven by better market conditions. These increases were partially offset by premium adjustments, timing and non-renewals in motor, professional lines, and property, largely related to the underperforming business.

On a net written premium basis the reinsurance segment grew 19%. The higher net growth is attributable to timing, and when adjusted, the net growth is consistent with the gross growth.

The reinsurance ex-PGAAP combined ratio was 89.1% which is almost 2 points lower than the same period last year. The improvement in reinsurance combined ratio was due to a 5 point decrease in the reinsurance segment current accident year loss ratio ex-cat and weather to 60.5%. This was driven by a decrease in mid-size loss experience in property and engineering and the reduction in attritional loss experience due to a combination of underwriting actions favorable rate and trend and some favorable mix. Pre-tax catastrophe and weather-related losses were $11 million in the quarter. This was primarily attributable to weather-related events in the quarter compared to $15 million during the same period of 2018. The reinsurance segment acquisition cost ratio of 22.3% was almost a point lower than last year, principally due to mix.

During the quarter, the G&A expense ratio decreased by six-tenths of a point compared to the second quarter of 2018, mainly due to additional fees from strategic capital partners. Net investment income of $138 million for the quarter increased $28 million or 25% from $110 million in the second quarter of 2018. This was due to an increase in income from fixed income investments that was attributable to increased rates as well as larger investment base, together with a $13 million investment gain associated with the sale of an alternative investment that I mentioned in my opening remarks. Our current book yield is 3% and our new money yield is 2.7%. The duration of our portfolio continues to be approximately three years.

With respect to capital actions. On April 1, we redeemed a $250 million senior note. And in June, we raised $300 million in funds at favorable terms. We intend to use the proceeds from the June notes for the partial repayment of our $500 million of senior notes maturing in June of 2020. That summarizes our second quarter results.

With that, I'll turn the call back over to Albert.

Albert A. Benchimol {BIO 2023727 <GO>}

Thank you, Pete. Let's discuss market trends in our positioning and then we'll open the call for questions. This period of price firming is now in its eighth quarter, having started in the fourth quarter of 2017. And we're starting to get the benefit of compound rate increases. As you've heard from other market participants, AXIS is also seeing both an acceleration of the pace of increases and an expansion into more lines and markets.

With insurance, rate increased more than 7% in the quarter, compared to 4% in the first quarter of this year. In the second quarter, 65% of our book had increases of 1% or more compared to 45% in the first quarter.

Moving on to market specific data. In our US division, average rate increases were more than 11%, an improvement from 9% this quarter. The strongest increases came in excess casualty where rates were up more than 15% while E&S property came in at close to 15%.

US primary casualty was up more than 6%, and for the second straight quarter, we generated rate increases of close to 5% within our US programs business. Overall, 92% of the US book renewed flat to up in the quarter.

Within our North American professional lines division, rates increased more than 2% on average. Our commercial management solutions unit saw increases of more than 9% and we also saw a nearly 5% increase in our Canadian specialty insurance business.

Across small accounts, however, we generally had more muted pricing action and we did see a very small decline in our profitable AXIS pro business. Nevertheless, 84% of the premium in this division renewed flat to up in the quarter.

In our London-based international insurance division our average rate increases were more than doubled at over 7% in this quarter versus 3% in the prior quarter. We saw double-digit increasing in our professional and casualty lines, renewable energy and direct and facultative property as well as mid to high single-digit increases in marine US property facilities and aviation.

In all, 97% of the international book renewed flat or up reflecting the comprehensive nature of change at Lloyd's and at the London market. We give the leadership of Lloyd's all the credit for initiating this broad-based improvement with the launch of the Decile 10 program last year. But what's encouraging is that management teams across the market have picked up the baton and appear to be seriously committed to driving profitability.

Given these developments, our strategic acquisition of Novae to accelerate our leadership at Lloyd's may prove to be very well timed. As of the spring, we now have fully integrated Novae into our business. Within a year and a half time, we brought the businesses together and we're today operating as one company. At the start of this year, we renewed the entire book into AXIS Syndicate 1686. Additionally, this past March, we brought all our London teams under one roof at the newly constructed scalpel building located directly across from Lloyd's.

In summary, for the second consecutive quarter, 92% of the total insurance book renewed flat or up. But price increases alone understate the true pace of progress in profitability. Other factors include the elimination of unattractive business which has a reasonably quick discovery period as well as improved terms and conditions. We're generally slower to recognize the benefits of improved terms and conditions as they're not always easily quantifiable, but I am confident that these will ultimately show up in our earnings. Another observation I'd like to make is that was a firmer market, our disciplined does not appear to be causing us any backlash. Our insurance retention ratios are within a couple of points of what they were last year. However, our new business volume was up over 50% compared to what it was in last year's second quarter. As I noted earlier, we believe we're very well positioned to take advantage of opportunities in this market.

Moving to reinsurance, we had a strong quarter that was highlighted by continued improvement in pricing. Looking holistically at our reinsurance book, more than 60% of the business is quota share. So generally, we'll be getting at least the same improvements that we're seeing in the primary markets, and perhaps better if we do some of the ceding commissions. Additionally, we're also seeing improved pricing in our excess of loss business.

During the quarter, we had a positive spring renewal season in both our Asia-Pacific and North America divisions. As Pete noted, we saw particularly strong growth in Japan where premiums more than doubled at the April 1 renewals. This was due to a combination of better pricing, new business and share gains. Other than Japan and Australia, the Rest of Asia Pacific markets remained flat to very modestly down.

In our North American division, we're benefiting from the underlying improvements we're seeing in most lines. Accident and health is an exception. There, we're seeing some modest pressure on short-term medical and life catastrophe business. The big item of interest in the second quarter were the June 1 renewals, which as always, were dominated by Florida placements. Continued loss emergence in Florida from Irma and Michael were a significant factor with large cat players demanding better pricing.

Rates were up 10% to 20% and even more for loss impacted and lower rate on line layers. We use the opportunity to improve both the profitability and the balance of our book. We increased gross cat premiums by almost 30% at June 1. But this growth was disproportionately out of Florida. Limits exposed to Florida only insurers now represent less than 50% of the June renewal book.

Let's move on to our Global Markets division, which covers global specialty such as agriculture, aviation, credit and surety, engineering, marine and mortgage business. I would characterize these markets as being in the early stages of recovery. Generally, all of them are seeing some sort of pricing increase with the strongest in aviation, marine and engineering given recent losses. But not every market is behaving similarly. The European, Middle East, Africa and Latin American markets, which do not have much volume in the second quarter, have been slow to move on pricing. An exception is casualty, which is up low-single digits in Europe and in the high single-digit, low double-digit range in London.

Separately at the July 1 renewals, which cover multiple geographies but represent less than 10% of our annual gross reinsurance premium, we saw a continuation of the trends that I just enumerated. Catastrophe business is not a big part of our July 1 renewals, but nevertheless, we observe continued disciplined. This was evidenced by positive rate momentum with many programs being placed very late in the renewal cycle.

Cat pricing was flat to up 10% depending on the region and loss experience. We did not grow our cat business of July 1, preferring to take our exposure at the June 1 renewals. We also use the opportunity to further optimize our portfolio and cut back on some property treaties.

The net of it all is that our July 1 renewals were down a bit under 10% of expiring premiums off a small base.

So, overall, reinsurance markets are also recovering with a few regional differences. However, given all the action we've seen to date, we hope for improvement that will be more broad based at the next January 1 renewals.

There's been much talk about what's driving recent price action and how long they may last. Our perspective is that this is a loss-driven correction. We believe the industry is appropriately reacting to loss trends that have deteriorated over the past few years and that have exacerbated the negative impact of several years of price declines.

Indeed, it's our view that with, even with the increases that we've seen in the last two years, many lines of business are still not at acceptable pricing. We believe the price action will continue into 2020 and perhaps longer for a number of reasons including the fact that these more recent loss trends are unlikely to dissipate in the near future.

Moreover, as a result of these factors, it's unlikely that carriers will be able to benefit from reserve releases as they have in the past. Current earnings will be paramount. But I also caution that this is not a hard market where almost everything is priced adequately. This is an underwriters market were selection and portfolio construction will be important differentiating factors. We believe that the changes that we've made to our company in the last few years have prepared us well for this type of market.

Lastly, I'd like to cover the Capital Markets participation in our industry. There is no doubt that it's been stressed this year, given trapped capital and redemptions from dissatisfied investors. Its actions have caused reinsurers to think more critically about the retro strategies and the risk-adjusted returns of their business, which has contributed to some of the corrections we just discussed. I think this was a good development, as this industry for too long acted as if third-party capital was unlimited, cheap and unconcerned with losses. The developments this year are an indication that ILS and third-party capital will be a disciplined participant in our industry, prepared to put large sums of money to work but also requiring adequate risk-adjusted returns. That's a good thing for our industry and for AXIS.

In that regard, I'm proud that AXIS is one of the very small number of companies that successfully raised more money this year and from a broader array of investors. That has allowed us to write more gross premium on their behalf and generate attractive fees in the process. Our fees from strategic partnerships were up 59% in the first half of this year to $39 million. This is great progress and we're well on our way to making fee business an important and attractive part of our revenues and profit streams.

So to conclude, it's been a good quarter and the progress that we're making speaks to the strength of our strategy and the disciplined actions that we're taking. Our pathway to profitable growth is looking good. We have the best portfolio we've had in many years. And while there's more that we must do, AXIS is well-positioned to reap the benefits of an increasingly attractive market.

And, now, let's please open the line for questions.

Questions And Answers

Operator

Thank you. We will now begin the question-and-answer session. (Operator Instructions) Our first question today will come from Amit Kumar of Buckingham Research. Please go ahead.

Q - Amit Kumar {BIO 15025799 <GO>}

Thanks, and good morning. A few questions. Maybe, I'll start with the insurance and then re-queue. Going back to the discussion on the underlying loss ratio of 58.7%, you mentioned 3.5 points was from mid-size losses, if I exclude that I get into on a 56% or change. Is that the right way to think about it? Or how should we think about additional headroom for improvement on the underlying loss ratio as the book gets rebalanced further?

A - Peter Vogt {BIO 17059745 <GO>}

Yeah. Amit, this is Pete. I'll handle that. Yeah, the 3.5 was actually the increase over last year, the number of large losses or mid-size losses is actually higher than that, but it was skewed this quarter. It was higher than we normally see. But if I take the book and I think about an adjustment for that with regard to mid-size losses, as we've talked to you about the canceled business that we actually have on the books, that hurt us in the quarter by about 2 points. And so, if I think about where we are, and then adjust for some of the canceled business, I continue to think that the trend does get us back down to where we think we should be in insurance, which would be in that mid-50s range or 55-ish for that ex-cat loss ratio on a go-forward.

A - Albert A. Benchimol {BIO 2023727 <GO>}

But that would be probably without some of the rate over trend that we have writing in '19 and will be earning in '20.

A - Peter Vogt {BIO 17059745 <GO>}

Yes. And that would just be what we expect to see in the second half of 2018 view. Again, as Albert has mentioned, the pricing we're seeing currently in insurance is definitely in excess of trend, and so we expect that to continue to improve as we think about 2020.

Q - Amit Kumar {BIO 15025799 <GO>}

So let's talk about that. On the last call, I think you had mentioned in response to a few questions that rate over trend, I think, was 1 percentage or I guess 100 basis points, clearly, pricing has accelerated, but do you get the sense that we are at the point where we should expand the thought process or should we give it a few more quarters.

A - Peter Vogt {BIO 17059745 <GO>}

I'm sorry. Are we at the point where we should expand?

A - Matt Rohrmann {BIO 15132648 <GO>}

The thought process.

Q - Amit Kumar {BIO 15025799 <GO>}

The rate over loss trend discussion, I think it was -- that delta was 100 basis points on the last conference call.

A - Albert A. Benchimol {BIO 2023727 <GO>}

I think, that's right. If you look at where we are and you look at rate over trend and its contribution to where we were, in the first half of this year, we probably gave it a benefit of about 50, 60 basis points and that reflects slightly higher loss ratios that we put up in liability and professional lines to reflect some of these losses, so we wanted to make sure that we were fully reflective of some of these trends that I've just discussed. But we're still seeing well over half a point of rate over trend in the earned premium that we're running through the portfolio this year. I think what's more interesting is that we should be north of 200 basis points of rate over trend if you look at the pricing that we're getting in the second half -- sorry, in the second quarter. So, obviously, we would expect the improvement to be -- that is driven by rate over trend to accelerate in '20 over the improvement that we've had in '19.

Q - Amit Kumar {BIO 15025799 <GO>}

Got it. Good color. The only question and I'll stop after this is, there has been this discussion on social inflation in the jury awards litigation trends, Albert, did you have a view on that and has that view changed over, let's say, I don't know, from 2018 to 2019 based on some of the worsening, if you will, if I can use that word in the loss trends.

A - Albert A. Benchimol {BIO 2023727 <GO>}

So our views on this have actually emerged and evolved actually over the last six years. And let me give you a little bit about that. So we were, as you know, and I've referred to it before 2013, 2014, we were dissatisfied with what we were seeing in our own primary D&O book.

And as you'll recall at the time, we made some corrections and significantly reduced our primary D&O business. On the public side, we increased our attachment points much higher and reduced our limits. As a result of that, although you've been seeing deterioration in the D&O markets over the last two, three years, we've been protected, if you would, from that trend, because we've been higher up and frankly not writing a lot of public D&O.

Another area where that is in the same color, and, again, I've spoken to that in the past is on our excess casualty book. As you know, we have been concerned that excess casualty above $1 million or above $2 million has been the same levels for the last 20 years. And with the inflation that we're talking about, we were seeing a lot more judgments and claims coming into the lower layers of excess making that really a working layer. And so, we've done two things as a result of that. We have both reduced our growth ambitions in that area, but, importantly, increased our attachment points and shortened our limits in our liability book and, frankly, we're very pleased with the trends that we're seeing in our excess casualty book.

And then, finally, I would say, we've been concerned for some time with regard to auto liability, and that is a very small part of our book and very highly reinsured. So, yes, we have observed a slight acceleration in the last couple of years in the markets, but as far as our book is concerned we've been working hard to reduce our exposures to those areas over the last few years.

Q - Amit Kumar {BIO 15025799 <GO>}

That's very helpful. I'll stop here. Thanks for the answers. And I will re-queue. Thanks.

A - Peter Vogt {BIO 17059745 <GO>}

Thanks.

Operator

The next question will come from Brian Meredith of UBS. Please go ahead.

Q - Brian Meredith {BIO 3108204 <GO>}

Thanks. A couple of quick ones here. First, I'm just curious, any impact from the recent rate change on Ogden on (technical difficulty) what your loss ratios could look like going forward?

A - Albert A. Benchimol {BIO 2023727 <GO>}

Yes, and no. I think that the industry, historically, had assumed that the rates would be corrected to a higher rate and, therefore, incorporated a lot of their pricing and assumption that the rate would get back in line. I think that that has now been proved to be a false assumption. And my expectations, you're actually going to see pricing increase in excess motor in the UK as a result of that.

From our perspective in terms of reserves, frankly, it's a lot of moving pieces, right. As I told you, we've been reserving it at minus 0.75 all along, but there's not much left, we've been paying off the claims from '17 and prior. So there is a little bit of benefit, no doubt, but frankly in the context of a $12 billion reserve base, it's a rounding error.

Q - Brian Meredith {BIO 3108204 <GO>}

Great. Now, but I'm just curious, could you give us your thoughts on ability or kind of outlook on putting more capital to work at Lloyd's?

A - Albert A. Benchimol {BIO 2023727 <GO>}

Well, our view on putting capital to work at Lloyd's is simply a function of the attractiveness of that business versus the other opportunities that we have. A big part of what you've been seeing in the reduction in our insurance volume has a lot to do with the fact that Lloyd's, as we all recognize, was challenged. It required us to make some corrections to the book of business. Peter made reference to the fact that we canceled some property business. A lot of that was associated with the SPA, so we didn't see any net impact. But I will tell you that I have told our underwriters and I'm happy to repeat to them on this call, if the business is good we want to write more of it. And so, we would be very happy to grow both at Lloyd's and in the US and other markets if we find that the returns are attractive.

Q - Brian Meredith {BIO 3108204 <GO>}

Great. And then I'm just curious, I know you mentioned rate activity it good. How does your US E&S business kind of growth look like on a premium basis versus what's going on overseas are you seeing some good with that at this point?

A - Albert A. Benchimol {BIO 2023727 <GO>}

The answer is yes and no. We are not growing our property book, it's down actually year-over-year in the first half of '19, specifically, as a result of the actions that we've taken to cancel a number of programs, a number of facilities and binders and take corrective action to improve our property results and reduce our portfolio volatility. And in fact, Pete mentioned the fact that the property loss ratios have improved, that's a good thing. I've made reference to the fact that our portfolio volatility is reducing, that's a good thing. And so, I think we've right-sized our property portfolio.

And now as we think about growing the property portfolio, it's really about growing it within the context of a growing diversified balanced consolidated portfolio. We are not in favor of unbalancing our portfolio. We want to grow property but in the context of a balanced portfolio.

Q - Brian Meredith {BIO 3108204 <GO>}

Makes a lot of sense. And then, Albert, my last question for you is, you talked about great numbers right now with rate in excess of trend, but when we think about kind of going forward, and kind of for modeling purposes, think about it, given what's going on with trend right now and it sounds like some caution with respect to what's going on with trend, should we really expect that much improvement in your underlying combined ratios? Are you going to be a little more cautious in kind of how you book those numbers given just some uncertainty there?

A - Albert A. Benchimol {BIO 2023727 <GO>}

So, again, two parts to your answer.

Q - Brian Meredith {BIO 3108204 <GO>}

Yeah.

A - Albert A. Benchimol {BIO 2023727 <GO>}

Absolutely, we will be cautious in booking our loss ratios to make sure that we properly reflect trends. The second part of your questions. I'm very confident that we should be able to get at least 200 basis points of rate over trend next year.

Q - Brian Meredith {BIO 3108204 <GO>}

Yeah. That's great. Thank you.

FINAL

Bloomberg Transcript

Operator

Our next question will come from Jay Cohen of Bank of America Securities. Please go ahead.

Q - Jay Cohen {BIO 1498813 <GO>}

Yes, thank you. I'm wondering, Albert, in addition price, you talked about improvements in terms and conditions and I'm hoping you can give us some examples of that.

A - Albert A. Benchimol {BIO 2023727 <GO>}

Sure, the easiest one is increased attachment points and sublimits although sometimes that's incorporated in pricing, but generally in terms of that, it's limits to certain number of days or are increasing in the number of days as required for BI. It's sub-limiting a number of different loss classes. It's compelling groups to be repaired rather than replaced. There are a number of different factors that you are incorporating in the policies, and it's almost impossible to turn around and say, well that's worth a 0.1 or a 0.2 on the loss ratio. But what happens is that every -- not -- I wouldn't say every, but a large number of contracts get to incorporate more restrictive conditions such that the potential loss is reduced.

Q - Jay Cohen {BIO 1498813 <GO>}

Got it. Now, that makes sense. That's helpful. And I guess on the insurance side, there is a lot of moving pieces, would you expect to see your net premiums grow next year in insurance everything that you see in the market?

A - Albert A. Benchimol {BIO 2023727 <GO>}

I would hope so. Yes. Because, in fact, if you even if you look at this year, if you look at our net written premiums they're essentially flat. And so, we've been able to reduce the property book and take some corrective action in a number of areas, all the while, we've been able to grow in other lines that we found attractive. So we're already growing in those lines of business that we find attractive. It's my belief that the bulk of our corrective actions have already been taken. That doesn't mean that there aren't a few things that we can do, but the bulk of our corrective actions have already been taken. Therefore, I think the growth will shine through and if these conditions continue, if we're seeing these kinds of pricing trends continue, that would make us feel that we're getting into attractive territory, we would absolutely want to grow that book.

Q - Jay Cohen {BIO 1498813 <GO>}

Helpful answers as usual. Thank you.

A - Albert A. Benchimol {BIO 2023727 <GO>}

Welcome.

Operator

The next question will come from Meyer Shields of KBW. Please go ahead.

Q - Meyer Shields {BIO 4281064 <GO>}

Good morning. Albert, one question on property. I guess, I understand the need for balance and the reduction of volatility, but I guess I would have expected some, at least, offsetting growth from pricing. What am I missing there?

A - Albert A. Benchimol {BIO 2023727 <GO>}

No, I think it's -- I think what you're seeing is an even larger reduction in volatility and in limits. As I've said to you, we felt that we have made a lot of good progress in our book over the last several years. And what '17 and '18 showed was, unfortunately, that progress was not coming through in a highly volatile property loss environment. And so, we determined that we wanted to rebalance our book.

As I said, I think we've made those changes now and you're absolutely correct, we ought to be able to see some improvement in terms of rates on the property book that should drive top line. What I was referring to is that when it comes to exposures, I would want to make sure that those exposures grow in balance with the rest of the portfolio. So thank you for allowing me to correct that.

Q - Meyer Shields {BIO 4281064 <GO>}

Always happy to help. A question, I guess --

A - Peter Vogt {BIO 17059745 <GO>}

I would just say, with regard to property, if you're just looking at growth, Meyer, I just want to remind you that we did exit our relationship with Securis. With that said, Syndicate 61129. And that really is weighing on the results this year on the growth side, and that was 90% reinsured back to them. So I would look more on a net basis. And on a net basis, property is down just into the low double-digits year-over-year. And so, we're still feeling good about, we've made the corrective actions. But, obviously, on a growth side, it looks like a bigger drop than we're actually feeling on the net.

Q - Meyer Shields {BIO 4281064 <GO>}

Okay. Now, that's helpful. And that makes a lot of sense. I was hoping you could talk a little bit about reinsurance, is there any way of quantifying the one-time impact of reserve charges for Jebi and the late reported claims, so we can see the, I guess, what I would call, underlying reserve releases?

A - Peter Vogt {BIO 17059745 <GO>}

Yes, I mean, we know what that is. We've move Jebi up to about a $15 billion market event and that cost us about $10 million in the quarter, Meyer. And on the late reported property claims, it was really coming from one cedent and it was through a number of accident years, not really in '18 accident year. So we're digging into those claims. But right now, we've posted them all. We got the claims border out and that was actually $20 million in the quarter.

Q - Meyer Shields {BIO 4281064 <GO>}

Okay. So there was a $30 million offsets to --

A - Peter Vogt {BIO 17059745 <GO>}

So that really -- that was a real driver down of the reinsurance PYD. Other than that, reinsurance prior period development would have been more on a normalized track.

Q - Meyer Shields {BIO 4281064 <GO>}

Perfect. Thank you so much.

Operator

The next question will come from Elyse Greenspan of Wells Fargo. Please go ahead.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Hi, good morning. My first question is on the insurance side, Pete, I believe you said that there was about two points from some of the run-off business coming through with the loss ratio in the quarter, could you give us a sense of what the drag on margins could be in the third and fourth quarter and is the expectation that that would have no impact on the 2020 margins within insurance?

A - Peter Vogt {BIO 17059745 <GO>}

Yeah, Elyse, I would say right now the UPR on that is coming down. If you recall in the first quarter, that book really behaved itself well. But it was two points in this quarter. As I go into 2020, we still have, we'll have a little bit of an impact but it will be very immaterial because we'll still have to earn some premium from some of the MGA relationships we got out of. But it is coming down and I would expect next year's drag to be de minimis because premium should be pretty low.

Q - Elyse Greenspan {BIO 17263315 <GO>}

And what about the third and fourth quarter of this year?

A - Peter Vogt {BIO 17059745 <GO>}

At that point, it's hard to tell because it's a bit of a spiky book. So I really wouldn't want to say either way. But right now, I'd say the underlying fundamentals are that premium is coming down. As I said, it hurt us by two points in this particular quarter. But as you're thinking about running it down to zero, you can use any methodology you'd like. But it is a bit as I'd say one of the reasons we're getting rid of it is it's a bit of a volatile book and it was -- didn't hurt us in the first quarter; two points this quarter.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay, that's helpful. And then, Albert, in your upgrading commentary, when you gave us the rates, are those just on renewals? And then I'd be interested, you did point to some pretty substantial growth within your insurance business in the quarter, what kind of rates are you seeing on new as compared to some of the renewal rates that you gave us in your commentary?

A - Albert A. Benchimol {BIO 2023727 <GO>}

Thank you, Elyse. We don't have as much of a system in place on new business, because obviously we don't have the old pricing in, but we do take a look at what the expiring pricing is when we get the submission. And I would say that, anecdotally, it is our belief that we are getting much better pricing on our new business than we're getting on our renewal business, and we do keep that but it's more, it's more on a pad of paper than it is on a computer. So it's an anecdotal reflection.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay, that's helpful. And then, you guys, you mentioned the two-point the delta that you see between rate and trend into 2020. And, Albert, you also mentioned that you think that this cycle has legs, right, prices should continue at least into 2020. I guess, what I'm trying to connect with the thought is, I mean, you guys have not really seen loss costs, it sounds like moved so much on your book and there is a decent spread between price and trend. So if loss cost isn't necessarily going to spike so much, what's going to be that catalyst that we're going to keep seeing prices go up or is it more just that there are some folks that are under reserved and that's going to add legs to what's going on here?

A - Albert A. Benchimol {BIO 2023727 <GO>}

Right. So a couple of things to be clear. So when I talked about this 200 basis points, a, I'm absolutely talking about insurance not reinsurance rates; we're talking about insurance rates, number one. And number two, that presumes that we're going to continue to get the 7% plus pricing increases that we've exhibited here, right, this, and my belief is that it will continue.

Now, with regards to what gives me belief that it will continue into 2020 and perhaps later is that, as I mentioned earlier, there are still a number of lines that even with the increases that we're seeing in '19, on a written basis, we still don't think it's profitable or not profitable but not adequately profitable. And so I think that there are a number of lines that will not be adequately priced unless we sustain these pricing increases into 2020.

With regard to some of the loss trends that we've discussed, I wasn't saying that these loss trends were not happening. What I was saying was that they weren't happening as much in our book because of the actions that we've taken over the last five years, but we certainly agree with what we are hearing and reading from others with regard to the substantial increases in D&O loss costs and liability loss cost and so on and so forth. But given the way we've positioned our portfolio in the last five years, we've been -- we've benefited from having less of a negative impact.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay, that's helpful. And then if I can squeeze in one last numbers question. Pete, I believe last quarter you had said on the ex-PGAAP acquisition cost ratio would run around

23 for the balance of the year. It was a little bit better this quarter. Have your forward expectations for the back half of the year changed?

A - Peter Vogt {BIO 17059745 <GO>}

Yes, actually my, I would say my forward expectations have changed a bit, Elyse. I've been saying 23 since we've been talking about PGAAP for the last six quarters, what I would tell you is some of the mix changes we've seen on the books we've actually got rid of some of the more the MGA business, which is a little bit more expensive on the acquisition costs. And even in this market, we've seen some of our variable costs come down a little bit. So as Albert is talking about rate increases, we're also seeing some better terms and conditions with our trading partners. So I would think it's going to come down a little bit -- I can't see getting below 22, Elyse, but somewhere in that 22 to 23 range.

Q - Elyse Greenspan {BIO 17263315 <GO>}

That's very helpful. Thank you, guys. I appreciate the color.

A - Albert A. Benchimol {BIO 2023727 <GO>}

Elyse, I hadn't quite finished my answer on the legs of this rate. So let me just add a little bit more. I think the -- there are a number of other factors. So we talked about adequacy, which I think is not there in a lot of lines. I did mention as I've said before that this industry is unlikely to benefit from the same kind of a contribution to income from PYD. And obviously, I think that will drive increased demands for current year income. I would say that as long as interest rates stay low for longer and that will be another driver of the issue. Again, these large losses that we've seen in marine this quarter, some of the aviation losses that we've seen, there's a lot of stuff happening. I think there's still a lot of loss events spiky loss events that should drive some.

I could tell you that at Lloyd's, I fully expect that the planning process that is going to go through Lloyd's this year is going to require request demand ongoing continued discipline. So I think there's just a lot of factors that make me feel comfortable that, obviously, I can't guarantee it, but it makes me feel comfortable that we should see this into 2020 and perhaps and perhaps longer.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay, thanks. Albert. I appreciate the follow up.

A - Albert A. Benchimol {BIO 2023727 <GO>}

No problem.

Operator

(Operator Instruction) Our next question will come from Josh Shanker of Deutsche Bank. Please go ahead.

Q - Josh Shanker {BIO 5292022 <GO>}

Yeah. Good morning, everyone, and congratulations on the quarter.

A - Albert A. Benchimol {BIO 2023727 <GO>}

Thank you.

Q - Josh Shanker {BIO 5292022 <GO>}

I know you, for competitive reasons, you don't want to give too much away but I'm hoping I can get as much out of you as I can. You wrote a decent amount of operating cat in the quarter and you said that, obviously, improvement reinsurance margins were a bit related to business mix. I was wondering if you could put any numbers to how much putting on cat business and non-cat quarter helped the numbers and reinsurance. And on the other side, on insurance, the non-renewal of the Accident & Health book, I'm wondering if you can talk about that a bit more and talk about what the margins on this business were, whether you want to non-renew that book and just give us some color as to how that impacted the margin overall.

A - Peter Vogt {BIO 17059745 <GO>}

So, probably, the best way to look at this thing is one of the things that we look at when we worked through our loss bridges and our analysis, we of course, look at the mix impact and we've talked about the mix impact for quite some time. And I would argue that as we were earning less property premium on the insurance side, the mix impact was actually modest adverse.

Yes, it was.

A - Albert A. Benchimol {BIO 2023727 <GO>}

You have the numbers Pete, why don't you --

A - Peter Vogt {BIO 17059745 <GO>}

Yeah, I do. So, Josh, if specifically in reinsurance, with the fact that we've written a little bit more cat, I'd say the mix change has actually helped the loss ratio by about at 0.5.

A - Unidentified Speaker

I'm sorry. Just cut-off the second you said that, that was my phone.

A - Peter Vogt {BIO 17059745 <GO>}

I'm sorry, on the reinsurance side the mix changes by writing a little bit more cat business overall for the quarter helped it by about 0.5 point.

Q - Josh Shanker {BIO 5292022 <GO>}

Okay.

A - Peter Vogt {BIO 17059745 <GO>}

And the flip side, on the insurance side, because we've written less property and quite honestly written more liability and professional lines, the insurance side actually got hurt by about 0.5 point on mix.

Q - Josh Shanker {BIO 5292022 <GO>}

Yes. And the Accident & Health, I mean, that's a sort of something that's differentiated you guys over the years from a number of your competitors. And I guess one large participant and you decided to part ways, can you talk about that a little bit?

A - Albert A. Benchimol {BIO 2023727 <GO>}

Yeah. It was simply the fact that there was a -- we were hoping to see more progress in the direction of that program, and at the end of the day, we weren't seeing it and we agreed to part ways.

Q - Josh Shanker {BIO 5292022 <GO>}

Okay. And mix impact, did that have much of an impact at all on the underwriting ratios?

A - Albert A. Benchimol {BIO 2023727 <GO>}

Not really. No, and I think long term obviously, the reason we're doing this is because we think that it will as we run off this business, have a better -- have a positive impact on our loss ratios.

Q - Josh Shanker {BIO 5292022 <GO>}

Okay.

A - Albert A. Benchimol {BIO 2023727 <GO>}

There's nothing in the quarter.

A - Peter Vogt {BIO 17059745 <GO>}

Yeah, nothing in the quarter.

Q - Josh Shanker {BIO 5292022 <GO>}

Okay. Well, thank you for the answers and best of luck with the remainder of the year in 2020.

A - Albert A. Benchimol {BIO 2023727 <GO>}

Thanks, Josh.

Operator

Ladies and gentlemen, this will conclude our question-and-answer session. At this time, I'd like to turn the conference back over to Albert Benchimol for his closing remarks.

A - Albert A. Benchimol {BIO 2023727 <GO>}

Thank you, operator. And thank you to all our participants for your time this morning. As I said at the beginning of today's call, this has been a good quarter. And our operating income of $165 million, well, that's been the best in five years. We recognize that our work is far from finished. We know where we need to focus. And our team is working very hard to continue executing on our strategy. And because of that, I must take a moment to say how proud and appreciative I am of our team. So, to all the AXIS colleagues who are listening on this call, thank you for your hard work and for all that you're doing to make us a stronger company. And to everybody else, thank you for joining us and we look forward to reporting on our further progress. Have a good day.

Operator

The conference has now concluded. We thank you for attending today's presentation. You may now disconnect your lines.