Q1 2014 Earnings Call

Company Participants

- Alex Maloney, Group Chief Executive Officer & Chief Executive Officer-Lancashire Insurance Company (UK) Limited
- Elaine Whelan, Group Chief Financial Officer & Chief Executive Officer-Lancashire Insurance Company Limited
- Paul Gregory, Group Chief Underwriting Officer & Chief Underwriting Officer
- Peter David Scales, Chief Executive Officer
- Unverified Participant

Other Participants

- Andy D. Broadfield, Analyst
- Ben Cohen, Analyst
- Chris D. Hitchings, Analyst
- Maciej K. Wasilewicz, Analyst
- Thomas Fossard, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good afternoon and welcome to the Lancashire Holdings Q1 2014 Results Call. Throughout the call, all participants will be in a listen-only mode, and afterwards, there'll be a question-and-answer session. Just to remind you, this conference call is being recorded.

Today, I'm pleased to present Alex Maloney, Group CEO. Please begin your meeting.

Alex Maloney {BIO 16314494 <GO>}

Okay. Thank you. Good afternoon, ladies and gentlemen. Thank you for dialing in. I'm joined by following colleagues. We have Elaine Whelan, our Chief Financial Officer; Paul Gregory, our Chief Underwriting Officer; and Peter Scales, our Cathedral CEO; and Darren Redhead, our Kinesis CEO. And we also have Denise O'Donoghue, who's our Group Head of Investments.

As I've already said elsewhere, a lot has changed for the Lancashire Group during the first quarter of 2014. Kinesis has been launched very successfully. We've integrated well with our new colleagues from Cathedral. We've expanded the Lancashire lines into Syndicate 3010 in Lloyd's; and we've completed building out our Bermuda Property Cat XL portfolio.

We've also added a modest allocation of risk assets to our investment portfolio to help balance our interest rate risk, and we're progressing along the road to Solvency II compliance.

In the wider market, it is clear that retained earnings and new capital are outstripping any increase in demand in the reinsurance and retrocession world. And this, in turn, is displacing capital into the direct insurance lines. But the barriers to entry in direct business are much stronger than in the highly commoditized world of property retrocession.

Our energy, D&F, marine, and aviation policies are intricate and detailed and require a real level of expertise, not just in pricing, but in the adjustment of claims, too. Clients and brokers respect this and want to know that their insurer is an expert in their field, with a track record in setting premiums and paying claims.

The Cathedral US property Cat XL book is a prime example of relationship-driven business, where the performance over 20 years has more than ensured enduring customer loyalty. There have been some indications, as well, that some of the broker facilities we have seen are failing to gain new traction and some are even losing their existing support.

In terms of people, obviously, the big news is retirement of our founder, Richard Brindle, which took effect from yesterday. Richard helped to build a remarkable franchise at Lancashire, which has led its peer group in numerous metrics across the last eight years.

His insistence on process and systems has ensured that I and the rest of the management team, have a smooth path to take over the running of the group. So we sincerely thank Richard for his vision and energy, but I am utterly confident that we have the right team to build on his success to-date.

I now hand over to Elaine Whelan.

Paul Gregory {BIO 16314515 <GO>}

Paul Gregory.

Alex Maloney {BIO 16314494 <GO>}

Sorry, Paul Gregory.

Paul Gregory {BIO 16314515 <GO>}

Thanks, Alex. We're undoubtedly in a challenging market, but the strength of our franchise across the three pillars of our business is helping us to weather these challenges, defend our core portfolio, and even grow in some selected areas.

Lancashire, Cathedral and Kinesis add value through their ability to deploy significant amounts of capacity to lead important contracts, and to fairly and promptly adjust claims. This can clearly be seen in Kinesis' deployment of $290 million of limit in the quarter, the robust defense of our core portfolios at both Cathedral and Lancashire UK, and the successful execution of the switch of catastrophe exposures from retro to Cat XL at Lancashire Bermuda.

We're working hard on developing our business, with the approval of Lloyd's of our business plan to add terror and energy lines to Syndicate 3010; continuing to work on new products for Kinesis; and there's been a strong increase in submissions for Lancashire Bermuda in UK, up by approximately 17% in the quarter.

With regard to our buildout of Syndicate 3010, we'd like to place on record our thanks to both our clients and brokers for showing us such strong early support.

In both energy and terrorism, we've been able to make a positive start, finding high quality additional business to the group, following our approval from Lloyd's at the beginning of April.

It's true that pricing is on its way down in almost all segments and the bright spots are few and far between. However, in Cathedral's property buying portfolio, where rates are more closely aligned to the U.S. retail market than the international wholesale market, prices have been maintained or even improved a little.

On the international Group P&I accounts, rates were up around 20%, although we kept our premium increase below this level as we slightly reduced our exposure. Our energy excess liability portfolio pricing was generally flat, at the strong levels attained since Macondo. But outside of this, pricing was under pressure, and we've had to walk away from some business in classes where reductions were unjustified. This was seen most dramatically on the Lancashire Bermuda and Accordion retrocession portfolio, where pricing reductions of 20% were not uncommon. And as a result, we drastically cut back exposures and redeployed our capacity into Cat XL.

We've now built a core portfolio of property Cat XL at Lancashire Bermuda to replace the more opportunistic and potentially volatile retro and large line D&F that we once wrote.

In the right market, we can reenter the retro arena, either through Lancashire Bermuda or Kinesis. But the majority of our Cat XL relationships are cross cycle. We've been able to buy $100 million of retro to protect this Cat XL which, in itself, tells you much about how we view the market.

The energy market is also seeing declines after four years of compound increases. This extends to Lancashire UK's niche deepwater Gulf of Mexico wind book, but demand remains buoyant with plenty of new projects and strong relationships with key buyers. Indeed, we've seen a number of new projects right around the world in offshore energy, with several of them stretching market capacity, allowing Lancashire to develop our excess construction portfolio as well.

Aviation and marine continues to suffer from an excess of capacity, chasing non-correlating business. And both Lancashire UK and Cathedral maintain their focus on very small subsets of the overall markets. The satellite launch portfolio are seeing some growth year-on-year, but this is unpredictable and should not be read as a trend.

Kinesis followed up the $252 million of limit deployed at 1/1 with an additional $37.5 million in February, all in its multiclass reinsurance product. Darren Redhead and his team continue to both receive interest in this from potential clients and to explore other niche products suitable to a collateralized balance sheet.

One of the other bright spots is the increased availability and better pricing of our own reinsurances for both Cathedral and for Lancashire. We've been able to buy additional limit with broader coverage at improved pricing in many areas, which will, again, limit volatility and improve the net result in the event of any shock losses. As a major borrower of reinsurance now, we should never forget that the weakening rate environment is not just a one-way street for our business.

I'll now pass over to Elaine Whelan.

Elaine Whelan {BIO 17002364 <GO>}

Thanks, Paul. Hi, everyone. Our results are on our website as usual. We had another reasonable quarter, producing an overall ROE of 3.9%. As I said in our release, 3.5% of that comes from Lancashire, with the balance a combination of Cathedral's contribution and acquisition adjustments. Those acquisition adjustments relate to our finite life intangible assets and will tail off over the next couple of quarters as we amortize that.

Our total goodwill and intangible asset balance should stand at about $154 million by the end of the year. (08:23-08:27) and as Paul said, we have drastically cut back our retro book with only $10.7 million of premiums written in the first quarter compared to $67.6 million in Q1 last year.

Bear in mind (08:39) retro book with Accordion qualifying premiums and is 100% ceded to the Accordion vehicle. The impact of the reduction in retro and earnings was, therefore, minimal.

Focus on protecting our core book, combined with the increased market (08:57) business has increased our premiums from $31.3 million in Q1 2013 to $69.4 million in Q1 2014. Some of that business was written in a multiyear basis about 30% of the total, so we'll have the benefit of those earnings coming through next year as well.

Otherwise, the Lancaster lines, there were some small movements resulting in the overall book being only slightly behind last year in terms of top line. For Cathedral, we picked up $108.2 million of premium this quarter, a bit behind our Q1 last year mostly due to rate reductions in the property reinsurance and aviation books.

On the ceded side, as I mentioned, we're no longer ceding to the Accordion vehicle, so there's a substantial reduction for that. We added $40.7 million of ceded premiums from Cathedral with the balance of the increased spend in the quarter due to the additional cover (09:50-09:56). We've continued to include Cathedral's income statement in our supplement, and I noticed there that their insurance spend was lower this quarter compared to last year. Again, that is a result of improved pricing and available product.

(10:07-10:12) quarter, we've written a little bit of retro but less than last year. Our 1/4 property cat renewals held up reasonably well (10:19-10:27)

Unverified Participant

Operator?

Operator

Hello.

Unverified Participant

Hello. This is dropping out apparently. We're going to have to dial back in.

Operator

Okay. That's fine. You mean your line is fine. It just seems that Denise's line doesn't seem to be - seems to be cutting in and out.

Unverified Participant

Okay. Denise, can you drop off and dial back in, please?

Everyone else is here. Can we just drop Denise from the call?

Operator

Yes. Denise has actually disconnected now.

Unverified Participant

Okay. Sounds better.

Elaine Whelan {BIO 17002364 <GO>}

So how much of that came through? Where should I pick up from?

Unverified Participant

Please, start your paragraph again.

Elaine Whelan {BIO 17002364 <GO>}

Okay. Let me pick up in there. The rest of premiums, again. So for the second quarter we've written a little bit of retro, but less than last year. Our 1/4 property cat renewals held up reasonably well with pricing off about 15%. For some existing clients who have been purchasing this year, we generally made up that lost premium on new layers that came to market.

Overall, depending on how the energy and June property cat renewals go, I'd expect the Lancashire second quarter book to be broadly flat to last year, and a slight uptick in the Cathedral book due to the new energy and terror business we expect to write in the wholly owned syndicate.

Acquisition costs in the first quarter were impacted significantly by the Accordion vehicle as we received $6.7 million of profit commission and commutation of our quota share as the vehicle is now in run-off.

Excluding the impact of the profit commission and also reinstatement premiums, our acquisition cost ratio would have been a more normal 20.3%, and I'd expect our adjusted acquisition cost ratio for the year to be around 20% or 21%.

On losses, there are no real events to speak of and very low attrition reported for the 2014 accident year, but we did have some development in the 2013 accident year, which gave us net adverse development for the quarter. That was principally in relation to one large late-reported energy claim, and we'll continue to monitor the development of that over the coming months.

Our reserves for previous large events were relatively stable. Our accident year loss ratio was 28.4%, which is a reasonable reflection of our expected attritional losses.

On investments, another positive, if unspectacular, return as we benefited from the spread down in the quarter. We have more or less liquidated our emerging market debt portfolio now with just $22 million left, and we've continued to add to our bank loan portfolio.

We had fairly high cash balances at the end of the quarter and that's, in part, due to the amalgamation of the Lancashire and Cathedral portfolios; in part holding cash from the special dividend we just paid; and in part due to funding a small hedge fund portfolio at the beginning of April.

So far, we have allocated $67.5 million to low volatility hedge funds really to diversify our portfolio and help manage our exposure to rising interest rates. Our tail risk hedge also remains in place. You should see our cash come down and our duration extend a bit through the second quarter. No dramatic changes, but some minor adjustments to complete our consolidation of the portfolio. We'll also allocate a bit more to our hedge fund portfolio.

On KCM, no real change in financial terms from last quarter as our next draw will be around 1/6. So on capital called to-date, we'll earn about $5 million in underwriting fees for the year. Although just be aware, we're earning that in line with the underlying risk profiles of portfolio Kinesis Re, so it will be earned mostly over the U.S. hurricane season.

Again, profit commissions could be around $9 million, depending on the loss activity, but we won't receive anything until Q1 2015 at the earliest. $0.6 million of our other income is the first quarter share of the underwriting fees, with $3 million being the profit commission we received on the termination of Saltire with that vehicle also now in run-off. The remainder of our other income is managing agency fees from Cathedral.

Lastly, bits and pieces; G&A is higher, due to the addition of Cathedral, but also the amortization of our intangible assets. I'd expect the ratio to come down a little over the rest of the year.

Financing costs are impacted by the mark to market of our interest rate swaps and our subordinated debt, so around $4 million a quarter is a reasonable reflection of debt and LSE costs and the like for the mark to market on the swaps.

Our tax credit for the quarter is due to the run-off of the deferred tax liability created from our finite life intangible assets, so that will be fully released by Q3.

Just wrapping up then in capital, our book is broadly stable as we continue to focus on core clients and our PMLs are in line with expectation. We'll see a little bit of growth in Syndicate 3010, but nothing particularly capital intensive at this stage.

With the 1/6 and 1/7 property cat renewals coming up and we're in the middle of the Gulf energy renewals, so we'll see how those go. But as we always say, if there's no change in market conditions, you can expect a substantial proportion of our earnings will be returned by way of a special dividend later in the year. We'd, obviously, love to be able to put our earnings to work, but we don't think that's likely based on our current outlook.

With that, I'll now hand over to the operator for questions.

Q&A

Operator

Thank you. Our first question comes from Frank Cawood from Frank Cawood Associates (15:42). Please go ahead with your question.

Yes. Congratulations on a fluid transition, and we all miss Richard and wish him very well. But I just want you to know that I have the utmost confidence in the bench as it has been put. I think the bench is, perhaps, stronger than many realized.

Elaine, I have a question for you. On the duration in the portfolio, I know there's been some talk about the way duration is calculated. It's not necessarily the same as term on corporate bonds, but some of these could be reset, perhaps, for a longer term. Some of the duration calculations have to do, I think, with the assumption that they might be called a little bit early. Have you had any kind of look through into that to see what might happen to that if some of these were not, in fact, called early?

A - Elaine Whelan {BIO 17002364 <GO>}

No, we're following a fairly standard duration calculation. But I think one thing just to note on the duration that's in there, the tail risk hedge that we've got knock about 0.2 off our duration and we also had pretty high cash balances over the end of the year for paying dividends and for the amalgamation of the two portfolios between us and Cathedral as well. And so that kind of brings everything down. And we also liquidated almost all of our EMD portfolio, and that was also quite a long duration so that brings it down a little bit as well. And...

Q - Operator

Okay, that's - yes, good. So the tail risk has been recovering in that area, too. And just a couple of questions, I guess, for the - maybe this would be for Peter Scales. We noted there's a little expansion maybe in a new line of business with some other underwriters coming in with Cathedral. Any comment on that, sir?

A - Peter David Scales {BIO 2108933 <GO>}

In terms of the energy and terror in Lancashire, we had the Lloyd's approval in the start of April; started trading two weeks, three weeks later after putting some reinsurance programs in place. I'm sure Paul Gregory will give you some more color on that. But things have gone very well. You may have read in the press of some other gentleman may be joining us, who we are delighted about. Equally, they are currently working for their current employer, and we would be delighted to give some color on this further down the line when we're able to do so.

At the moment, they're doing the right thing, looking after their clients and brokers, first of all; we're very happy to encourage that. And when we have a proper story and we have some metrics of what effect that will have on the build-out of 3010, we'll be delighted to share that with you.

Q - Operator

Great, thank you.

A - Peter David Scales {BIO 2108933 <GO>}

But at the moment, they're doing their job as they're supposed to.

Q - Operator

Thanks very much. And for, Alex, again, congratulations on keeping things very well hedged as you're going into wind season in the U.S. and so that's – I think it's a very good profile. You could perhaps post a little higher earnings if you hadn't done that, but I'm very comfortable with that.

A - Alex Maloney {BIO 16314494 <GO>}

Okay, Frank (18:43). Thank you.

Operator

Our next question comes from Chris Hutchings (sic) [Chris Hitchings] from KBW. Please go ahead with your question.

Q - Chris D. Hitchings {BIO 2034501 <GO>}

Good morning. This is Chris Hitchings here. My near brother Chris Hutchings isn't on the line. Two things: on the cat, I mean, presumably the energy loss is the Statoil, can you give us some color on how that's being provisioned, and is that the entire component of the deterioration on the 2013 year?

Could you tell us what, if anything, you put in for Malaysian Air and within the numbers and presumably that's included in your attritional losses at the moment, if at all?

Thirdly, yes, can you give us some color on the words substantial – significant proportion of the earnings to be distributed in dividend? It seems to be slightly different wording to what you used in the past. Is that intended to signal anything? I know this is Elaine's wording, and she's always terribly careful about these things. Thank you.

A - Alex Maloney {BIO 16314494 <GO>}

Hi, Chris. Thanks for that. We'll go to PG for the energy one. Elaine, can you do the...

A - Elaine Whelan {BIO 17002364 <GO>}

Yeah. I don't know that I'm smart enough to be signaling that much with my words in terms of substantial earnings. We've been splitting our dividend towards the end of the year for the last couple of years. It depends very much on our outlook. If we've got a very solid, clear outlook, then that may mean that we're more comfortable returning a higher proportion of our earnings, but we've typically been under the kind of 75% to 90% range, give or take, so that's kind of very substantial, but...

Q - Chris D. Hitchings {BIO 2034501 <GO>}

Okay.

A - Elaine Whelan {BIO 17002364 <GO>}

...in terms to the 2013 losses, we can't really comment on the specifics of individual claims, but the insurance provider does always seem to help a little bit with that. There are a couple of little energy losses in there and also a little bit of development on some European winter storms on the Cathedral side of things. Again, Malaysian, Cathedral clearly have a (20:54), but I can't really comment too much on the specifics of it, other than to say perhaps that their reinsurance program kicks in another $7.5 million...

A - Paul Gregory {BIO 16314515 <GO>}

Yeah. And with regard to the one particular energy loss from 2013, there is currently a range on that, which is quite normal for energy losses. And we're conservatively reserved on that particular loss, quite normal for energy losses – (21:25) nature of the underlying risk, the things to be notified late every now and again.

Q - Chris D. Hitchings {BIO 2034501 <GO>}

Sorry, just to come back on the aviation loss, you do not specifically say what you've provided, but you point out that the $7.5 million retention. Does that mean you have provided at $7.5 million or more than $7.5 million?

A - Peter David Scales {BIO 2108933 <GO>}

Chris, it's Peter. The $7.5 million, as you said is a retention; but that's on Syndicate 2010...

Q - Chris D. Hitchings {BIO 2034501 <GO>}

Okay.

A - Peter David Scales {BIO 2108933 <GO>}

...of which Lancashire piece is 58%, that's the piece to take. But the $7.5 million gets us into the program and, basically, in the lower, middle reaches of that, the reinstatement (22:10) are a wash, so it doesn't really make too much difference to us.

Q - Chris D. Hitchings {BIO 2034501 <GO>}

Okay. Thanks very much indeed.

Operator

Our next question comes from Andy Broadfield from Barclays. Please go ahead with your question.

Q - Andy D. Broadfield {BIO 7273415 <GO>}

Hi there. That was quick. I only just pressed the button. Three questions, really, around the nature of a softening cycle that – I just had some questions around retention, multiyear contracts, and the split of new business as well.

So just on retention, actually maybe this is a first and third together. Retention versus new business, there's always a conflict between people who actively manage their portfolios and people who move into new business lines they haven't previously been in, or straying into sort of parts of business lines they haven't really strayed into before. I was just wondering if you could characterize, or quantify first, how much of your business in the first quarter was retained – what your retention levels were versus sort of historic retention levels and, therefore, the amount of new business you're writing. And also, your confidence that those areas you are perhaps expanding into a little bit more, there's a reason why you're picking it up and other people are dropping it off, why you are feeling confident that you know more than those people who are no longer writing it? That's the first question.

The second question just around – there was a comment in your release this morning about multiyear contracts; I think it was only a small passing comment, but again, that's a typical softening cycle characteristic is to write multiyear contracts. So I just wanted to get your thoughts on that as well, please.

A - Alex Maloney {BIO 16314494 <GO>}

Right, okay, Andy. It's Alex. I think our view of the current market is it's undoubtedly getting more difficult. That means, for Lancashire, that we're still going to be the Lancashire that we were in the past, but we just go about it a sort of slightly different way.

So this market is all about managing your core portfolio. It's all about trying to make that portfolio more efficient, and that may be the use of more reinsurance. So there's different ways to get the same result, if you like.

And as I said, everyone focuses on the market reducing, but every time that happens, so does our reinsurance bill. So there are opportunities there. It is about managing your core portfolio. You're absolutely right, if you have grand plans in this market, you need to make sure that you're being honest with yourself, because I think some companies will look to expand and look to get into lines of business which they don't understand as a function of a soft market. And that generally goes wrong and there's no reason why, I believe, that won't go wrong again.

If you think about our approach, our approach is and has always been, we don't go into any line of business unless we feel we can make a difference, and unless we feel we've got the best-in-breed underwriters. So the team that's going into Cathedral, if you talk to some brokers in the market, they are the best-in-breed underwriters, and that is the only way we will go into any new line of business in this market.

Because, as I said, you have to be honest with yourself. If you don't have the best underwriters that have got the best track records and the client relationships, you're set up to fail, whoever you are. And I think we are honest enough to know that you can't always swim against the tide in this market, but there are things you can do around the edges, which we will continue to do.

The new business, renewal business question is you have to identify where that new business is coming from. So some of the property cat new business that we've written is new top layers, so it's not business that we've stolen from someone else. But you are right, in general, new business can be cheaper than renewal business. And there's no panic here. There's no one here that's looking to dramatically grow our book. We'll still be opportunistic, but you have to be realistic about the market.

Q - Andy D. Broadfield {BIO 7273415 <GO>}

Just a couple of follow-ups on that, I guess, which is one, without adding lumps to your business like you did obviously with Cathedral, lumps may not sound very flattering, but chunks of business deal to you, we should expect your portfolio to be shrinking given your historic capital discipline.

A - Alex Maloney {BIO 16314494 <GO>}

Yeah. I mean...

Q - Andy D. Broadfield {BIO 7273415 <GO>}

...and that's not happening, right?

A - Alex Maloney {BIO 16314494 <GO>}

Well, there is different ways to do that. So our portfolio may look similar, but you have to look about how much reinsurance we're now purchasing and how much volatility you've got around our earnings. So as the market continues to decline, we will probably stay on most of our business, which is core business, but we'll probably buy more reinsurance.

If you look at how much reinsurance we've already purchased this year, it's the most amount of reinsurance we've ever bought in our history. And that will continue as the market goes down. So we are still going to manage our capital, if you like, but in a slightly different way. And if we can find - if there's people out there that are more hungry than us that we can pass some of our risk to, why wouldn't we do that? So nothing has changed. The way we're going about it is slightly different.

Q - Andy D. Broadfield {BIO 7273415 <GO>}

Yeah, that all makes sense. I guess, i.e., it's hard for me to imagine how you can be buying more reinsurance without freeing up more capital, and therefore likely to either be having declining ROEs because you'll have more free capital you can't utilize or you'll try to use that by going into more areas. Just that conflict that sort of cyclical or circular argument that I'm not sure I fully understand, but maybe another conversation offline or something there.

One final sort of specific question which I think I mentioned around the multiyear contracts. Is there anything to mention on that or is that just a passing comment on the...?

A - Alex Maloney {BIO 16314494 <GO>}

Let me just say one more thing about what you just said there. When you buy in reinsurance, it's very easy to get sucked into the – you only buy reinsurance because it looks good on the model. So there will be some reinsurance that we purchased that – on a technical basis doesn't look the most capital efficient thing you could. But you have to get the balance of old-fashioned reinsurance buying with some sort of capital relief reinsurance buying. So you have to make sure you get that correct.

Quite frankly, we could go out and buy $200 million of ILWs tomorrow that would look great on a model, would give you a huge capital relief, but in the event of a loss, probably it wouldn't pay. So it's about getting that balance correct.

On the long-term deals, we were very successful selling long-term deals on our energy Gulf of Mexico book. We started selling those deals because we thought we were at the top of the market. That has insulated our pricing.

But if you look at the amount of long-term deals we have in the company, overall, it's probably less than 20%. So we're not going to tie up the majority of our portfolio on a long-term basis, because obviously, if something happens and rates go up. We don't want to be locked into the bottom of the market if we are at the bottom.

But we're not going to do that. So there will always be a limitation on how much we will sell on a multiyear basis. I think we're probably where we want to be already. I don't see us doing a huge amount more.

Q - Andy D. Broadfield {BIO 7273415 <GO>}

Okay. And I'm sorry to keep going on, but the one last question on that then. The reinsurance buying that you're talking about then is should we just expect lower volatility from these reinsurance you're buying, rather than sort of out of the money capital relief-type contracts. Is that the characteristic you're buying at the moment?

A - Alex Maloney {BIO 16314494 <GO>}

Yeah. I mean, it depends where the loss comes and how big the loss is. So if you look at our energy portfolio, we can't really buy in much more than we currently buy in. So that won't stop losses that have happened this month. But if you go to the other end of the curve, Lancashire's always been very comfortable writing some big lines, and we've taken some reasonably large net exposures. If one of those claims come home going forward, yes, our numbers would definitely be less volatile. We're taking out a lot of the tail risk.

Q - Andy D. Broadfield {BIO 7273415 <GO>}

Okay. Thank you so much.

Operator

Our next question comes from Maciej Wasilewicz from Morgan Stanley. Please go ahead with your question.

Q - Maciej K. Wasilewicz {BIO 16462204 <GO>}

Hi. I've got a couple of annoying specific questions, and then one more general question. First annoying specific question is on your financing costs. I think they were about double what they were last year; just if you could explain where that came from?

Secondly on other operating expenses, you went to $27 million from $17 million last year. Is that essentially the new run-rate with the Cathedral incorporated? Was there any funnies in there?

And in terms of the general question, I just wanted to know, looking at the renewals in April, but also more specifically the ones that are coming up, I know everyone gives their estimated price movements for contracts they wrote previously. But, of course, there's a lot of judgment that goes into that because it's very difficult to quantify some of the changes that are being made. Is there a particular pressure on any given terms and conditions that you can identify that's a new trend or that's something that we should be watching when, I guess, when others and when everyone reports their renewals or is it pretty much just a top-line price game from here?

A - Alex Maloney {BIO 16314494 <GO>}

So do you want to start?

A - Elaine Whelan {BIO 17002364 <GO>}

Sure. And hi. It's Elaine. I'll start on the financing costs. They're relatively stable quarter-on-quarter, other than interest rate swaps we've got. So that's obviously subject to interest rate movement. So if you take the subordinated debt that we have, the subordinated debt that Cathedral has and the senior debt that we have, plus average our sea costs and whatnot, then you probably get to about $4 million a quarter in terms of run rate. The variation that you're seeing in this quarter is entirely driven by the mark-to-market on the swap.

On the G&A, there's a few kind of funnies that come in this year just purely as a result of the acquisition. We have a finite life intangible asset that we have to amortize, so there's $4.4 million in our G&A this quarter that relates to that. And there will be slightly less than that next quarter, and then less again in Q3, then we'll be finished with that one. So that will be a bit of an anomaly this year, but as that tails off, we do expect the G&A ratio to trend down.

If you're looking for kind of a run-rate G&A, we're obviously adding in one full quarter of Cathedral's G&A on top of one full quarter of our G&A this time around as well. So if you took last year's G&A for both of us and backed out a little bit for acquisition expenses that we would both have incurred last year, then you probably got something that looks like a reasonable run-rate. So I'd knock about $5 million off for us and about $5 million off for Cathedral, just in terms of costs.

A - Paul Gregory {BIO 16314515 <GO>}

Hi, it's Paul Gregory here. I think at the moment, in general, the main focus is on price, so clients and brokers are aiming to get their costs down. And that applies across pretty much all of our lines of business, as I've mentioned earlier. Particularly in the direct lines, the focus is price as opposed to terms and conditions.

And there's a little bit on terms and conditions in areas of reinsurance, but again, the main focus is getting the price of the product down. There are certain areas, such as increased reinstatement options that are being looked at. But the main focus is price at the moment. That's not to say that won't change as we move through the cycle, and level at which people come in and buy reinsurance would be looked at. But at the moment, as I said, price, rate online, are the main areas that are the focus points.

Q - Maciej K. Wasilewicz {BIO 16462204 <GO>}

Thank you.

Operator

Our next question comes from Ben Cohen from Canaccord Genuity. Please go ahead with your question.

Q - Ben Cohen {BIO 1541726 <GO>}

Hi. Thank you very much. I had two questions. The first was on capital requirements. I think you indicated last year and I think with the fourth quarter results that you need about $1.6 billion of total capital. Does that still hold? Would you see that moving at all materially through the course of the year?

And my second question was, the movement in earned premium in the first quarter, does that give us a reasonable run-rate for the change that we should expect for the full year? Thank you.

A - Elaine Whelan {BIO 17002364 <GO>}

Hi, Ben. It's Elaine. In terms of capital requirement, nothing's really changed. We put our books together and everything's kind of shaken out more or less where we expected it to be. So it's expected still to be sitting around that $1.6 billion for the rest of this year, subject to anything that happens, obviously.

And in terms of the earned premium, we do have Cathedral's income statement in at the back of our supplement. So you can combine – I mean, their debt book is fairly stable. So I think, more or less whatever comes off in the reinsurance book in terms of pricing, we can add it back in, in terms of energy and terror, and earn that out over the year. So the earning pattern should be reasonably stable, other than the fact that there's a little bit less reinsurance in there this time round.

And, again, ours, if you kind of back out the Accordion levels, then that should be about your run rate. So the reason it's come down is entirely because we've just added on their book of business into this quarter. And they do tend to write a bit more of their annual book first quarter than we do. So that slowed us down a little bit. I'd expect we get back to kind of about the 100% level by the end of the year.

Q - Ben Cohen {BIO 1541726 <GO>}

Okay. 100% of the net written, is that?

A - Elaine Whelan {BIO 17002364 <GO>}

Yeah, more or less.

Q - Ben Cohen {BIO 1541726 <GO>}

Okay. Thank you. Thanks.

Operator

We have a follow-up question from Maciej Wasilewicz. Please go ahead with your question.

Q - Maciej K. Wasilewicz {BIO 16462204 <GO>}

Thanks for taking one last question from me. I just wanted to know, if you could remind me again, in Kinesis, if you had a clean year, and also if you had an expected year, I guess, the mean average year, what would the profit commission look like on the current AUM?

A - Alex Maloney {BIO 16314494 <GO>}

Hi. It's Alex here. It might be approximately about $5 million, maybe a little bit less on the mean. On the expected, it would be about $3 million.

Q - Maciej K. Wasilewicz {BIO 16462204 <GO>}

Thank you.

Operator

Our next question comes from Fossard from HSBC. Please go ahead with your question.

Q - Thomas Fossard {BIO 1941215 <GO>}

Yes. Good afternoon, guys. Two questions for me. The first one would be on Russia and Ukraine. Does that create any tension on your political risk book? Is it something that you are looking carefully at?

Second question would be for Elaine. On the attritional loss ratio, you indicated that the 28.4% in Q1 was a fairly good proxy for the attritional loss ratio going forward. But in the press release, you indicated that the attritional sounds to be a bit – or to be running slightly below the normalized run rate. So if you could be a bit more precise on what you meant. And that's it, basically. Thanks.

A - Alex Maloney {BIO 16314494 <GO>}

Okay. So I'll take the first one. Yes, we do have exposure in Ukraine and Russia. We have very little actually in Ukraine. We don't have a lot there at all. We, of course, have more in Russia. We are monitoring that situation very closely. We currently haven't written $1 of additional exposure for that book since the event happened, and it's unlikely we'll write any more exposure to that event coming forward.

And obviously, the deals we write do amortize over time anyway, so any exposure we have reduces over time. As I said, we're monitoring it closely. We're happy with our market share. There's not that much more we can do, quite frankly, apart from not writing any more new business at the moment.

A - Elaine Whelan {BIO 17002364 <GO>}

In terms of the attritional loss ratio, I think, what we previously said was, before adding on Cathedral, we're sitting around the 22%, 23%, and adding Cathedral into the mix brings us really to that 25% attritional loss ratio. And just purely by price adjusting that, you get to the 27%, 28% attritional ratio. And I think that's a good place to start. And so we'll see how the rest of the year goes.

The comment in this quarter is really just getting at that, that's the kind of reasonable level for an accident year loss ratio in the absence of any kind of significant cat events or significant losses that there's always going to be little bits and pieces that come through, and I think that's what you're seeing this quarter; nothing really other than the prior year development that's really worth talking about.

Q - Thomas Fossard {BIO 1941215 <GO>}

Okay. Thank you.

Operator

We have a follow-up question from Chris Hitchings from KBW. Please go ahead with your question.

Q - Chris D. Hitchings {BIO 2034501 <GO>}

Yes. I'm sorry, come back in. Just two very simple things. Just on your answer, Elaine, on earned premium, surely one influence on earned premium is the multiyear contracts. Presumably that's the main factor.

And secondly, a purely admin thing; I actually lost chunks of you before the bit you started to repeat. And while it'll be lovely to hear you through all that again, it might be better, if you simply circulated to all of us a script of Elaine's chat. Thanks.

A - Elaine Whelan {BIO 17002364 <GO>}

Yes, sure, no problem. I'm sure you don't want me to run through it all again. In terms of multiyear contracts, we've got the benefit of energy multiyear contracts in 2012 and 2013 coming through. So the only thing pointed out in terms of the next part of that the older ones run off in (41:17).

Q - Chris D. Hitchings {BIO 2034501 <GO>}

Yes.

A - Elaine Whelan {BIO 17002364 <GO>}

In terms of the cat book, you're probably talking about $20 million worth of premium that was written on a multiyear basis. We'll get $10 million of that this year and $10 million of that next year, just roughly. It doesn't really have a huge impact.

Q - Chris D. Hitchings {BIO 2034501 <GO>}

Okay. Thank you.

Operator

We have another follow-up question from Frank Cawood (41:36). Please go ahead with your question.

Yes. Again, just a little clarification, not so much from you as related to the other question about the capital management, although it's unstated. I think typically, as you're in the early part of the year, you would want to have a little more of a cushion because you're coming into the hurricane season, which is your highest PML.

But if the hurricane season is fairly benign, then that turns out to be a little extra cushion at the end of the year, allowing funds for repatriation to shareholders. So I guess your strategy is exactly the same now as it has been for many years. Is that correct, Elaine and others?

A - Elaine Whelan {BIO 17002364 <GO>}

Yeah. Exactly right, Frank (42:18). And I mean, we're obviously going to adjust it for the market that we're in, but the underlying principles just don't really change very much.

Q - Operator

Good. I just want (42:26) on that because that's just the practicality of it. You need to have that little extra as you're going into that and then coming out, if it's not bad, then you've got some free cash that you can do different things with, so good.

Okay. There appear to be no further questions at this time.

A - Alex Maloney {BIO 16314494 <GO>}

Okay. Thank you and we will see you next quarter.

Operator

This now concludes our conference call. Thank you all for attending. You may now disconnect your lines.