FINAL

Bloomberg Transcript

Q3 2013 Earnings Call

Company Participants

- Jeff Kelly, EVP and CFO
- Kevin O'Donnell, President and CEO
- Peter Hill, IR

Other Participants

- Brian Meredith, Analyst
- Crystal Lu, Analyst
- Ian Gutterman, Analyst
- Jay Cohen, Analyst
- Josh Shanker, Analyst
- Josh Stirling, Analyst
- Matt Carletti, Analyst
- Michael Nannizzi, Analyst
- Sarah DeWitt, Analyst
- Vinay Misquith, Analyst

Presentation

Operator

Good day, ladies and gentlemen. My name is Montserrat, and I will be your conference operator today. At this time, I would like to welcome everyone to the RenaissanceRe Third Quarter financial results conference call. All lines have been placed on mute to prevent any background noise.

Following today's presentation there will be a question-and-answer session. (Operator Instructions)

I would now like to pass this call over to your first host, Mr. Peter Hill. Sir, you may begin your conference.

Peter Hill {BIO 15385944 <GO>}

Good morning, and thank you for joining our Third Quarter 2013 financial results conference call. Yesterday after the market closed we issued our quarterly release. If you didn't get a copy, please call me at 212-521-4800 and we will make sure to provide you with one.

There will be an audio replay of the call available from about 1 PM Eastern Time today through midnight on November 27. The replay can be accessed by dialing 855-859-2056 or 404-537-3406. The passcode you will need for both numbers is 78498780.

Today's call is also available through the investor information section of www.renre.com and will be archived on RenaissanceRe's website through midnight on January 15, 2014.

Before we begin I am obliged to caution that today's discussion may contain forward-looking statements and actual results may differ materially from those discussed. Additional information regarding the factors shaping these outcomes can be found on RenaissanceRe's SEC filings to which we direct you.

With us to discuss today's results are Kevin O'Donnell, President and Chief Executive Officer, and Jeff Kelly, Executive Vice President and Chief Financial Officer. I would now like to turn the call over to Kevin. Kevin?

Kevin O'Donnell

Thanks, Peter and good morning everyone. I will start off the call today by making some general comments. Then I will turn it over to Jeff to do the financial results, and before taking questions I will come on to make a few more comments.

The Third Quarter call is always an interesting one for us. It takes place at a time when we transition our focus from the active management of our in-force portfolio to planning for our new portfolio in light of the upcoming renewal.

I'm pleased to report strong performance for the Third Quarter. We reported an operating ROE of 19%, and growth in tangible book value per share plus accumulated dividends of 5%.

We achieved this in a low interest rate environment with competitive market conditions. Our results reflect light cat activity. They also reflect actions we took early in the year to improve the profile of our portfolio.

Conditions throughout the Atlantic Basin were unfavorable to hurricane activity, even though the tropical storm count was consistent with historic levels. Our scientists at WeatherPredict do not believe that this season implies any long-term trend.

Generally speaking, the underwriting environment in property catastrophe and other reinsurance lines remains competitive, with abundant supply of both traditional and nontraditional capacity.

There has been a lot of discussion this year about convergence, with a particular focus on new or nontraditional capacity. The participation of nontraditional capital in our industry, however, is anything but new. We have been managing many forms of capital including third-party for well over a decade.

It is our job to find the most efficient capital and deliver it to our clients by matching it with the most attractive risk. Third-party capital is just one more tool, making our job easier.

What is different about the current environment is that capital is coming in when rates are going down. Our capital, because it is primarily from retained earnings, can be patient. Much of the third-party capital, on the other hand, needs to be deployed or returned.

So now more than ever, discipline is important. While the customers benefit from the new competition, ultimately capital must be paid adequately for the risk assumed. New capital should be deployed carefully and only when it mutually benefits the provider and the end-user.

Over our history we have developed a reputation as good stewards of capital and disciplined underwriters. Capital providers know this, and that is why we will continue to be a market of first call for deployment.

Strong capital stewardship and underwriting discipline allows us to make the best use of this new capital. For example, we are seeing client needs that are most efficiently fulfilled on a collateralized balance sheet. We plan to fill that need by raising capital in a targeted manner, using our Upsilon joint venture.

On the other hand, we don't think that increasing the size of DaVinci makes sense right now, for other investors or for our clients. But our clients are still benefiting from the new capital as we have been able to restructuring DaVinci's investor base to make it more stable over the long-term.

If we look at the total capital invested into DaVinci by our top investors, that total represents significantly less than 1% of their aggregate capital under management. This is patient capital.

Another subject of intense speculation is the amount of capital on the sidelines. I believe that it is this fear of the additional capital, as much as anything else, that has been driving the rhetoric around convergence. It is instructive to point out that the actual amount of convergence capital is relatively minor compared to the size of traditional balance sheets. Retained earnings this quarter will outstrip new capital infusions many times over.

In addition, we are beginning to see the first signs that third-party capital is cooling to insurance risk as markets have continued to soften. I don't know if that trend will continue, but whatever the future holds for convergence, the ability to be responsive to these various market dynamics will be key in the months and years to come.

In that regard I believe our flexible business model, experience and proven access to the capital markets, make RenaissanceRe the best placed Company going forward.

Let me turn the call over to Jeff, and then, as I said, I will come on for a few more comments after him. Jeff?

Jeff Kelly {BIO 20911735 <GO>}

Thanks, Kevin. Good morning everyone. As Kevin said, I will cover our Third Quarter and year-to-date financial results, and also provide you with our initial 2014 topline forecast.

We reported solid results in the Third Quarter as loss activity was fairly benign and investment performance was favorable. From a topline perspective, the Third Quarter tends to be light for catastrophe reinsurance renewals. However, our specialty and Lloyd's units did report continued strong premium growth.

We reported net income of $180 million or $4.01 per diluted share, and operating income of $151 million or $3.36 per diluted share for the Third Quarter. Net realized and unrealized gains on investments totaled $29 million.

The consolidated combined ratio was 48.6% in the Third Quarter.

The annualized operating ROE was 18.7% and our tangible book value per share, including change in accumulated dividends, increased by 4.9% during the period. For the first nine months of 2013 the annualized operating ROE was 17.7%, and tangible book value per share plus change in accumulated dividends was up sharply at 10.9%.

Let me shift to the segment results beginning with our reinsurance segment, which includes cat and specialty, followed by our Lloyd's segment. Beginning with cat reinsurance, managed cat gross premiums written increased $10.6 million, or 13.5% compared with the year-ago period during the Third Quarter.

Net of reinstatement premiums, managed cat gross premiums written increased 25.7% from a year ago in the Third Quarter. Ceded premiums totaled $50 million in the Third Quarter, reflecting increased reinsurance purchases, including the issuance of our 144A cat bond through the Mona Lisa facility early in the quarter.

For the first nine months of the year managed cat gross premiums written declined $29 million or 2.2% relative to the year ago period. Adjusted for reinstatement premiums in the current and year-ago periods, managed cat gross premiums written would have declined 4.8% for the first nine months of the year.

This compares with our full-year 2013 guidance for the segment of a decline of 10%. Our largely flat underlying premium volume in a very competitive marketplace speaks to the strength of our underwriting franchise and market position.

Ceded premiums for the first nine months of the year totaled $364 million compared to $411 million in the comparative period. The decline in ceded premiums relative to a year ago reflects both lower cost retro protection as well as a reshaping of our portfolio early in the year, which led us to retain slightly more risk in lower layers.

The Third Quarter combined ratio for the cat unit of 30.1% benefited from a low level of catastrophe loss experience. We did not have material losses related to notable industry loss event such as the German hailstorms or flooding in Colorado.

Net favorable reserve development totaled a modest $6 million for the cat unit in the quarter, relating primarily to a $5 million reduction to our loss estimate for Hurricane Ike. We did not make any meaningful reserve adjustments during the quarter to our ultimate loss estimates for storm Sandy or for the major loss events of 2010 and 2011.

For the first nine months of the year the cat unit combined ratio came in at 32.3%, with favorable reserve development totaling $43 million.

Specialty reinsurance gross premiums written increased 58% in the Third Quarter to $60 million, primarily driven by additional quota share premium. Percentage growth rates for this segment can be uneven on a quarterly basis, giving timing differences and the relatively small premium base.

For the first nine months of the year gross premiums written increased 14% compared to the year-ago period. This was above our prior guidance for slight growth in the year.

The specialty combined ratio for the Third Quarter came in at 62.7% with favorable reserve development totaling $3 million. For the nine months of the year, the combined ratio for the specialty segment was 68.1% with reserve releases of $23 million resulting in a 14.6percentage point benefit to the underwriting margin.

In our Lloyd's segment we generated $40 million of premiums in the Third Quarter, an increase of 39% compared with the year-ago period. For the first nine months of the year, Lloyd gross premiums written increased 37% to $183 million. This compares with our annual growth rate guidance of above 30% for the full year 2013.

The Lloyd's unit incurred a $2.5 million underwriting loss in the Third Quarter, driven in part by a $3 million net unfavorable reserve development principally relating to a single late reported claim. The expense ratio remained high at 45.5%, but has been declining sequentially as business volume increases. For the first nine months of the year, the Lloyd's combined ratio came in at 101.5%.

Turning to investments, we reported net investment income of $60 million in the Third Quarter. Recurring investment income from fixed maturity investments remained under pressure due to low level of yields on our bond portfolio, and totaled $24 million in the quarter.

Our other investments portfolio generated a gain of $37 million in the Third Quarter. Our private equity and hedge funds had positive performance and generated gains of $14 million.

During the quarter we reallocated our portfolio of bank loans from other investments to our fixed maturity investments to reflect the change in their holding structure from investment funds to separate accounts. Thus, in future quarters we will not be reflecting mark to market gains and losses on these securities as a part of investment income. Instead, adjustments in the valuation of these bonds will show up below the operating income line within realized and unrealized gains and losses.

Our other investments performance also included an $18 million gain related to an upward mark to market adjustment for our investment in Essent. This is a startup mortgage insurance company that we made a strategic investment in during 2009, and which we had accounted for at fair value.

The increase in the value of our stake in Essent reflects our estimate of fair value at the end of September. Following the IPO last week, we intend to shift this investment to be reflected as equity investments trading on our balance sheet. And its value will then be based on its public share price.

So on a go forward basis, valuation adjustments post the IPO valuation will be reflected in realized and unrealized gains and losses on investments, which are not included in our operating income.

The total return on the overall investment portfolio was 1.4% for the Third Quarter. The duration of our investment portfolio remained short at 2.1 years and has remained roughly flat over the course of the year. The yield to maturity on fixed income and short-term investments was roughly flat as well relative to that of the Second Quarter at 1.7%.

On a year-to-date basis our investment portfolio has generated a 1.5% total return.

As we have stated on recent calls, we believe we have capital in excess of our requirements, given our current portfolio and our current outlook for business growth.

Share repurchases during the quarter were again relatively modest, totaling 224,000 shares for an aggregate cost of $19 million. For the first nine months of the year, we repurchased 1.8 million shares for a total of $141 million, with the vast majority of the shares bought back in the First Quarter.

We generally take a pause in share buyback activity during wind season, although we did buy back some shares through our 10b5-1 plan early in the quarter. We remain committed to returning capital to shareholders in a disciplined manner and share repurchases will remain our primary method of doing so.

We have, however, remained active in terms of managing our overall capital structure. And recall in the Second Quarter we refinanced our preference shares at more attractive rates.

Also, earlier this year we returned $150 million of capital to third-party investors in DaVinci as well as repaying a $100 million senior note issue that matured in the middle of February.

Our balance sheet remains strong with considerable excess capital, and from a liquidity standpoint, over $750 million in cash and securities at our holding company.

Our line item relating to discontinued operations reflects a loss of $9.8 million. This relates primarily to an $8.8 million loss on our sale of our weather and energy risk management unit, REAL, to Munich Re at a discount to carried value during the quarter. As noted in our release, all prior periods presented have been reclassified to reflect the results of REAL in discontinued operations.

Finally, let me give you our initial topline forecast for 2014. For managed cat we estimate premiums will be down about 10% in 2014, excluding the impact of reinstatement premiums. This reflects our expectation for continued price competition as well as having fewer business opportunities that meet our return hurdles.

In specialty reinsurance we are forecasting the top line to be up 15%, reflecting some new business opportunities. Keep in mind that the growth in this segment can be lumpy due to the relatively small size of the premium base.

In our Lloyd's unit we expect premiums be up over 20% for the year. Recall, too, that this growth is off a relatively small premium base and we continue to be in the building and growth phase for this platform.

Finally, I would remind everyone that premium estimates of this nature are subject to considerable risk and uncertainty, and our goal in providing them to you is to give you our best estimate at this time.

Thanks, and with that I will turn the call back over to Kevin.

Kevin O'Donnell

Thanks, Jeff. As you can see from our guidance we are expecting a challenging renewal for property cat. Over our 20 years we have experienced many softening markets. In my view we're better positioned today from the perspective of tools, people, and capital than we have ever been.

With the risk management frameworks we have in place, our insight into the risks we're assuming is improving all the time. That helps us write with conviction, and we believe we will be able to build an attractive portfolio for 2014.

At the same time we will manage our exposure using multiple channels, including ceded reinsurance and trading with third-party capital. We expect to see continued demand at attractive terms for the aggregate retro product we offer through our Upsilon sidecar.

One of the changes we will be focusing on in the market is the expiration of TRIA at the end of 2014. We have historically been a large provider of both international and US terrorism coverage. We have the people, technology and capital to write this risk, and believe that if demand for this product increases, capacity will be there to meet it.

Outside of property reinsurance the environment for our casualty and specialty reinsurance that we write is also competitive. However, as primary insurance pricing in some specialty classes continues to improve, we have seen increased quota share opportunities. We have strong capabilities in the specialty lines.

Since this risk is diversifying to our property cat exposure, our cost of capital for most of these lines is very efficient. The challenge to growing this book is that many classes are simply not profitable enough for the risks being ceded.

Specialty Re is building out the new US platform in a disciplined manner, leveraging the expertise and relationships we have developed in our other business units. Our Lloyd's unit is on plan, meeting expected targets.

Over the past few years we have developed our syndicate's underwriting capabilities and infrastructure to allow it to compete effectively in the market. As this operation continues to gain scale, we expect profitability to improve.

Looking ahead, our strong market presence and client and broker relationships position us well to construct a high-quality book of business. We will optimize our portfolio using our joint venture relationships and the opportunities offered by the retro and security markets.

Our strong traditional balance sheet and other vehicles can be ramped up quickly if the need arises. This level of versatility has served us well over the years, and we believe it will continue to serve us well as we look to maximize shareholder value over the long term.

And now, operator, we are ready to take the questions.

Questions And Answers

Operator

(Operator Instructions) Sarah DeWitt, Barclays.

Q - Sarah DeWitt {BIO 18946247 <GO>}

Given the growth that we are seeing in alternative capital, could you just talk about what opportunities you are seeing to manage more sidecars or ventures? I know you mentioned increasing Upsilon Re, but not DaVinci. And how much could that be, the increase in capital at Upsilon Re?

A - Kevin O'Donnell

Sure. In order to think about third-party capital, we tend to look to our clients first. And the reason we have decided to increase the size of Upsilon is because we think there is significant demand for the retro product that we offer, which is -- tends to be more of a worldwide (product), which is efficient on a collateralized structure -- more efficient than on a rated balance sheet.

DaVinci actually is one in which the market for US cat has been relatively flat over the last 12 months. So when we look to our clients, they don't need additional capital to be introduced into the more traditional layers being placed. However, we did change the profile of some of our investors within DaVinci, which we think will be long-term beneficial to us.

And so, although we are not changing -- increasing the size of DaVinci, we are constantly changing the capital structure supporting it, adding efficiency and longevity to the vehicle.

Q - Sarah DeWitt {BIO 18946247 <GO>}

Okay. Great. Then just looking at your operating ROE, up 19% for the quarter, usually in a low cat quarter you are north of 20%. So does this reflect more business mix shift or is it because of rate reductions? And to the extent it is because of rate reductions, how much further would rates need to fall in property catastrophe before hitting your minimum return hurdles?

A - Jeff Kelly {BIO 20911735 <GO>}

This is Jeff. So taking the first part of your question, I think the light cat quarter comparison with years ago -- years ago returns and similar environments are fundamentally a function of the declining interest rate and investment return environment as well as, I think, depending on where your starting period is, just pricing in the business overall.

So we like the pricing in the business. We like our portfolio, but pricing is down, obviously, from some previous periods. So I think for a number of reasons even in a light -- a very light cat quarter -- returns a bit lower than they would have otherwise been in previous years.

A - Kevin O'Donnell

With regard to your rate question, as to how much rates would need to fall, the first point I would like to make is I think the market is softening, but there is still plenty of adequate risk. If we go back to the way we have traditionally talked about the market as between adequate return buckets, low return buckets and negative return buckets, we believe that over the near-term there is ample risk residing in the adequate bucket, even though rates are moving down, for us to continue to produce superior returns.

I think to think about it as a binary point in which we are in or out of the market isn't the way that we think about it. We are constantly looking forward and pro forma-ing our book. When we pro forma our book we are looking at not just rate changes, but how we're going to structure our capital, how much third-party capital we're going to have and how much retro we're going to have.

So when I look forward I see ample opportunity for us to continue to provide capacity. I also see that we are better positioned to sustain market changes, because of the flexibility of our platform.

Q - Sarah DeWitt {BIO 18946247 <GO>}

Great. Thanks for the answers.

Operator

Vinay Misquith, Evercore.

Q - Vinay Misquith {BIO 6989856 <GO>}

The first question is on top line guidance. The down 10% seems actually pretty good considering that we have heard pricing in the prop cat is down more than 10%. Could you help me understand the guidance? Because my thoughts would be that you would write less business, because less of the business would meet your written criteria. Thanks.

A - Kevin O'Donnell

Sure, thanks. The top line guidance -- right now there is a lot of discussion as to how rates are changing in the market, but it's still pretty early in the 1/1 renewal cycle, so there's not a ton of actual price discovery out there.

Again, I would point to the flexibility of the way we build our book of business. So what we have provided is what the top line is, but we will significantly look to manage our book through other mechanisms, whether it be third-party capital, Upsilon has additional opportunities, and also with the way in which we structure our retro programs.

So to focus only on one component being the change in our top line doesn't really necessarily reflect the way in which we are going to build the book over the course of the renewal. There is still a lot of uncertainty as to what 1/1 will look like at this point, and we will continue to modify our strategy as we get closer to the renewal date.

Q - Vinay Misquith {BIO 6989856 <GO>}

Okay, okay. The second question is you mentioned that rates are -- still meet your written threshold. What are those written thresholds right now?

A - Kevin O'Donnell

The way we think about our business is looking at what is our portfolio returning, and then what is the marginal difference of each deal that we add. So the portfolio really reflects where we think the market is going.

So I don't think it would be the most informative way to think about it that there is a specific hurdle where deals are good or bad. It depends on the way in which we are going to structure the risk and the way we are going to bring it on to our portfolio on a net basis.

Q - Vinay Misquith {BIO 6989856 <GO>}

Sure. My question was more in terms of what ROE do you think is an adequate return, if you want to share that with us?

A - Kevin O'Donnell

I would think that -- that's again -- looking at it, our business -- we would deal unexpected basis. And what is ultimately produced is how we have done against that expected basis. But we have been doing it for 20 years, so I would point you to our long-term returns as an adequate place to start.

Q - Vinay Misquith {BIO 6989856 <GO>}

Okay. Great. Then one last question on share repurchases. Would it be fair to assume that 100% of your earnings are available either for dividends or share repurchases this year and next year?

A - Jeff Kelly {BIO 20911735 <GO>}

Yes, I think it would be fair to assume that. We have, as I said, a fair amount of excess capital, what we believe is excess capital. And it would be available to be -- if there aren't other business opportunities that develop for it, and as Kevin noted, there are a lot of levers we can pull in that potential deployment. But it is possible that we could return up to that much.

Q - Vinay Misquith {BIO 6989856 <GO>}

Sure. I am just looking at next year. The top line guidance is down 10%, but is that mostly due to rate and so, therefore, no capital frees up? Or do you actually free up some capital from your topline being down on the cat side?

A - Kevin O'Donnell

I think there is a lot of moving pieces in the way we do this, but I think to keep it simple, I would assume that most of that is rate change, and the pro forma portfolios have a similar risk profile. One thing, if we go back to what we said on the last quarter, we are constantly shifting whether we have risk lower in the -- have more exposed return periods or less exposed return periods.

Those sorts of shifts will occur. But I think in general if you think of the guidance as mostly rate, it's probably as good as anything.

Q - Vinay Misquith {BIO 6989856 <GO>}

Sure, and just to clarify that the growth in the specialty and the Lloyd's will not require (any more) capital, correct?

A - Kevin O'Donnell

When we look at it on our economic balance sheet, that's true. We have to post some collateral at Lloyd's, but those are -- the driver in our decision is the economic. And we're still going to be dominated by our cat exposure, so the marginal capital allocation is very small.

Q - Vinay Misquith {BIO 6989856 <GO>}

Okay. Thank you.

Operator

Michael Nannizzi, Goldman Sachs.

Q - Michael Nannizzi {BIO 15198493 <GO>}

So just one question. On the third-party capital vehicles, what sort of hurdle rate for returns do you have in those vehicles versus your own balance sheet? And I'm assuming DaVinci is similar, but maybe for Upsilon or some of the other structures, I'm just curious how to think about where -- what is the return profile you need to put business into those structures? Thanks.

A - Kevin O'Donnell

Sure. I think it really depends on the structure, so if you look at our cat bond it really is based on the multiple to expected loss as to what we are paying, which is a single-digit return. If you look at things we did in Tim Re, which are concentrated risks mostly in Florida, the expectation for returns actually is quite high. So we try to match the investors that we speak to, to the return profile of the deal that we have.

I think you are right in thinking about DaVinci is being a similar profile to the RenRe cat book. But that is a different type -- that is a permanent vehicle where, in something like Tim Re, we are going out based on an opportunity (multiple speakers). But it really depends on just the risk that we are putting into it, as to the type of investment investor we are attracting.

Q - Michael Nannizzi {BIO 15198493 <GO>}

Got it, thanks. Then what was -- you insinuated a change to the profile of investors in DaVinci. Could you elaborate on that a bit more?

A - Kevin O'Donnell

Sure, if you go back when DaVinci, or even just going way back when DaVinci was first started, and then when we changed the size of it in 2005, we came in with, in 2005, certainly, with more hedge funds. And now we have much more of a pension fund endowment type investment profile within DaVinci.

So that's why I thought making the comment about the size of the overall assets under management of our investors compared to what they have allocated into DaVinci, I think, is an important point.

Q - Michael Nannizzi {BIO 15198493 <GO>}

Got it, and then just one other question on the ceded premiums. So clearly, those were higher, at least than we had this quarter. I would have thought, though, that maybe expense ratio would have benefited a bit more just given how I would imagine the ceding commissions would run through there.

I am just curious. Can you -- is that right or is that not right?

A - Jeff Kelly {BIO 20911735 <GO>}

I am not sure I understand your question. Can you --?

Q - Michael Nannizzi {BIO 15198493 <GO>}

Should higher ceded premiums help to reduce the expense ratio because of the ceding commissions that you receive from the counterparties you are ceding the business to?

A - Jeff Kelly {BIO 20911735 <GO>}

Well yes. The ceded -- a big part of the increase in the ceded premium in the Third Quarter was the cat bond we issued, and there is no ceded premium on that.

Q - Michael Nannizzi {BIO 15198493 <GO>}

Got it, okay, that makes sense. Okay. Thank you.

Operator

Mike Zaremski, Credit Suisse.

Q - Crystal Lu {BIO 21493547 <GO>}

This is Crystal Lu filling in for Mike. My first question is can you help us think about the potential for new reinsurance demand coming in online in Florida as a result of, number one, Citizens' drive to depopulate, and, number two, Citizens' clearinghouse?

A - Kevin O'Donnell

Sure. Looking at Citizens, the takeouts are -- there are more takeouts going on, and Citizens rates are going up. The other thing I would point to is Citizens is also buying reinsurance. So we have got a lot of components of the Florida market that have good tailwinds.

Additionally, when I mentioned that the US cat market has been relatively flat, we did see the Florida market grow modestly and part of it is because of the takeouts.

The clearinghouse will come online and be operational in the next year, so I think we will have better sense as to what opportunities really come out of the clearinghouse. We're optimistic that it can serve to reduce the size of some of the state-funded reinsurance vehicles, which we think is a good thing long-term.

The final thing as we have seen a lot of new startups in Florida, and I think, again, that is again pointing to confidence that there will be more migration of risk from the state facilities to the private facilities. So all of that leads up to be -- for us to be optimistic. But a lot can unfold between now and the June/July renewals.

Q - Crystal Lu {BIO 21493547 <GO>}

Okay. Great. And I know you currently don't plan on increasing the size of DaVinci, but given current insurance-linked securities market dynamics, if there are very large catastrophes would it be more likely RenRe raises more capital within DaVinci versus from equity investors?

A - Kevin O'Donnell

I think that's a hard thing to forecast. I certainly believe that we will have ample opportunity to raise capital in both, but it will really depend on what the event is and what the market dynamics are at the time of the loss. I think being -- having the flexibility to access capital from such a wide variety of sources, no matter what the outcome is, will position us best compared to other participants in the market.

A - Jeff Kelly {BIO 20911735 <GO>}

I would just add to Kevin's answer that we feel that we have -- we do feel we have a lot of flexibility to raise capital on both balance sheets.

Q - Crystal Lu {BIO 21493547 <GO>}

Okay. Thank you.

Operator

Josh Stirling, Sanford Bernstein.

Q - Josh Stirling {BIO 17463087 <GO>}

I am wondering if you could just talk through a little bit more some of what's driving your growth in specialty and at Lloyd's. Obviously, you're coming up small bases, but generally the market is getting a bit more competitive, and love to get a sense of what your go to market strategy is here and what opportunities you guys think you are taking advantage of. Thank you.

A - Kevin O'Donnell

Sure. I think you hit the nail on the head just in your comment there, that it is off a small base, but let me talk a little bit more specifically about each of the platforms. The Lloyd's platform we have built out and built more depth into each of the underwriting teams, so we are really just accessing business that we have been accessing for the last couple of years with ample opportunity to grow. It's a very large market, and we are still a small participant.

In the US side -- excuse me, on the specialty side, we have opened a new office in the US which will allow us a little bit more flexibility to write some additional quota share type business that we wanted to have a higher degree of touch than what we are comfortable with from the Bermuda-based balance sheets, so we feel that will create some opportunity. We think there is some positive movement in certain classes on the primary side, so we will look to leverage into that.

The final piece is just regarding our economic capital model, which I touched on earlier, is this is very efficient growth for us, because it really doesn't require any additional hard capital. We are simply leveraging the efficiency within our balance sheets and structures.

So it's not that we are chasing a market where we see strong headwinds. It's really picking our spots and being opportunistic and growing it against a very efficient capital base.

Q - Josh Stirling {BIO 17463087 <GO>}

And I guess I'm curious on your specialty business, actually, I guess I will ask two follow-ups. One, I think you made the point that you're leveraging your capital, and you just drew a distinction between economic capital and hard dollars. And I guess the first follow-up is would you expect these guys to return appropriate midteens targets on an absolute allocated hard capital base, or if it's just really a marginal benefit in your economic analysis?

Then the second question is when you think about your specialty lines, is this -- some of your -- you guys are most famous doing sort of more exotic things like worker's comp and catastrophe and terrorism and so on and so forth. Is this is not -- but this is -- I guess the question is what actually are these primary lines you are doing for your customers?

And what -- you said there are some primary lines benefiting. Obviously, that is happening on the primary side. I'm curious which of these lines you guys are targeting and if they are sort of -- how they fit with the traditional RenRe focus on cat and very focused on well-modeled risks? Thanks.

A - Kevin O'Donnell

Let me take your first question, which is regarding economic and hard capital returns. I think it's a great question, and one of things we do on each deal is we look at the absolute standalone returns for a deal. Then we look at the marginal returns.

The gating issue we've had on the specialty business is the standalone returns for the deals. So is there enough profit in the deal for us to accept that level of risk? Because we know once we add in even a small degree of profit against the overall portfolio that we have, the marginal return will be higher.

So we are very, very focused on that and careful to make sure that the standalone issue -- the standalone return is understood and appropriate for the risk that we are taking.

Regarding what types of specialty lines, I think that does change a bit over time. If you look at where we have been more successful, we talk about specialty and casualty together. We have been more successful on the specialty lines, and then I would say more in some of the professional lines in specialty. That's really where we have seen some of the better rate change.

As far as workers' comp, you had mentioned that. That is not focus of where we are trying to grow the book of business.

Q - Josh Stirling {BIO 17463087 <GO>}

Great. Thanks. Good luck on 1/1. Thank you.

Operator

Josh Shanker, Deutsche Bank.

Q - Josh Shanker {BIO 5292022 <GO>}

Following up Mike Nannizzi's question, and the quota share cede, at what point in this market does it become, for you, a better market to be a buyer of reinsurance than a seller? Are we at that inflection point or how are you thinking about things here? Where is the arbitrage opportunity?

A - Kevin O'Donnell

So I think that is really a spread question. So if you go back over our history, we are kind of what I would consider to be a nontraditional buyer of retro. In that when we are looking our portfolio, we are looking at inwards business, outwards business recessions to see which and how to optimize the portfolio.

We have ceded in what I would consider to be the hardest markets, and we have ceded in what I would consider to be the softest markets. So it's not that it's a specific point where we're going to be on one side of the fence or the other. It's really how we are shaping our portfolio and how we are able to capture the best economics we can on a net portfolio basis.

Q - Josh Shanker {BIO 5292022 <GO>}

In negotiations do you need to make clear your appetite to buy retro early on, or is it widely available for you after 1/1?

A - Kevin O'Donnell

I'm not sure -- if you are asking do we disclose to our clients how we are managing our risk.

Q - Josh Shanker {BIO 5292022 <GO>}

No, no, no. More or less, if you find someone who you would like to cede business to, do you -- are you able to see where your book stands and then make that decision? Or do you have to have a view going in about how much risk you are taking on, and buy your retro as part of your renewal season package?

A - Kevin O'Donnell

Okay, so I think it's a little bit of both, actually. Since we are pro forma-ing our book of business, and we have an ability to have a much more detailed conversation with some of our capital about what the book is likely to look like.

Examples of that would be we are putting together a third-party capital vehicle like Tim, Starbound, Upsilon. We can be very precise as to what business we are likely to cede to it, where on the other side, if we are trading at ILWU or something where it really is not informed by the way we construct our book, we really don't have to have any disclosures as to the way we have constructed our portfolio or what we are likely to do.

Q - Josh Shanker {BIO 5292022 <GO>}

And in terms of the market right now, is there plenty of capacity in the market for that type of business? Or at least your view will be at 1/1 there will be?

A - Kevin O'Donnell

You mean for us to cede?

Q - Josh Shanker {BIO 5292022 <GO>}

Yes.

A - Kevin O'Donnell

I think it is one that, again, since we don't go out with the program we can be flexible and purchase our retro now, in February, in June. It doesn't matter. And it is about optimizing our portfolio, not building required capital. So I think whether it's available on 1/1, we are somewhat agnostic about.

But what we are not agnostic about is being in the discussion and being able to see what is available early, and be able to respond to those offerings quickly.

Q - Josh Shanker {BIO 5292022 <GO>}

Understood. Well thank you for all the answers and good luck.

A - Kevin O'Donnell

Appreciate it.

Operator

Jay Cohen, Bank of America.

Q - Jay Cohen {BIO 1498813 <GO>}

I guess a question on the specialty business. Looks like the accident year loss ratio is quite a bit lower than it had been running, if my numbers are correct. I am wondering what is behind that.

At the same time the acquisition expense ratio is quite a bit above what it had been running. It suggests maybe a shift in business mix. But I'm wonder if you can explain why these numbers look a bit different than the previous quarters?

A - Kevin O'Donnell

Let me touch on just the acquisition. The acquisition one is the mix is shifting a little bit from XoL to a little bit more quota share. Part of that is just the way we're repositioning some of our balance sheets with -- and the US platform. And as far as the acquisition loss ratio -- just looking for the numbers here.

A - Jeff Kelly {BIO 20911735 <GO>}

Yes, I think it is just a relatively light loss period, Jay. I don't think there's anything special going on.

Q - Jay Cohen {BIO 1498813 <GO>}

Great, thank you.

Operator

Brian Meredith, UBS.

Q - Brian Meredith {BIO 3108204 <GO>}

Jeff, just one quick numbers question. The yield on your fixed income portfolio for the quarter, does that incorporate the bank loan facilities in there for the full quarter? Or will we see a change in the Fourth Quarter result of the switch?

A - Jeff Kelly {BIO 20911735 <GO>}

That's a great question. I think it will probably change it slightly. In the context of the overall portfolio, it's a relatively small number.

But it will be included now as part of the fixed income securities portfolio as opposed to private investments or private -- privately held or other investments. So it should tick it up slightly.

Q - Brian Meredith {BIO 3108204 <GO>}

Tick it up a little bit, okay, great.

A - Jeff Kelly {BIO 20911735 <GO>}

It will be very minimal based on the size, though.

Q - Brian Meredith {BIO 3108204 <GO>}

Got you. And Kevin, two questions. First, was wondering if you could just expand your comment about the slowdown in demand that you are seeing from alternative capital providers?

A - Kevin O'Donnell

Sure. What I was saying there is we have seen the first signs of that. And what that is, is really a shifting dialogue at this point where when we're out -- we have a lot of conversations with different types of capital, either that walk in the front door or that we go out and solicit. And they are hearing a lot of the discussion on the market that rates are changing. And they are trying to understand how that is going to impact returns on the capital that they are putting forth.

So I think is one that -- if you go back seven months ago, that dialogue wasn't there. And there was just an eagerness to have discussions about cat and cat returns. I think right now that discussion is more muted because of the discussions around price change.

Q - Brian Meredith {BIO 3108204 <GO>}

Got you. And my second question, Kevin, I am just curious, as we look at your portfolio going forward in the cat book and what you retain on your balance sheet versus what you cede out to third parties and retro, do you expect that because of what's going on with alternative capital that maybe what you retain on your own balance sheet will be lower peak exposure and more of the peak exposures are going to be ceded off?

Should we see a kind of a shift going on here, since that's where the collateralized market typically is more competitive?

A - Kevin O'Donnell

That's a good point. That's a hard one to answer. If you go back to our previous call, we talked about that we were hotter down low, specifically with the 6/1, 7/1 renewal. So that's really for Atlantic hurricane.

I think we are -- because of the relationships that we have, we have a lot of flexibility to change the profile of our book. So I wouldn't want to go out and say that we're going to have more or less of one type of risk than the other. But we will leverage whatever is available in the market on both an inwards and outwards basis, to structure into making sure that we find the most desirable risk and the most efficient capital.

That sometimes may be reducing risk in certain areas or increasing risk in others. Or it might be just where we are playing either very low in the stack of capital or more exposed return periods or less exposed return periods.

But I think your point about the collateralized capital being most efficient in peak zones is an important one, because as they move outside of the peak zones, the rated balance sheet is at least as efficient as the new capital coming in. So I think it is something for the time being we should focus on within Atlantic cat.

Q - Brian Meredith {BIO 3108204 <GO>}

And on that point, do you anticipate looking forward that perhaps the attractiveness of, call it Europe versus the US, may increase a little bit?

A - Kevin O'Donnell

On a relative basis, I think that is occurring. Looking forward in our pro forma we have an anticipation of more rate competition in the US than we do in Europe. All that being said, the absolute return from US business is still higher than the absolute return for European business.

Q - Brian Meredith {BIO 3108204 <GO>}

Great, thank you.

Operator

Ian Gutterman, BAM.

Q - Ian Gutterman {BIO 3106649 <GO>}

Kevin, I guess my first question is in the press release you mentioned that our results were helped by a decision early in the year to adjust your portfolio. Can you just give a little more color on that? Are you trying to say that you got off some risks that caused losses for the market this year or were you trying to say something else?

A - Kevin O'Donnell

No. It wasn't that. It was more of how we structure it on an (expected) basis. So if you go back, we bought a cat bond. We changed the size of Upsilon. We didn't renew Tim Re.

We change the profile of the book, as I just mentioned, as to how we wrote the Atlantic hurricane season. It's all those of things combined.

Q - Ian Gutterman {BIO 3106649 <GO>}

Got it, got it; makes sense. On Upsilon, I just wanted to refresh my memory a bit. The retro that vehicle writes, how much of that -- is that for external parties reinsurance? Or is that for your own reinsurance book buying retro? Remind me who the client is on that.

A - Kevin O'Donnell

No. It is -- let me say this, so it's clear. It's protection of third parties, so it is not -- Upsilon is not writing a retro on RenRe or DaVinci.

Q - Ian Gutterman {BIO 3106649 <GO>}

Okay, that's what I thought. I just wanted to make sure. Then is there any appetite to expand it from just being collateralized retro to doing collateralized reinsurance, given it seems the primary insurers are looking to allocate portions of their program to collateralized?

A - Kevin O'Donnell

I think when we talk about it, generally the preponderance of risk that is currently in it is retro. But we do have flexibility to write reinsurance as well.

Q - Ian Gutterman {BIO 3106649 <GO>}

Okay, is that a plan to increase that this year? Obviously, as you get -- I think historically Upsilon has been a 1/1 vehicle. But to the extent a lot of Florida guys have been putting collateral slices on their programs, might we see Upsilon write some midyear too?

A - Kevin O'Donnell

We did write some risk later in the year last year as well, so I think we could -- Upsilon is targeted at a specific opportunity. I think we may -- if there is different opportunities in Florida we could always change the profile of some of the risk or some of the criteria that we have with Upsilon, or we could just start a new vehicle.

Q - Ian Gutterman {BIO 3106649 <GO>}

Okay, got it, got it. Then I guess it hasn't come up, the reserve releases were the lowest in several years. Was there any pockets of adverse that offset the normal level of releases or it was just favorable less than usual?

A - Jeff Kelly {BIO 20911735 <GO>}

Yes. It was just favorable less than usual.

Q - Ian Gutterman {BIO 3106649 <GO>}

Okay. And any specific lines that came from -- or types of risk that came from -- actual versus expected, versus actual events or anything like that?

A - Jeff Kelly {BIO 20911735 <GO>}

No, favorable -- favorable development in all segments of the business were very light this quarter.

Q - Ian Gutterman {BIO 3106649 <GO>}

Okay, got it.

A - Jeff Kelly {BIO 20911735 <GO>}

Favorable and unfavorable were very light this quarter.

Q - Ian Gutterman {BIO 3106649 <GO>}

Got it, great. I think that's all I have for now. Thank you.

Operator

Matt Carletti, GMP Securities.

Q - Matt Carletti {BIO 5249827 <GO>}

Just a quick question for Jeff. That late reported claim at Lloyd's that had a little bit of adverse prior period, can you quantify that, so we can just see what the underlying trend was there?

A - Jeff Kelly {BIO 20911735 <GO>}

It was about $3 million.

Q - Matt Carletti {BIO 5249827 <GO>}

$3 million, all right, great, thanks a lot.

Operator

And there are no further questions at this time. I would like to pass the call back to your presenters for any closing remarks.

A - Kevin O'Donnell

I would just like to thank you all for your time and look forward to speaking to you next quarter.

Operator

Ladies and gentlemen. with this we conclude today's presentation. We thank you for joining. You may now disconnect.