Q4 2011 Earnings Call

Company Participants

- Anne Waleski, VP, CFO, Treasurer
- Mike Crowley, President, Co
- Ritchie Whitt, President, Co
- Tom Gayner, President, CIO

Other Participants

- Arash Yazdani, Analyst
- David West, Analyst
- Jay Cohen, Analyst
- John Fox, Analyst
- Kevin Shields, Analyst
- Mark Dwelle, Analyst
- Mark Hughes, Analyst
- Matthew Barry, Analyst
- Ray Iardella, Analyst
- Ron Bobman, Analyst

Presentation

Operator

Greetings and welcome to Markel Corporation Fourth Quarter 2011 earnings call. (Operator Instructions). It is now my pleasure to introduce your host Tom Gayner President of Markel Corporation. Thank you, Mr. Gayner, you may begin

Tom Gayner {BIO 1896932 <GO>}

Thank you,, Lewis. Good morning. It is my privileged this morning of having the duel honor of wishing you happy Groundhog Day and welcome you to the Markel Corporation 2011 Fourth Quarter conference call. We appreciate you joining us and look forward to updating you on our progress at Markel and answering your thoughtful questions about our business. As is our custom Anne Waleski our Chief Financial Officer will update you on the numbers. My co Presidents Ritchie Whitt and Mike Crowley will update you on insurance operations. And then I will speak about our investment operations and Markel Ventures.

Before jumping in though, the rules say I must take a little swim in the Safe Harbor as such here goes. During our call today we may make forward-looking statements. Additional information about factors that could actual results to differ materially from those projected in the forward-looking statements is described under the caption Risk Factors and Safe Harbor and Cautionary statements on our most recent annual report on 10-K and quarterly report on form10-Q, and on pages 6 to 8 on our press release dated February 1, 2012. We may also discuss certain non-GAAP financial measures in the call today you may find a reconciliation to GAAP of these measures either in the press release or on our website at www.markelcorp.com in the Investor Information section under non GAAP reconciliations.

With that, Anne.

Anne Waleski {BIO 16735457 <GO>}

Thank you, Tom. Good morning, everyone. I'm going to follow the same format that I have in prior quarters. I am going to focus my comments primarily on year-to-date results. I will start by discussing our operational results, followed by a brief discussion of investment results and bring them together with a discussion of our total results for the year.

Our total revenue grew 18%, $2.6 billion in 2011 from $2.2 billion 2010. The increase is due to increase revenue from our insurance operation and non-insurance operations, which we refer to as Markel Ventures. Moving into the insurance result. Gross premium volume was just under $2.3 billion in 2011 up 16% compared to 2010. This increase was due to higher growth premium volume in the Specialty Admitted and London Insurance market segment.

As of December 31, 2011 the Specialty Admitted segment included $227 million of gross written premiums from our FirstComp workers' comp operation, which we acquired in late 2010. The increase growth in the London Insurance segment was due in part to an increase in premiums written by Elliott Special Risk, which was converted from MGA operation to a risk bearing insurance division in 2010. We also saw significant increases in our premium volume within our Marine and Energy division due in part to offering larger line sizes and improved pricing environment.

Net written premiums were approximately $2 billion up 15% to the prior year. Retention were 89% in both 2011 and 2010. Earned premiums increased 14% and included approximately $200 million of earned premiums in the Specialty Admitted segment from FirstComp compared to $37 million last year. The increase in earned premium was also due to higher growth premium volume in the London Insurance market segment compared to 2010. Our combined ratio was 102% for 2011 compared to 97% in 2010. Our goal is to earn underwriting profits and we are disappointed that we failed to met that goal this year.

The increase in the combined ratio was due to a higher current accident loss ratio. Partially offset by more favorable development of prior years loss reserve and a lower expense ratio compared to 2010. The combined ratio for 2011 included $152 million or 8 points of underwriting loss relating to natural catastrophes, including losses from the Thai floods in the Fourth Quarter and losses from Hurricane Irene, the US tornadoes, the Australian floods, the New Zealand earthquakes, and the Japanese catastrophe all of which occurred during the first nine-months of 2011. Our 2010 combined ratio included $17 million for 1 point of underwriting lossrelated to Chilean earthquake. The 2010 combined ratio also included $75 million or 4 points of underwriting loss on two programs now on runoff. That were exposed to losses associate with the adverse conditions in the residential mortgage market.

Favorable redundancies on prior years loss reserve increased to $354 million or 18 points of favorable development. Compared to $278 million or 16 points of favorable development 2010. The increase was primarily due to more favorable development of prior year losses in the E&S segments. Our 2011 expense ratio was 41% that is down approximately 1 point as compared to 2010. The lower expense ratio in 2011 was primarily due to lower cost associated with our system and profit initiatives and lower profit sharing experience.

Next I will discuss the results of our Markel Ventures operations. In 2011, revenues from Markel Ventures were $317 million as compared to $166 million in 2010. Net income to shareholders from Markel Ventures $7.7 million in 2011 as compared to $4.2 million in 2010. Revenue and net income to shareholders from Markel Ventures increased in 2011 as compared to 2010 primarily due to our acquisition of RD Holdings also know as Retail Data and Diamond Health Care in late 2010.

Moving to our investment results. Investment income was $264 million for 2011 compared to $273 million in 2010 Net investment income included an adverse change in the fair market value of our credit default swap of $4 million in 2011as compared to a favorable change of $2 million in 2010. The decrease in investment income was also due to lower investment yield which were partially offset by having a larger portfolio in 2011 compared to 2010. Net realized investments gains were $36 million in both 2011 and 2010. Unrealized gains increased $183 million before taxes in 2011 due to an increase in the fair market value of our fixed maturity.

At December 31, 2011, we held six maturities of $54 million or less than 1 % of invested assets from insurer domicile in Portugal, Ireland, Italy, and Spain. We have new insurers in Greece. We have an additional $730 million or 8% of invested assets from issuers domicile in other European countries including (inaudible). Tom will go into further detail on investments in his comments.

Looking at our total results for 2011, we reported net income to shareholders of $142 million compared to $267 million in 2010. Book value per share increased 8% to $352 per share at December 31, 2011, from $326 per share at December 31, 2010. The effective tax rate was 22% in 2011, compared to an effective tax rate of 9% in 2010. Our effective rate in 2010 included 11 points of nonrecurring tax benefits related to foreign operations and our decision last year to permanently reinvest from those operations outside of the US.

Next I will make a couple of comments on cash flow and the balance sheet. Operating cash flow was $311 million for 2011 compared to operating cash flow of $223 million for 2010. This increase was primarily due to higher cash flows from underwriting activities in the Specialty Admitted segment and positive operating cash flow from our Markel Ventures operations.

Investments in cash at the holding company were approximately $1.2 billion at December 31, 2011, as compared to a little less than $900 million as of December 31, 2010. The increase from the prior year is primarily due to the issuance of debt during the Second Quarter 2011 and dividend from subsidiary offset in part by interest payments and stock repurchases. Lastly we have repurchased 110,000 shares of our common stock for approximately $42 million in 2011.

At this point I will turn it over to Mike to further discuss operations.

Mike Crowley {BIO 6836605 <GO>}

Thanks, Anne. Good morning. My comments regarding the North America segment for the quarter will be brief. We recognize that signals and opinions on the current market conditions are mixed -- however, we are clearly seeing a property and casualty market that is in transition. During the Fourth Quarter we experienced Casualty rates that were flattening, and Property rates increasing at a modest pace. This is certainly an improvement over the rate. environment that we have witnessed for a long time.

At Markel we began seeking modest rate increases in November, and today our new and renew business success ratios have remained relatively constant. We are carefully monitoring responses to our rate actions. And will seek additional increases where condition warrant those increases without jeopardizing profitable business. Our underwriters are telling us that competition remains strong, but they are not having to, quote, fight and claw for every renewal.

While we are optimistic, we will have to see if this trend will continue in early 2012. At Markel Specialty excluding FirstComp premium was up 4% in the Fourth Quarter versus 2010, including FirstComp Markel Specialty was up 24% compared to the Fourth Quarter of 2010. Year-to-date Markel Specialty is up 3% excluding FirstComp and up 53% including FirstComp.

The main highlight in the Fourth Quarter at Markel Specialty was the announcement of our acquisition of THOMCO. This deal was closed in early January. THOMCO brings to Markel a terrific track record of program development and administration, as well as the seasoned and talented group of associates. Greg Thompson and his team will become our admitted program division, and Greg will continue his role leading THOMCO as he has done for 32 years. During 2012 we will concentrate our efforts on moving the majority of THOMCO programs to Markel paper. We will begin this process in April and continue throughout the calendar year.

Other highlights at Markel Specialty include the combination and reorganization of our property casualty and Markel Risk Solutions unit into a more focused commercial business platform. The new unit will be called Markel Specialty Commercial. This combination will result in a more streamline operation and a more clearly defined underwriting appetite.

We also took a (inaudible) of concentrated actions in our Accident and Health unit to improve the loss ratio. These changes may reduce volumes, but deliver a much improved loss ratio in 2012.

For the Fourth Quarter our E&S segment generated growth of 12% in our core products. For the fiscal year the growth in core products was approximately 7%. This growth improved dramatically from the First Quarter to the Fourth Quarter, which is evidence that our One Markel initiative is consistently gaining traction with our agents and brokers. Submission activity also increased lending further support to our belief that One Markel is working and that market conditions are in a transition to a better environment.

Our underwriting teams across the five regions of our E&S operations have stabilized, and we now have experience underwriters for virtually all of our products in all of our regions. We also continue the second phase of overhauling our agents portal to improve functionality and efficiency for those agents that are accessing us through our website.

We foresee a continue release of additional product classes available for automated pricing, underwriting, and quoting throughout 2012. During the Fourth Quarter our product line leadership group completed a review of all pricing for all major product lines and as previously mentioned began implementing changes in November.

We are taking a deliberate and class specific approach to pricing. Seeking increases across all product lines. This has been communicated both internally to all of our underwriters and to our agents. With regards to new product development, we finalized the contract of pollution coverage form tooffer as part of our binding casualty product. We believe this will be popular with our contractor Risk, which is one of our larger classes in the binding book. In summary we are ending 2012 optimistic that the rate environment is improving, confident in our underwriting teams, encouraged by the growth opportunities in both Specialties and E&S segments.

At this time, I will call turn the call over to Richie Whitt

Ritchie Whitt

Thanks, Mike. Good morning, everybody. I will be exceeding brief with my comments as well. As many of the trends that we discussed in the first three quarters in the year really continued into the Fourth Quarter. Markel International generated gross written premiums of a 148 million in the Fourth Quarter, and 825 million for the year ending 2011.

The increases for the year that was approximately 14% this is adjusted for the impact of currency movement. Again this primarily represented organic growth in our Marine and Energy division and the ramp up of written premiums from Elliott Special Risk. Elliott Special Risk is really fully reflected in our financials at this point. As result of organic growth strategic acquisition such as Elliott and the continued development of our branch office network 2011 represents the most annual premium we have written since the beginning of our international operations back in 2000.

As we all know top line growth is nice, but it is really all about underwriting profitability. Unfortunately we fell sort of our underwriting goals due to a 124 million of catastrophe losses, which included almost 19 million of Thai flood losses in the Fourth Quarter. While none of these individual losses or the losses in total exceeded our risk tolerance they contributed to a disappointing underwriting result for the year.

It was a record year for insurance CAT losses at about 105 billion, but I have to be honest it doesn't make us feel much better. We have already made adjustments to our catastrophe underwriting strategy, and we are going to continue to refine our approaches as we move forward. The biggest thing that could help in terms of making our catastrophe business more profitable, would be achieving higher prices for our capacity.

And regarding pricing January warrant renewals in London were up in many lines. We are seeing similar things to what Mike mentioned in the US. Property lines in particular were up on January 1, but I think there was a sense of disappointment as we might have hoped that given all the significant activity in 2011 we would have seen a bit more in terms of price movement in January 1.

We are going to remain patient and disciplined, and we are only going to put our capacity out there when we feel like the prices are adequate. We certainly can't predict with certainty, but we believe that prices will continue to strengthen in both Property and we think Casualty will follow as the year progresses. We certainly are going to be pushing for additional rate on the things we quote, and we will see what happens.

While we weren't happy to report an underwriting loss at Markel International and at Markel Corporation, we don't want to lose sight of the many accomplishments that our International team had in 2011. We greatly expanded and strengthened our retail branch network and created a management structure to enhance our focus on our retail branch operation. We just recently completed a small joint venture deal in Germany which is going to give us the opportunity to start learning about the German market.

Elliott Special Risk as I said earlier is fully reflected in our numbers at this point, and it is performing extremely well. The team there has done a great job. We have added key management talent, and we continue to search for and cultivate opportunities to build out our Markel International footprint and platform. We are well position for 2012 and we are really looking forward to it. With that I will turn it back over to Tom.

Tom Gayner {BIO 1896932 <GO>}

Thank you, Richie. I am pleased to report a variety of encouraging items from the investment and Markel Ventures component of Markel. First let's start with investment. In 2011 we earned a total return of 6.5% on our investment portfolio. Fixed income earned 7.6%, and equity earned 3.2% During the year interest rates started low and went lower. As a consequence we have over earned the coupon rate of returns on the fixed income portfolio. We continue to believe that rates are unnaturally low and suppressed by non market forces.

As we painfully observed with natural catastrophe in our insurance operations this year, Mother nature can swamp main made (inaudible) when she choices to do so. Consequently we remain cautious about what the forces of nature will do when the man-made levies protecting zero interest rates break. As such we continue to remain shorter than usual durations on our bond portfolio.

This means we forego current investment income in exchange for protecting the balance sheet of the Markel Corporation. We are balance sheet oriented in all we do at Markel, and we will continue to follow this path. We just simply do not believe in an extended period of zero percent interest rates and we are acting accordingly.

On our equity investment we earned 3.2% in 2011. While we don't manage versus the SMP 500, We do find it a valuable voting to provide a frame of reference about what our investment returns should realistically be overtime. I'm pleased to report to you that our return was a 110 basis points ahead of that index, more importantly over the two decades we keep track of this statistic we out performed them by 190 basis points per year.

We certainly think that two decades of data supports our case that we add value in our equity operations both against the SMP 500 index as well as against fixed income alternatives. Our four part discipline of buying stakes in businesses with good returns on capital, run by honest and talented managers with reinvestment opportunities in capital discipline at fair prices works for both public and private investment opportunities.

Speaking of private opportunities, 2011 was a very productive year for Markel Ventures. For 2011 revenues came in at about $317 million versus a $166 million a year ago. And EBITDA was $37 million an 80% plus increase compared to the $20 million in 2010. As always a reconciliation of EBITDA to net income is available on the website.

We added Weldship to manufacturer and lesser of two trailers that serves the industrial gas market in the Third Quarter. And we continue to have active discussion underway with others that would like to join Markel. We continue to build a reputation as a great home for passionate business people to build their organizations, and we will report to you our progress as it occurs.

I'd like to point out that given the lower level of interest rates in general our investment income line which is interest and dividend income declined from $273 million in $264 million in 2011. That is not surprising, it is just the math of lower interest rates coupled with our decision to protect the balance sheet by owning predominately short term rather than long term bonds.

The investment income line is the gross pretax number that doesn't take out interest expense, taxes, depreciation, or amortization. As such, I think it is comparable to and I am comfortable with adding the growing EBITDA line from Markel Ventures to get a gauge of what is happening under the hood at Markel. When you do that, the combination of these two items grew from 293 million in 2010 to 301 million in 2011.

By the way, we also had gains of 106 million in both years that are not included in those numbers. I think the fact that this number grew at Markel in the face of lower interest rates and tough overall business conditions, should provide you a sense of optimism about your Company. I am also optimistic about our outlook. And I look forward in speaking with you in future periods to update you as we continue down this path augmenting the ways in which we can create value in fair market.

With that I will stop, and open the floor for questions, for those of you with questions.

Questions And Answers

Operator

Thank you. (Operator Instructions). Our first question comes from the line of Arash Yazdani with Stifel Nicolaus. Please proceed with your question.

Q - Arash Yazdani {BIO 16172189 <GO>}

Hi. Good morning. Couple of questions. Are you guys see still seeing competition from standard carriers, and if so how big of an impact do you think that is going to have on the cycle turn going forward?

A - Mike Crowley {BIO 6836605 <GO>}

We are continuing to see competition from the standard carriers. It remains to be seen what that competition is going to look like. We don't discount it. While the market is in transition we expect to see continued competition from the standard carriers.

Q - Arash Yazdani {BIO 16172189 <GO>}

Thanks. And my next question is have you determined the impact of the new DAC accounting yet on Book value?

A - Anne Waleski {BIO 16735457 <GO>}

We have. We are going to implement prospectively, effective 1-1 as required,. And we expect to see an unfavorable impact of approximately 2 points on the 2012 expense ratio.

Q - Arash Yazdani {BIO 16172189 <GO>}

Okay. But it won't affect Book value at all since you are doing it prospectively as of now, right?

A - Anne Waleski {BIO 16735457 <GO>}

That is correct.

Q - Arash Yazdani {BIO 16172189 <GO>}

All right. That is all for me. Thank you.

A - Mike Crowley {BIO 6836605 <GO>}

Thank you.

Operator

Our next question come from the line of Mark Hughes with Sun Trust Investment. Please proceed with your question.

Q - Mark Hughes {BIO 1506147 <GO>}

Thank you. Good morning. The expense ratio you have taken a 2 point hit. The underlying expenses will they hold relatively steady, or can we anticipate some improvement there?

A - Ritchie Whitt

I think we anticipate some improvement, Mark. Obviously our gross written is growing, earned premium is growing, and those help a lot. Although obviously we are working on the expense side of the equation as well. So, yes, we would expect our expense ratio to improve a bit in 2012.

Q - Mark Hughes {BIO 1506147 <GO>}

Right. The other expenses were up a bit this quarter compared to the other revenue. Is that an anomaly, what should we expect there going forward?

A - Anne Waleski {BIO 16735457 <GO>}

I don't have handy what that is. My gut instinct is it is coming out of the increased acquisitions in the Markel Ventures realm relative to their increased revenues, but we can follow-up off line if you want and get you a more specific answer.

Q - Mark Hughes {BIO 1506147 <GO>}

I think it had been running, the expense ratio, in recent quarters relative to revenue is more like 80, high 80s. Would we expect it to return perhaps to that kind of level again relative to other revenue?

A - Tom Gayner {BIO 1896932 <GO>}

We don't think of it that way. Let me make 1 qualitative comment, and I would advise you to speak with Anne to get the details on this. As I have said earlier both in this call andevery other call in the history of Markel Corporation, we are balance sheet oriented. And I would suggest to you that that applies to the Markel Ventures operations as well.

So in purchase accounting and accounting for the transactions that are involved we tend to be some what heavy-handed and try to be conservative as possible to have the best balance sheet presentation possible, and if that is at the expense of the income statement so be it.

Given the acquisition activity and the completion to purchase accounting and that sort of thing, that was probably a bit disproportional in the Fourth Quarter. I encourage you to follow-up with Anne on the details with that.

A - Anne Waleski {BIO 16735457 <GO>}

We also as we moved Aspen from non risk to risk bearing, you may see some shift there. But like I said we can take it off line and I can give you the specifics.

Q - Mark Hughes {BIO 1506147 <GO>}

Right. Exactly. Any comments you can make regarding where you see a reserve redundancies? You had the (inaudible) Fourth Quarter releases a very good year in 2011.

A - Anne Waleski {BIO 16735457 <GO>}

Right. The reserve redundancy in prior years have predominately been in the professional and products liability lines as well as casualty programs for years between 2004 and 2009.

Q - Mark Hughes {BIO 1506147 <GO>}

What do you think about that going forward?

A - Anne Waleski {BIO 16735457 <GO>}

I would expect to continue to see prior year redundancy given our conservatism in reserving. It is possible you could see the amounts flatten out.

A - Ritchie Whitt

Yes, Mark I would add, we talk about this probably every year, we try to make sure the end of the your the balance sheet is at least conservative as it was in the end of the prior year. So we have been very consistent in terms of how we set our loss reserves and our confidence in the loss reserve. But as Anne said the realty is there is just not as much room in the last few accident years as there were in probably 2008, 2007, 2006 accident years.

So the reality is I think over time unless you start seeing price increases, and we hope we are starting to see price increases, you would expect those numbers to continue to trend down.

Q - Mark Hughes {BIO 1506147 <GO>}

Thanks for that.

Operator

Our next question comes from the line of John Fox from Fenimore Asset Managment. Please proceed with your question.

Q - John Fox {BIO 18976738 <GO>}

Okay. Thank you. Good morning, everyone.

A - Mike Crowley {BIO 6836605 <GO>}

Good morning, John.

Q - John Fox {BIO 18976738 <GO>}

First for Tom. Tom, could you give us an outlook given the acquisitions you made in the Fourth Quarter, and then possibly you made one in January? Maybe an outlook for Ventures revenue for 2012?

A - Tom Gayner {BIO 1896932 <GO>}

Sure, the acquisition in January comes from the insurance side that is not part of Markel Ventures. But for instance if you look at the Fourth Quarter the other revenue line which largely describes (inaudible) so if you times that by four that wouldn't be wildly wrong for the existing set of business that we own. We are busy, and we are talking to people in hopes to add another family or two to the Markel family over the course of the year, but we start off with that.

And then the other consistent statement I have made about the Makel Ventures revenues and this applies to the earlier statements as well. I encourage you to look at the reconciliation of EBITDA to net income and what we talked about is these business should have double digit percentages of EBITDA from the revenue line and we expect that tocontinue to be the case. And you can sort of track it through that schedule (inaudible) on a regular quarterly basis.

Q - John Fox {BIO 18976738 <GO>}

Okay. Thank you. Then I had a question on THOMCO probably for somebody else. Is it possible to quantify that impact I guess it is going to be in the Specialty Admitted line?

A - Mike Crowley {BIO 6836605 <GO>}

Yes. And THOMCO placed about a $160 million of premium in 2011.

Q - John Fox {BIO 18976738 <GO>}

Okay. So you would bring that on to your paper?

A - Mike Crowley {BIO 6836605 <GO>}

Not all of it in 2012. We do plan to convert the majority of their programs overtime to Markel paper. We will start in April.

Q - John Fox {BIO 18976738 <GO>}

Okay.

A - Ritchie Whitt

So you are not going to see a $160 million in 2012, it is going to be a progression as the year goes by.

A - Anne Waleski {BIO 16735457 <GO>}

It is about $60 million.

A - Ritchie Whitt

Our best guess today would be $60 million, but that depends on filings and all sorts of things in terms of how quickly we can get those programs moved.

Q - John Fox {BIO 18976738 <GO>}

Right. Okay. That is very helpful. This is probable a dumb question after 2011. What do you guys when you underwrite consider to be quote, unquote, normal CAT load?

A - Tom Gayner {BIO 1896932 <GO>}

The normal CAT load. That is an interesting one. I would hope it is something less than a 150 million which is what it was this year.

Q - John Fox {BIO 18976738 <GO>}

It was 8 points as I --

A - Tom Gayner {BIO 1896932 <GO>}

We would think 8 points -- as I have said Munich Re at least is saying they believe this year was a record CAT year at a 105 billion. Swiss Re kind of has the2005 and 2011 swapped from Munich Re one and two.

Q - John Fox {BIO 18976738 <GO>}

Right.

A - Tom Gayner {BIO 1896932 <GO>}

8 points. I think we did a reasonable job of managing our catastrophe exposures. I would be very disappointed if we had another 8 point kind of year. I would have to go look, John, but I think typically we run 2 points to 3 points a year would be my guess.

Q - John Fox {BIO 18976738 <GO>}

Okay. I'm just wondering if you could talk about the balance sheet philosophy with over a billion at the holding company and the rate of return on bonds being low as Tom describe for good reasons. Your yield on your bonds is much lower than your interest expense on your debt, and you have a lot of cash, your premium to surplus is low, the ratio is low. So why issue debt, and how are you thinking about the cost of your debt in the balance sheet at this point?

A - Tom Gayner {BIO 1896932 <GO>}

You are correct on each and everyone of your points. In the last couple of months the tempo of activity in Markel continues to pick up the pace. So in terms of deploying that capital and fully recognizing what it costs our internal insurance operations can and are growing. We have done a couple of acquisitions on the insurance side.

We have done a couple of acquisitions on Markel Ventures, and we also repurchase some stock, and we are going to be open minded about doing all of those things. And every single dollar we have extending on anyone of those 4 items has been something we think earns pretty good rates on return and we are productively using that capital. We see a lot of things in front of us it is nice to have ammo when we are running like this.

Q - John Fox {BIO 18976738 <GO>}

Okay. I will wait to see those. Thank you, very much.

A - Tom Gayner {BIO 1896932 <GO>}

Thanks, John. You and me both.

Operator

Our next question comes from the line of Mark Dwelle from RBC Capital Markets. Please proceed with your question.

Q - Mark Dwelle {BIO 4211726 <GO>}

Good morning. A few questions. The rated growth in the E&S segment was significantly higher in the Fourth Quarter than what we had seen in a while I guess after your comments you hadn't really pursuing rates aggressively until the mid point of the quarter. I was curious what accounted for the additional run rate in the quarter.

A - Mike Crowley {BIO 6836605 <GO>}

This is Mike. I just attended two of our agent council meetings down in Florida and the basic feedback that we are getting from the agents is the fact that One Markel decision was the right decision. We have the right underwriters in place in the field. They are pleased with what they seen with Markel. They say that our breathe of products is at least if not considerably larger than our most of our competitors.

So there are a lot of factors that are playing into our growth. Clearly getting some more rate is part of it in the Fourth Quarter. But as you mentioned we really didn't start going after rate increase and they were modest until November. We are just seeing traction in the One Markel model. Our efforts are paying off. We feel good about it. The feed back we got from both of our binding and broker agents was very positive. And the job we have to do now is just continue that momentum.

Q - Mark Dwelle {BIO 4211726 <GO>}

Would you characterize that then as new business wins or just expansion of business with existing clientele?

A - Mike Crowley {BIO 6836605 <GO>}

I think both.

Q - Mark Dwelle {BIO 4211726 <GO>}

Okay. Fair enough. With respect to THOMCO could you talk a little bit about what lines of business and what sorts of products are involved there that you would hope to bring over the books over the course 2012 and 2013.

A - Mike Crowley {BIO 6836605 <GO>}

They have a number of different programs and not all of these will be brought over to Markel paper, but they have a program for child care centers, social services, medical transportations, senior living, fitness clubs, pest control operators, inflatable rentals and some others. The medical transportation program is their largest.

Q - Mark Dwelle {BIO 4211726 <GO>}

Is the under lining product though is it commercial multi policy, or is it commercial auto, workers' comp?

A - Mike Crowley {BIO 6836605 <GO>}

Yes. It is more packaged business.

A - Ritchie Whitt

Package business just like our Specialty business and you probably heard there,Mark, there is a lot of complimentary programs there with child care and social services and some of the other things. So it really is a nice fit.

Q - Mark Dwelle {BIO 4211726 <GO>}

Okay.

A - Tom Gayner {BIO 1896932 <GO>}

Imagine, Mark, if you would, that the Pittsburg Steelers were in the Super Bowl and they won and you had a party with inflatable rentals you would want to make sure your operator has insurance. THOMCO would be the provider of that type of insurance.

Q - Mark Dwelle {BIO 4211726 <GO>}

I will look forward to getting some of that next year.

A - Mike Crowley {BIO 6836605 <GO>}

It is consistent with what we have done before in the Specialty segment.

Q - Mark Dwelle {BIO 4211726 <GO>}

Okay. My last question is you had mention the share repurchases for the year. Was there any portion of that that was in the Fourth Quarter?

A - Anne Waleski {BIO 16735457 <GO>}

There was a portion of that in the Fourth Quarter. And that number is $8.9 million to roughly $9 million about 25,000 shares.

Q - Mark Dwelle {BIO 4211726 <GO>}

Okay. Thanks very much.

A - Anne Waleski {BIO 16735457 <GO>}

Sure.

Operator

Our next question comes from the line of Jay Cohen from Bank of America Merrill Lynch. Please proceed with your question.

Q - Jay Cohen {BIO 1498813 <GO>}

Yes. Thank you. Tom, you gave me a great idea for celebrating when the Giants win the Super Bowl this year.

A - Tom Gayner {BIO 1896932 <GO>}

We are happy to sell insurance for either color tent.

Q - Jay Cohen {BIO 1498813 <GO>}

One follow-up on THOMCO have the underwriting margins for this business historically been in line with what Markel has produce?

A - Mike Crowley {BIO 6836605 <GO>}

The answer would be yes. Obviously they are written by other insurance companies and they have their own pricing and own pricing models. We are comfortable that the business will be underwritten with the same guidelines and the same conservatism that we write other lines at Markel Specialty.

Q - Jay Cohen {BIO 1498813 <GO>}

Got it. Other question interest expense ticked down a little bit. I don't know if there was a big change in the debt outstanding it seemed to go up a little bit. I'm wonder what is behind that, in the Fourth Quarter I'm talking?

A - Anne Waleski {BIO 16735457 <GO>}

In the Fourth Quarter, I'm not sure, Jay, but we can pull the details out on that and I can pick it up with you outside of this.

Q - Jay Cohen {BIO 1498813 <GO>}

Okay. I think that is it for now -- just one thing the expense ratio. So a 2 point, all else being equal a 2 point increase in the expense ratio because of the change and accounting for DAC that goes into 2013 as well, correct?

A - Anne Waleski {BIO 16735457 <GO>}

No that should all be in 2012.

Q - Jay Cohen {BIO 1498813 <GO>}

Just in 2012. That is helpful, thank you very much.

Operator

Our next question comes from the line of Matthew Barry from Lane Five Capital Management. Please proceed with your question.

Q - Matthew Barry {BIO 16707301 <GO>}

Hello, gentlemen and lady, I apologize. Mike, question for you about FirstComp quickly. I may be covering old ground, I apologize if that is true. FirstComp this year a nice little bump up in revenue that you guys can play with, but obviously at this point not profitable and was a weight on Specialty Admitted.

What I was hoping you could explain to me is a little bit about the reason for FirstComp's lack of profitability -- you're plans for addressing it and the time line on that?. And maybe if you could give me by way of explanation something of a compare and contrast with FirstComp and the rest of the business in Specialty Admitted, so we can think about how FirstComp will shake out compared to the other businesses in terms of long term profitability track?

A - Mike Crowley {BIO 6836605 <GO>}

When we acquired FirstComp we knew what the workers' compensation market looked like, and we knew that this was going to be a transition to the levels of profitability that would satisfy us going forward, and they followed that. They grew more this year than we anticipated, but they moved into a couple of new states where they were successful.

They continue to manage their California exposure well. It is a challenge. The workers' compensation market is incredibly soft. You have the issue with the various state regulators depressing the ability to price the comp the way we would like to.

At the same time we were successful in getting our cross sell efforts under way with the FirstComp sales people and the FirstComp agents. And we continue to drive growth in the whole Specialty division by selling some of our Markel Specialty products to the FirstComp agents. I think we have appointed several hundred FirstComp agents out of the 400 that we identified at this point to sell other Markel products.

We are clearly in constant discussion with the FirstComp team, and this is a transition process in terms of their success and their loss ratio and it is just going to take some time.

Q - Matthew Barry {BIO 16707301 <GO>}

Do you have a sense of the rough timeline for moving that forward and how you think profitability will shape up?

A - Mike Crowley {BIO 6836605 <GO>}

I could you give you a time line if I knew what the market was going to be. It is going to be a continuous transition. I think the --

A - Ritchie Whitt

I'll just add to that maybe, Matthew. It is tough market, and I will tell you what the results of FirstComp right now are probably more about the market than what FirstComp is doing. I think they are doing about everything we could ask them to do. They were able to grow their business a little bit by moving into some other states. They have been deemphasizing California. California is great when it's rolling and it is terrible when it is at the bottom.

So what they have done is they have really diversified -- they are diversifing their Book away from California. Which I think is going to takesome of the cycle out of the their Book going forward. The other thing we have been doing this year, and we still have a little ways to go, is we are just getting them inline with our reserving philosophy. That is a bit of a drag at the moment in terms of the results they report. They are moving in the right direction and probably are ahead of what are expectations were at this.

Q - Matthew Barry {BIO 16707301 <GO>}

Okay. That is helpful. And then one thing this is fairly general question, Ritchie, in terms of Markel International and the expansion underway over there and exciting things going on in Germany in expanding retail branch and so on. Outside of the US, do you see -- the places you are going into do you see underwriting standards above or below the US in general? Do you consider the international market ripe for pickings or a tough way to expand?

A - Ritchie Whitt

It is amazing to me it doesn't matter where you go in the world the markets are competitive. Now, some may be slightly less competitive than the US, and some are actually more competitive than the US if you can believe that. But it is amazing how global the insurance market has become, and they are all fairly competitive. But what we gone in and tried to do is go in with good teams that know that market and know what sort of price they need to be able to make an underwriting profit.

We are starting it small. We are not going in there with a big splash. We are going in with small teams and looking to build 20 million to 25 million of volume. It is a safe strategy that we are pursing. But I wouldn't kid you there is no ripe for the taking market out there right now. We certainly are hoping they are changing, but I wouldn't say any of them are ripe for the taking.

Q - Matthew Barry {BIO 16707301 <GO>}

All right. Thank you, very much.

Operator

Our next question comes from the line of David West from Davenport & Company. Please proceed with your question.

Q - David West {BIO 1838548 <GO>}

Hey. Good morning.

A - Mike Crowley {BIO 6836605 <GO>}

Hey, David.

Q - David West {BIO 1838548 <GO>}

First a little follow-up since we are talking about FirstComp a little earlier could you talk a little bit, I know state by state this can vary, but in general you gave some great color about other pricing trends, but what about pricing trends in general in the workers' comp area?

A - Mike Crowley {BIO 6836605 <GO>}

We are not seeing a lot of movement there right now, David. We expect to follow the market at some point, but we are not seeing a lot of movement. What FirstComp has done, as I said earlier, they are trying to move to states where the opportunity to get more favorable rates in their mind is the right thing to do. Moving out of the California reducing some of that exposure is the right thing to do. Keep mind they write very small Workers' Compensation policies.

I think as the market does move in a better direction we can see improvement there. They are trying to find states where there is opportunity for them to write the kind of policies that they write on the small businesses and startup at a price where the rates in the state are more competitive -- not competitive but better in terms of us getting a underwriting profit then in some other states.

Q - David West {BIO 1838548 <GO>}

Very good. Switching over to the THOMCO deal. You mention they did a 160 million related premiums.

A - Mike Crowley {BIO 6836605 <GO>}

In excess of that, yes.

Q - David West {BIO 1838548 <GO>}

In excess. What did Markel formally account for that prior to acquisition.

A - Tom Gayner {BIO 1896932 <GO>}

We didn't have any of it.

A - Ritchie Whitt

We didn't close the deal until January.

A - Anne Waleski {BIO 16735457 <GO>}

We didn't write any of that business preacquisition.

A - Mike Crowley {BIO 6836605 <GO>}

We didn't write any of the business preacquisition. They were all with our competitors.

Q - David West {BIO 1838548 <GO>}

Okay. Very good.

A - Mike Crowley {BIO 6836605 <GO>}

We had none of that.

Q - David West {BIO 1838548 <GO>}

Tom, a quick question for you. There was some modest temporary impairment charges in the quarter what constituted those charges?

A - Tom Gayner {BIO 1896932 <GO>}

(inaudible) I is a reference you to Mr. Buffet's letter to the FCC about that topic if you want to see some other points of view that talk about it, but those are the rules. Nothing that I'm worried about economically.

Q - David West {BIO 1838548 <GO>}

Very good. The European investments you mentioned in the press release that really had nothing to do with it?

A - Tom Gayner {BIO 1896932 <GO>}

No.

A - Anne Waleski {BIO 16735457 <GO>}

That had nothing to do with it.

Q - David West {BIO 1838548 <GO>}

Okay. Thanks so much.

A - Mike Crowley {BIO 6836605 <GO>}

Thanks, David.

Operator

Our next question comes from the line of Kevin Shields from Pine River Capital. Please proceed with your question.

Q - Kevin Shields {BIO 3420770 <GO>}

Good morning, and thank you for taking my call.

A - Mike Crowley {BIO 6836605 <GO>}

Morning.

Q - Kevin Shields {BIO 3420770 <GO>}

I have two quick questions. Number one, what percent of the Book are you receiving price better than trend, and for this piece of the portfolio what is the persistency say versus the average of the portfolio total?

A - Ritchie Whitt

Wow, price better than trend. I would say in general you should probably think in terms of trend as 3 to 5. And I would say in very, very few places right now are we getting price increases better than trend. For the first time in a long time we are probably getting prices in a lot -- in some places that at least equal trend. I think we are shooting for 3 to 5 in some places, and if they stick we can find some more in it.

So pretty difficult question, but I would say the industry in general hasn't been getting anything close to trend in the several years. It seems like in the transition that Mike talked about we are starting to see some price increases that might be around trend. And hopefully by the time we get on this call with you next quarter, maybe we can talk about some prices that are maybe exceeding trend. I think that is probably the best I can do on answering that.

Q - Kevin Shields {BIO 3420770 <GO>}

Okay. And for the second question that loss cost trend range of 3 to 5, can you maybe flush it out for your major lines of business like (inaudible) workers' comp, Marine and others?

A - Tom Gayner {BIO 1896932 <GO>}

That is really hard, but I would say in general in very, very general you would tend to think of your liability lines at the higher end of that particularly your professional liability lines and then your property and others things are probably at the lower end of that. But that is a very general statement.

Q - Kevin Shields {BIO 3420770 <GO>}

Thank you.

Operator

Our next question comes from the line of Ron Bobman of Capital Returns. Please proceed with your question.

Q - Ron Bobman

Somebody made the comment early on the call that basically FirstComp was at or sort of ahead where you I guess expected it to be. I'm not sure if that was referring to sort of the transition pace or profitability?

A - Ritchie Whitt

That refers to top line.

Q - Ron Bobman

As far as top line. Okay. So it is not indicative of -- I think their was an earn out on the acquisition whether that earn out is on track to be earned or not, any insight on that? That is my only question.

A - Tom Gayner {BIO 1896932 <GO>}

The earn out was really on the opening balance sheet at this point it is nothing at this point is what the calculation would show. This is workers' comp business, so it take as while to develop so that could change. The earn out was really about the snapshot balance sheet the day we bought it.

Q - Ron Bobman

Okay. Thanks, guys, best of luck.

A - Mike Crowley {BIO 6836605 <GO>}

Thanks.

Operator

(Operator Instructions). Our next question comes from the line of Ray Iardella from Macquarie. Please proceed with your question.

Q - Ray Iardella {BIO 16279337 <GO>}

Good morning, guys. Just a couple don't want to ask all about FirstComp on the call. A couple of quick ones regarding, what states are you diversifying away from California. I know you had talked about some better premium growth there and diversification? Any clarity would be helpful.

A - Mike Crowley {BIO 6836605 <GO>}

We went into Louisiana and I am trying to remember what the other state was. Alaska I think. Louisiana and Alaska I think. Seems like there might have been one more, but I would have to get that for you.

Q - Ray Iardella {BIO 16279337 <GO>}

Okay.

A - Tom Gayner {BIO 1896932 <GO>}

Also with what the team has been doing is where they see better profitably states they have been pushing harder in those states and trying to grow the business there. They have been raising prices obviously as a lot of people have in California particularly in the areas where we are not seeing good performance in some extent you are shrinking California or what you are writing in California is a rate your more happy with. In other states where we are happier with the pricing environment we are trying to grow in those states. It is really a portfolio balancing exercise that those guys are working through, and I think they are doing a good job.

Q - Ray Iardella {BIO 16279337 <GO>}

Understood. I just wanted to make sure it wasn't some of the more problematic states that other people have talked about like in Illinois or potentially New York. I would assume you guys would be targeting the more profitable, I just wanted to double check.

A - Tom Gayner {BIO 1896932 <GO>}

We have a lot of the confidence in FirstComps' management in making those decision. They really have a very strong culture of metrics in understanding their business. We have an a lot of confidence that any moves they make will be in the right state.

Q - Ray Iardella {BIO 16279337 <GO>}

Okay, got it.. A quick one on the reserve side for FirstComp. I don't know if I did the math right, but I think for the year there was a little bit of adverse development from that business. I know you guys have a different reserving policy. I am just curious is that any particular accident year or is it across the board to get it up to your reserve philosophy.

A - Tom Gayner {BIO 1896932 <GO>}

I don't want to delve into details, but I want to add a sense of historical perspective to this. If we had to do the FirstComp deal all over again we would all do it. Enthusiastically in a New York minute. The point I want to make is if you look at any deal we have ever done in Markel, we have always had the practice of wanting to be more likely to be redundant indecision in our reserve, and that always has a time lag associate with it where reserve philosophy are harmonized across the various Markel units.

2011 we knew it going in, we know it right now that those reserve and philosophies are being harmonized, but we can see and feel and taste and touch the business that they are writing and the intelligence which they are pursuing their business to have a great deal of confidence in it. And in the (inaudible) time this deal like all the other deals will work out well for our shareholders.

Q - Ray Iardella {BIO 16279337 <GO>}

I appreciate that. And I know your history as far as reserving is concern. I guess 6 million doesn't seem like a lot to me, and if you are moving around reserves in the older accent years from more recent ones? Color like that would certainly be useful from our end.

The other question I want to ask about quickly is catastrophe exposures. I know you guys had said you had taken a step back and kind of looking at what you thought about catastrophe, but do you have any specific metrics you look at? I know you mentioned getting price increases you certainly be more willing to deploy some capital for CAT exposure, but just trying to get a sense of where you would think about that business going forward?

A - Tom Gayner {BIO 1896932 <GO>}

We like all the people that write this business we have a lot of metrics we look at and without getting into too much detail we clearly look at our 1 and 250 return period numbers. We do bootstrap method and just add up the TIV. we have gotten gates around the coast for winds. We look at the crustacean zones in California and make sure we are comfortable we are not overloaded in particular crustacean zones.

We have lots of metrics we look at, but the big thing we are doing right now is just continuing to focus on that and make sure we feel like we are making the appropriate moves and we are looking to increase pricing because we believe this business needs more price given the sort of events we saw in 2011.

So I think we made a lot of changes since 2005 and Katrina. We believe we have improved our methodology and approach significantly. But it is always evolving and we are always going to keep looking at it and try to continue to improve. When you write catastrophe business, you never want to get too comfortable. So we are always going to be looking and trying to get better.

Q - Ray Iardella {BIO 16279337 <GO>}

Great. Appreciate the color. Best of luck.

A - Tom Gayner {BIO 1896932 <GO>}

Thanks.

Operator

Our next question comes from the line of Jay Cohen from Bank of America Merrill Lynch. Please proceed with your question.

Q - Jay Cohen {BIO 1498813 <GO>}

Thanks. Just one quick numbers question. Do you happen to have the statutory surplus as of year end?

A - Anne Waleski {BIO 16735457 <GO>}

No, we don't have that yet, Jay. It will be a couple more weeks on that.

Q - Jay Cohen {BIO 1498813 <GO>}

Okay. And I guess more theoretical question. The make up of your earnings between accident year and prior year development is clearly much different than other companies far different. I mean essentially you are not making money on an accident year basis if we exclude the favorable development.

I think even if I added back catastrophe you wouldn't be. And clearly there has been this history of conservative reserving at the Company. But are you set up where you would at least expect to make money on an accident year basis? In other words, it feels as if you are being way overly conservative or maybe the world just has to catch up with you, what do you think is closest to the truth?

A - Ritchie Whitt

I would say, I don't know if you can get the numbers out of our annual reports I think you can. What you just describe has been consistent with Markel throughout time we are very conservative on the current accident year, and then overtime as things develop we allow that to come down. And that is just the way we have always done it.

I think I mention earlier there is no question the 2011 accident year is thinner than 2010 was and thinner than 2009 was. We still did everything we could to price it to an underwriting profit. But it is not going to be what 2010 was it is not going to be what earlier years were.

Q - Jay Cohen {BIO 1498813 <GO>}

It sounds like 2012 is going to be even worse because your price increases aren't yet keeping up with claims inflation? What is the underlying pressure there, ex catastrophe.

A - Ritchie Whitt

Well, I guess the thing I would say there is you estimate trends just as you estimate a lot of other things. The thing I think has probably surprised a lot of people in the last few years is trends have been somewhat benign. But you name it on trends, on our development factors we are going to be conservative on all of it. Watch it and our hope and expectation would be that it comes down over time.

A - Tom Gayner {BIO 1896932 <GO>}

And the one thing I would is add, Jay, in terms of philosophy, obviously the accounting is one issue which you rightly raised, but the good news is that we do get the cash on day one and those dollars regardless of whether we recognize the income from it this year or subsequent years those dollars do flow into the investment portfolio and start creating returns for shareholders.

Q - Jay Cohen {BIO 1498813 <GO>}

Absolutely. And I guess one last point, last question on this. I have had other companies tell me they try to get there accident number as close to accurate as possible because that gives them some insight into pricing. If we are way off either way it will give us misinformation on how we should be pricing the business. It doesn't seem to be impacting you.

I mean your pricing from what I hear in the market is pretty consistent and you are not way too high or low. Is that just an inaccurate statement that an accident year number has a lot of information content relative to how you price the business going forward?

A - Tom Gayner {BIO 1896932 <GO>}

They are certainly links, Jay, and I think part of why it works for us is we have done it a long time and we have done it consistently this way. We talk a lot about margin of safety and we talk about the fact there is a margin of safety in our loss reserving. We may take a slightly different view as we sit down to really come up with a pricing methodology.

There might be a slightly more conservatism in our reserving pick then there would be in our pricing pick. We spend a lot of time talking about those two numbers to make sure they are not disconnecting. They can be different but they can be different but we don't want them to disconnect.

Q - Jay Cohen {BIO 1498813 <GO>}

Got it. That's a helpful answer. Thanks a lot guys.

Operator

Our last question comes from the line of Ron Bobman from Capital Returns. Please proceed with your question.

Q - Ron Bobman

Actually I am doing a follow-up. Two questions having Greenburg on the Ace call yesterday. I think twice he made comments about the E&S Causality market. I think he used the work an area of stress or severe stress. I was wondering if you would describe either large pockets of or large portions of the E&S Casualty market experiencing stress?

That was sort of the first I had heard of it described as an extreme. And then I also noted I think I haven't heard any of the Markels on the call today. Am I right and is this a new procedure for the calls? Thanks.

A - Tom Gayner {BIO 1896932 <GO>}

Well, I will make two comments. One, we didn't hear Mr. Greenburg's comments from Ace, so we can't comment on comments we didn't hear. I wouldn't know how to address that. Yes, this has been the line up here for a year now or so, year and a half. We are here, and the Markels, I can assure you are listening as well, and will coach us as soon as we walk out of the room.

Q - Ron Bobman

How would you just generally describe E&S Causality as a stressed segment?

A - Ritchie Whitt

The only comment that I would make is we are not seeing significant price increases in the US Casualty market at this time.

Q - Ron Bobman

Okay. Thanks that is good.

Operator

There are no further question at this time. I would like to hand the call back over to Tom Gayner for closing comments.

A - Tom Gayner {BIO 1896932 <GO>}

Thank you, very much we are glad you were with us, and we look forward to catching up with you very soon. Take care.

Operator

This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.