Q1 2019 Earnings Call

Company Participants

- Francois Morin, Executive Vice President, Chief Financial Officer and Treasurer
- Marc Grandisson, President and Chief Executive Officer, Arch Capital Group Ltd

Other Participants

- Amit Kumar
- Elyse Greenspan
- Josh Shanker
- Meyer Shields
- Mike Zaremski
- Yaron Kinar

Presentation

Operator

Good day, ladies and gentlemen, and welcome to the First Quarter 2019 Arch Capital Group Earnings Conference Call. At this time all participants are in listen-only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. (Operator Instructions). As a reminder this conference call may be recorded.

Before, the company get started with its update, management wants to first remind everyone that certain statements in today's press release and discussed on this call may constitute forward-looking statements under the Federal Securities Laws. These statements are based upon management's current assessments and assumptions and are subject to a number of risks and uncertainties. Consequently, actual results may differ materially from those expressed or implied. For more information on the risks and other factors that may affect future performance, investors should review periodic reports that are filed by the company with the SEC from time to time. Additionally, certain statements contained in the call that are not based on historical facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995.

The company intends the forward-looking statements in the call to be subject to the Safe Harbor created thereby. Management also will make reference to some non-GAAP measures of financial performance. The reconciliation to GAAP and definition of operating income can be found in the company's current report on Form 8-K furnished the SEC yesterday, which contains the company's earnings press release and is available on the company's website.

I would now like to introduce your host for today's conference Mr.Marc Grandisson and Mr.Francois Morin. Sir's, you may begin.

Marc Grandisson {BIO 4369887 <GO>}

Thank you, Crystal, and good morning to you all. We have had a good start to the year as Arch grew book value per share by 7.4% to $23.12 at March 31 and generated operating earnings of $0.67 per share due to strong underwriting and investment results in the first quarter of 2019. As mentioned on our call last quarter, we continue to see modest upward rate movement in property and select casualty lines, along with reductions in ceding commissions paid by our reinsurance units. Our mortgage insurance or MI group, continues to operate in a market characterized by historically strong credit conditions and conservative lending standards. For Arch, this is an underwriting market where selection and segmentation remain key to generating favorable results. It is not a one size fits all market by any means.

On the one hand, we believe that the modest improvement in the property and casualty markets reflect broader economic growth particularly in the United States, while on the other hand we see inconsistent evidence of increased discipline by underwriters. We can sum up our view of current market conditions with two key virtues that describes how we operate at Arch prudence and patience.

Prudence has been a good advisor to us. In our P&C segments, rate changes in the quarter for our Insurance Group has been positive, but ranging in any one line from minus 5% to plus 8% averaging about plus 2.3%. Considering that insurance loss trend, our claim inflation typically runs about 200 bps above the CPI, we remain prudent in setting our loss picks and allocating additional capital in any single line given the uncertainty of future loss costs.

Prudence in our reserving process dictates that we maintain an appropriate margin for error because reserving errors can lead to pricing errors. We saw modest growth in the first quarter of 2019 in our Insurance Group as net written premium increased 8% due in part to the UK acquisition we mentioned last quarter.

The balance of the growth was from a combination of rate and new opportunities in short and medium tail lines. In typical Arch fashion, we remain focused on risk-adjusted returns and patience means that we seek evidence of acceptable margin improvement even as the market experiences some pullback in capacity such as in the larger commoditized lines and also within some E&S markets that you have heard about on other calls. Within our Reinsurance Group, property cat exposed rate are moving up after absorbing severe industry wide catastrophe losses these past two years. These losses have caused some dislocation in capacity across the industry and have paved the way for new opportunities which our underwriting teams were able to participate in. However, we remain focused on the absolute level of risk adjusted rates and selective in our approach to cat exposed business.

Now, turning to our MI segment. Overall the underwriting environment remains very attractive. Growth in our insurance in force is producing increases in earned premium and contributing to a future stream of earnings, that is strong and predictable . In MI, the key underwriting characteristics that drive earnings are credit quality and the economy, with which more than pricing drive ultimate performance. Therefore, even as pricing has become more competitive credit quality remains excellent and key macroeconomic factors are very good, which has resulted in very strong risk-adjusted returns.

As you may know, in MI from an accounting standpoint, these returns will be reflected in earnings, over several years. For the first quarter of 2019, our U.S. MI new insurance written or NIW, was $11.2 billion down about 2% from the same quarter a year ago. While NIW, reflects business written in the quarter, the more relevant indicator of insurance earnings is insurance in force, which Arch MI U.S. grew to $277 billion at the end of March of 2019. As with all our business units, in MI, we are focused on returns rather than market share and we intend to remain disciplined and agile. We believe that our long experience with RateStar and our insurance linked notes known as Bellemeade Securities provide Arch a competitive advantage with respect to risk management, our interface with lenders and our upfront risk selection.

As I alluded to earlier, our key risk parameters are at very healthy level levels. Credit quality as indicated by FICO scores remain strong across our enforced book with a weighted average score of 743. Our combined ratio in our MI segment remains exceptional 25.6% in the first quarter, which is substantially better, than the long-term industry average of the mid to high '40s.

With respect to our investment operations, higher yields available in the financial markets produced excellent results on both a yield and total return basis. Turning briefly now to risk management. For the past few years, and continuing into 2019, our property cat exposures remain at historically low levels with a 1-in-250 year peak zone at about 4% of tangible common equity at April 1.

In our MI segment, our issuance of Bellemeade Securities continued the pace with our second issue this year that closed yesterday and provides $620 million of reinsurance indemnity on more than $35 billion of insurance in force. We have issued $3.5 billion of Bellemeade Securities over the past four years which remains an important part of our risk management capabilities.

As of today, Bellemeade Securities provide protection on more than 90% of our existing insurance in force. With regards to PMIERs as of March 31 2019, Arch MI's U.S. sufficiency ratio was 146% of the GSE capital requirements known as the PMIERs as I mentioned. With that in mind and with that, I will turn it over to Francois, Morin to provide you more specifics on our quarterly results. Francois?

Francois Morin {BIO 17410715 <GO>}

Thank you, Marc, and good morning to all. Before I give you some comments on observations on our results for the first quarter, I wanted to remind you that consistent with prior practice, these comments are on a core basis which corresponds to Arch's financial results excluding the other segment.i.e., the operations of Watford Holdings Ltd. In our filings the term consolidated includes Watford.

As you know, Watford's common shares began trading on the NASDAQ global select market, on March 28, 2019. While this event now provides a market price on the value of our ownership in Watford, it does not impact the presentation of our financial statements or any of our disclosures which have remained unchanged since Watford's formation in 2014. After-tax operating income for the quarter was $275.9 million which translates to an annualized 12.3% operating return on average common equity and $0.67 per share. Book value per share was $23.12, at March 31st, a 7.4% increase from last quarter and a 13.3% increase from one year ago. This result, reflects the effect of strong contributions from both our underwriting operations and our investment portfolio.

Moving on to underwriting results. Losses from 2019 catastrophic events in the first quarter net the reinsurance recoverables and reinstatement premiums stood at $7.9 million or 0.6 combined ratio points. These losses, were nearly all observed in the results of our reinsurance segment, which were impacted by a handful of minor events across the globe. As for prior period, net loss reserve development, we recognized approximately $36.7 million of favorable development in the first quarter net of related adjustments or 3.0 combined ratio points, compared to 4.6 combined ratio points in the first quarter of 2018. Both the insurance and the mortgage segments experienced favorable development at $1.7 million and $36.6 million respectively.

The reinsurance segment experienced the minor amount of approximately $1.6 million of adverse development including 16 million related to Typhoon Jebi. The increase for this event reflects updated loss information received from scenes [ph] and additional industry data. The mortgage segment benefited from significant favorable development in our first lien portfolio or cure rates observed in recent quarters continued to be materially better than long-term averages and expectations. The insurance segments accident quarter combined ratio excluding cats was 100.2%, 150 basis points higher, than for the same period one year ago. The year-over-year comparison for the insurance segment is affected by two notable items.

First, as we mentioned on our previous call, our operating expense ratio was impacted by the shift in the timing of share based compensation from the second quarter to the first quarter. This shift increased, the first quarter expense ratio for this segment by approximately 94 basis points relative to one year ago. Second, we continue to invest in our insurance operations, including the integration of recent acquisitions in the U.S. and the U.K. The most notable impact to our expense ratio this quarter relates to our U.K. regional book, whose operating expenses added 110 basis points to our overall expense ratio for this segment.

As mentioned in the earnings release, we did not acquire an unearned premium portfolio with this acquisition and as a result the expense ratio will remain higher than the long-term run rate until the associated earned premium reaches a steady state. Overall, the underlying performance of our insurance segment showed improvements in the quarter mostly due to lower levels of attritional losses and acquisition expenses. The reinsurance segment accident quarter combined ratio excluding cat stood at 92.4% compared to 93.4% on the same basis one year ago.

As we mentioned on prior calls we tend to look at trailing 12 month analysis in order to assess the ongoing performance of our segments given the inherent volatility in the business that can emerge from quarter-to-quarter. The year-over-year comparison for the reinsurance segment is affected by the presence of a $10.2 million premium retroactive reinsurance transaction, we entered into this quarter, which contains sufficient risk transfer for insurance accounting treatment under GAAP.

While the overall combined ratio for this segment was basically unaffected. The impact of the transaction to each of the loss and expense ratio components was more observable, with the resulting increase of 90 basis points to the loss ratio and a decrease of 80 basis points to the expense ratio. Overall, we were able to reduce our expense ratio by approximately 400 basis point, mostly as a result of the growth in earned premium. Since the same quarter one year ago. The retroactive reinsurance transaction just mentioned and the shift in business mix. Once we adjust for these variations, the underlying performance of our reinsurance segment will remain stable this quarter. The Mortgage segments accident quarter combined ratio improved by 650 basis points from the first quarter of last year. As a result of continued strong underlying performance of the book, particularly within our U.S. primary MI operations.

The calendar quarter loss ratio of 3.5% compares favorably to the 15.5% in the same quarter of 2018, due to substantially lower delinquency rates. Part of the difference is also attributable to increased favorable prior year development, which was approximately 670 basis points higher, than last year. The expense ratio was 22.1% lower by 120 basis points than in the same period one year ago as a result of a higher level of earned premiums.

Total investment return for the quarter was a positive 270 basis points on a US dollar basis and a positive 348 basis points on a local currency basis. Contributing to this result was our decision to extend our portfolio duration slightly during the second half of 2018, combined with the defensive high-quality position of our fixed income portfolio and the solid performance of our equity portfolio consistent with the recovery in global financial markets.

The repositioning of our portfolio, during 2018, combined with the reinvestment of shorter maturity bonds of higher yields generated higher investment income year-over-year. We also benefited from higher than usual investment income from investment funds in the quarter. The corporate effective tax rate in the quarter on pre-tax operating income was 13.1% and reflects the geographic mix of our pre-tax income and a 50 basis point benefit from discrete tax items in the quarter.

As a result, the effective tax rate on pre-tax operating income excluding discrete items was 13.6% this quarter higher than the 10.4% rate from the same quarter last year. At this time, we believe it's still reasonable to expect that the effective tax rate on operating income will be in the range of 11% to 14% for the full year. As always, the effective tax rate could vary depending on the level and location of income or loss and varying tax rates in each jurisdiction.

With respect to capital management, we repurchased approximately 111,000 shares at an average price of $25.96 per share and an aggregate cost of $2.9 million, under our Rule 10b5 plan, that we implemented during this quarter's closed window period. Our remaining authorization, which expires in December 2019, stood at $161 million at March 31.

Our debt to capital ratio stood at 14.6% at quarter end, and debt plus preferred to total capital ratio was 21.2%, down 130 basis points from year-end 2018. With these introductory comments, we are now prepared to take your questions.

Questions And Answers

Operator

(Question And Answer)

Thank you. (Operator Instructions) (Operator Instructions). Our first question comes from Josh Shanker from Deutsche Bank. Your line is open.

Q - Josh Shanker {BIO 5292022 <GO>}

Yeah, thank you very much. Mark, I appreciate your comments about CPI and lost cost trend, look I think that at the very time you make a change in your outlook it might be the wrong time, but if you look at the past few years, what has been the lost cost trend and what year you're comfortable making that statement about, what year is two green and what years can you say yes, we know where the lost cost front wasn't say 2015?

A - Marc Grandisson {BIO 4369887 <GO>}

I think. Yes. So you have to -- it takes about three to four years to redevelop, and we're talking about primary business to really get a good sense of the CPI. So I think, if you look at the CPI I mean, we know what it is 1.8%, 1.7%, 1.9% that range has been consistent for the last two to three years. The pickup in the delta that I talked about the claim inflation spread above that CPI takes two to three years. So we have some good sense for probably 2015, 2014, 2016, we still have things developing for more reason underwriting years. And I would add that it's even more problematic or more difficult to fully assess when you in a specialty line of business and when you have of course excess policies.

Q - Josh Shanker {BIO 5292022 <GO>}

Generally, speaking was '15, '16 about 200 basis points above the lost cost -- above CPI?

A - Marc Grandisson {BIO 4369887 <GO>}

It was a bit above, that I believe. If I last time I checked the numbers about six months ago. We had a 150 bps above the CPI in trend inflation from '09 to about 2012 and I think it's since then picked up. So, I'm trying to look at a long-term average it's very hard to pin down the exact numbers.

Q - Josh Shanker {BIO 5292022 <GO>}

And I hope I can get two and a half questions in but there's some related.

A - Marc Grandisson {BIO 4369887 <GO>}

Okay

Q - Josh Shanker {BIO 5292022 <GO>}

I want to understand this structure of your Jebi exposure, I don't know how much you initially fixed for it, but you're not a big Japan player and you're not a huge property cat player. So I'm just trying to figure out what happened in the contract that you paid more, obviously the picks went up there and two, to what extent are higher reinsurance costs particularly on the Japan renewals that just passed, and then when you get to Florida, and the Gulf in the mid-year to what extent are the pricing increases we're seeing in property going to get somewhat swallowed by higher reinsurance costs.

A - Marc Grandisson {BIO 4369887 <GO>}

Okay. So that's about 3.5 questions. But I'll sort of take one at a time. The first one on Jebi. You're quite right our exposure has been on the weight for quite a while. We had actually, increased our exposure to quake of the Tohoku earthquake, but on the win side you're right we had been more careful. And this one is having a small amount of limits out there, mostly on the excess of loss basis and Japan also buys somewhat on the combined business, but most of all our exposure is on the wind and flood only still to this day. And really the initial numbers came in at $3 billion as you know developed to about $12.5 billion to $13 billion we believe as we speak.

What was missed by our ceding company not only by the reinsurance community was the business interruption and contingent via loss exposures that we're inherent in, exactly the location, where Jebi hit, and a lot of it had to do with semiconductor that carry a lot of issues a lot more issues from the BI and CBI perspective, which was not properly reflected, when you went through the path of the storm and modeled it that through the your existing portfolio exposure and the ceding companies had done the same thing, did not see happen, did not see this developing and it just so happened that it created it was not fully appreciated by most people by the whole market frankly.

So, this is sort of, where we are right now with Jebi. So, you talked about price increase, we've had we've seen some price increase in April 1st, as you know in Japan. But the price increase that we saw brought us back to about 20 -- the grade level in 2014. So, with a lot more subdued and lot more attained than we would have hoped for, based on those that indicator Josh, knowing us that we've increased somewhat but did not go significant increase. We are still trying to be patient, in seeing further rate changes.

As we talk about Florida, the initial discussions are that the demand is going to be stable but the supply of reinsurance is taken a pause. We don't know yet where it's going to go, but initial sign is that, it's taken a pause which should mean an interesting renewal from a reinsurance provider perspective.

Q - Josh Shanker {BIO 5292022 <GO>}

I was more interested in your outwards costs more than inwards opportunity. As you pay more for Reinsurance, does that limit the extent of these rate increases we're seeing in property lines?

A - Marc Grandisson {BIO 4369887 <GO>}

Well, no. Because, the big reinsurance purchase that we would do, would be on the insurance side. And we don't, we do not have a significant Florida or these kind of exposures, that would have created the loss into our layer. So we have a very different exposure from our cat perspective. So it doesn't really factor itself into pricing and it's not a significant change.

Q - Josh Shanker {BIO 5292022 <GO>}

That's perfect. Thank you very much.

A - Marc Grandisson {BIO 4369887 <GO>}

Thank you.

Operator

Thank you. Our next question comes from Amit Kumar from Buckingham Research. Your line is open.

Q - Amit Kumar {BIO 15025799 <GO>}

Okay, and good morning. Maybe two questions. The first one is a follow-up on the Jebi question. Can you also talk about, I guess, what's your -- what was your Trammy [ph] exposure and also talk about if there were any aviation losses in the accretional loss ratio?

A - Marc Grandisson {BIO 4369887 <GO>}

Well, first of all our Trammy exposure is de minimis, we have basically none. And the question in aviation is not something we're a big participant in. So it's also de minimis in terms of aviation losses part of the accretional loss.

Q - Amit Kumar {BIO 15025799 <GO>}

Got it, that's helpful. The other question, I guess, the only other question, I have is going back to Joshua's question. There is this sort of debate emerging between E&S pricing and commercial pricing and you haven't talked about this a lot earlier today. Can you maybe just spend some time? You gave us a range of minus 5% to plus 8%, and then that came out to plus 2.3%? Can you just talk about, how you're feeling about pricing versus loss cost trends in some of those lines and what would be the lines, where we're still trying to get rate increases? And how should we think about 2019 or is it time to sort of sharpen our pencils and think about margin expansion from here? Or would that be premature? Thanks.

A - Marc Grandisson {BIO 4369887 <GO>}

Yeah. So I think the best answer I can give you on what we think of where the margins are? Is, if you look at where we grew premium in this quarter. That will give you great indication so as to what our teams think in terms of absolute margin. Margin expansion is one thing, but it doesn't mean it's necessarily enough to get the return. So we've seen enough margin expansion in a few lines that we grew our exposure. What is the second part of the question again?

Q - Amit Kumar {BIO 15025799 <GO>}

In terms of some of those lines and adequacy in those lines versus loss cost trends?

A - Marc Grandisson {BIO 4369887 <GO>}

Yes The ones that we grew on a shorter tail of sign mostly, most of the growth has been in a shorter tail lines and the reason it's a little bit more easier to do so a because the lost costs are a little bit easier to pin down. You have loss less uncertainty about ultimate loss costs on the shorter tail lines. So that means that if you think you are perceived you're preceding a margin safety of rate above loss trend of X, you're more certain you're going to get this. In other lines of business such as E&S casualty, we like others have seen some pick up in pricing there, but there's a lot more uncertainty there in terms of what the gap between lost cost and end rate increase is and I would argue with some of them in some lines of business even though we would look to have like a 300 pickup let's say in margin they probably need a bit more than that to really make a big allocation of capital from our perspective. So it's really a transition and really an incremental marketplace.

A - Francois Morin {BIO 17410715 <GO>}

Yes. One thing I'll add to that just quickly on -- I mean the London market, as you know is going through a period of dislocation. We benefit from that we're not huge players in London, but we have a meaningful participation and -- both on the syndicate and the company side. Who knows, whether that is going to be sustainable for the rest of 2019 and into 2020 but certainly as Marc, alluded to some of the growth, we saw in the premiums, we wrote in Q1 are specifically related to opportunities in London in particular.

Q - Amit Kumar {BIO 15025799 <GO>}

Got it. I will stop here for the moment and I'll reach you. Thanks so much for the answers.

A - Marc Grandisson {BIO 4369887 <GO>}

Thanks, Amit.

A - Francois Morin {BIO 17410715 <GO>}

Thank you.

Operator

Thank you. Our next question comes from Elyse Greenspan from Wells Fargo. Your line is open.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Hi, thanks. My first question on the reinsurance side. Marc, in response to an earlier question. You said that supply is taking a pause. So now when we think about supply of capital in Florida. Is that a comment that you would make to overall capital to alternative capital to traditional capital, I guess as you think about the buckets of the capital sources for the upcoming part of renewals you could give us a little bit more color on how you think this will play out?

A - Marc Grandisson {BIO 4369887 <GO>}

Well I don't know how it's going to play out. I'll just talk about the early signs. But in terms of where it's coming from the supply the pause has been taken by all participants, because, implicitly in some of the traditional players, some of it is relying on alternative capital and is also alternative capital stand-alone as well. So, it's really it taking a step back. There are lot of moving parts in Florida. The (inaudible) benefits, the LAE adjustments and whatever else, the department asking for buying more limit. I mean there is a lot of moving parts right now, so people are still and people are waiting to see more up-to-date numbers, they've been developing as we all know for several quarters now. So everybody's taken a part.

I think it's a collective, it's not obviously a consensus that's developed by talking to one another obviously, but it seems to be this taking a pause positioning from the supply. But we've seen as before these, I want to be open. Sometimes, you see this and at the end people sort of roll over and do act differently than you would have thought they would behave. But, I'm just telling you, as we speak last information that I received this morning about the current state of the overall feeling in the marketplace

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay, thanks, and then back to some comments you guys have been making throughout the call on the primary insurance market. So it sounds like you guys are finding more opportunity in the shorter tail lines as opposed to some long tail lines. Just given on, some concerns about loss cost. Another company earlier today pointed to this being a casualty driven market upturn. Would you agree with that statement and maybe there's just, you guys are holding off really pushing for growth on the casualty side, just given -- waiting to see how loss translates out?

A - Marc Grandisson {BIO 4369887 <GO>}

So, well, I don't know if it's casualty led, but we've seen in terms of where we've allocated our efforts. Our efforts in capital such as that Francois mentioned, a lot of it is led by cat exposure and marine exposure and short tail exposure. So this is where we've been more allocating capital for the last six quarters, for three to four quarters and still continue on as we speak this quarter.

On the liability side for us to have a casualty led we would still need to see some pain in the marketplace. We're not seeing broad pain yet at least emerging on the insurance portfolios. What I would tell you and that might probably sort of size or is in line with what you the comment that was made earlier on some calls is that, the reinsurance market is actually being a bit more disciplined, a bit more reactive to the casualty placements. And that tells us indirectly that there's probably a bit more negative perception about the ultimate results in those numbers but I'm not sure that these results have been published. Yes.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay. And then, you see sorry, one last question. Are you seeing more business come from the standard market to the E&S market?

A - Marc Grandisson {BIO 4369887 <GO>}

Most of what we see is through, the E&S market. Most of the growth except for the UK regional obviously which is the specific focus but yes, the Lloyd's market, the Lloyd's business and the E&S market is where we are seeing more opportunities. Yes.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Then sorry, one last question. On the intangible what were a little bit higher than I'd have thought this quarter I think that's due to your two newer acquisitions, is that Q1 level kind of a good run rate for this year and can you give us a sense of where the intangibles amortization expense might come in in out years?

A - Francois Morin {BIO 17410715 <GO>}

Yeah. Well, certainly yes the part one, our practice for the amortization of the intangibles is linear throughout the year. So you should expect the remainder of 2019 to be at very much close to the same level that we had in Q1.

In terms, of outer years, we had given direction on specifically on the UGC transaction how it was going to wind down in 2020 and beyond. So we'd happy to recirculate that and give you an update on that. But that's very much scheduled and we know where we're at it's going to be. I don't have the numbers in front of me for 2020, but we can certainly, yes, give you that.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay, so the UGC numbers aren't changed and it's just up a little bit in the two recent yields?

A - Francois Morin {BIO 17410715 <GO>}

Exactly, that's correct, yes. UGC numbers were locked in at the time of the closing. Yes right.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay. Thanks so much, I appreciate the color.

A - Francois Morin {BIO 17410715 <GO>}

Thank you Elyse.

Operator

Thank you. Our next question comes from Mike Zaremski from Credit Suisse. Your line is open.

Q - Mike Zaremski {BIO 20606248 <GO>}

Hey, good morning. First question is on a mortgage insurance. I believe in Marc in the prepared remarks, you mentioned even as pricing has become more competitive we use that term. Is pricing currently becoming more competitive, I know that a lot of it's within these dynamic pricing models. So it's not as transparent and maybe you could comment on is that maybe why your market share, I know you don't focus on market share but maybe that's why your market share seems to like you've fallen quarter-over-quarter?

A - Marc Grandisson {BIO 4369887 <GO>}

Yeah. I think that, yes, I think it's true that there's well it's hard to see if it's a broad competition but certainly, there's a lot of dislocation occurring in the pricing, in the marketplace as a result of all these new risk-based pricing. It's very hard to see what it means and to even evaluate whether it's down or up or sideways. So we'll reserve ourselves some more time to evaluate and come to terms to what it means in this quarter. But certainly we haven't changed our pricing. We held the line and stayed the course on our risk-based pricing and at the end we just harvest what we put out there and what's stuck to the marketplace and but it's gonna take a while right markets are going through establishing their systems, educating the loan originators how it's used and fixing some of the bugs. So it's going to take several quarters for us to really see if there is truly that much more price competition. But I think the price competition that I mentioned in my remarks has been over the several last quarters. I was not specifically talking about this quarter.

Q - Mike Zaremski {BIO 20606248 <GO>}

Okay. That's helpful. And lastly, moving to kind of leverage levels on excess capital. If you could remind us, leverage is down to 21%-ish historically for UGC It was in the teens. Can you remind us is there a level that you've kind of soft promised the rating agencies and then also kind of curious whether holding dry powder is more or less important today versus in the past?

A - Francois Morin {BIO 17410715 <GO>}

Yes. Part one to your question, yes, 20% was roughly the number that we were the leverage level, the leverage level that we were targeting at the time of the acquisition and we are there today. So I think we're we accomplished what we set out to do and that's good news. And yes, part B, to your question absolutely dry powder is something that we always have been firm believers in. Whether it's deploying the capital in a potential other opportunities, whether they're acquisitions or if this rate environment picks up steam and gives us the opportunity to put more of capital at work in the business in any of our three segments, we want to have that ability to do so. So the answer to your question is yes. Having the flexibility is something that we've always believed in and thankfully I think we're there right now.

Q - Mike Zaremski {BIO 20606248 <GO>}

Thank you.

A - Marc Grandisson {BIO 4369887 <GO>}

Okay Mike.

Operator

Thank you. Our next question comes from Yaron Kinar from Goldman Sachs. Your line is open.

Q - Yaron Kinar {BIO 17146197 <GO>}

Hi, good morning, I want to circle back on the reinsurance part of your development, so even exclude the Jebi adverse evolvement I think net you see a bit of a decrease year-over-year. Can you maybe talk about the moving pieces there?

A - Francois Morin {BIO 17410715 <GO>}

Yeah. A couple of things that I'd say more minor I mean there has been some timing of some claims that came through that yes impacted favorable or the level of favorable developments in our reinsurance segment reserves. No question that we didn't -- we've had a healthy level of reserve releases over the years that were not we never planned for it. We always observe the data and we always react to the data. It turns out this quarter, the level of favorable wasn't as high as it has been in prior quarters.

Does it revert back to a higher level next quarter? We don't know we'll find out in three months. But no question that Jebi was a big part of it. There's a couple of other small moving parts that are just I think a bit more noise and somewhat (inaudible) in terms of the timing of the events that affected the aggregate level of PYD on the reinsurance segment.

A - Marc Grandisson {BIO 4369887 <GO>}

And I think our lost cost trend the discussion Yaron is certainly key into our being prudent and careful and the way we sort preserves, because things could be shifting and so that is already part of the part of informing our decisions currently, is not recent but it's certainly part of that as well.

Q - Yaron Kinar {BIO 17146197 <GO>}

Understood. I guess what I'm trying to get had those is the over year change, again excluding Jebi coming more from short tail lines more for longer tail lines?

A - Francois Morin {BIO 17410715 <GO>}

It's a mixed bag. It's a bit of both.

Q - Yaron Kinar {BIO 17146197 <GO>}

Okay, and then with regards to the U.K. block that you acquired. Should we expect it to be fully earned in within roughly 12 months period until January of 2020.

A - Francois Morin {BIO 17410715 <GO>}

Yeah. Pretty much right. So the premium it's a ramp up. So it's effectively a start-up. And we it won't be 50% earned by in 2019 but you're right Q1 into next year like to think that the run rate of earned premium is going to be a pretty steady. And there's nothing specific nothing special about their annual policies and that should the accounting should follow pretty easily from there.

Q - Yaron Kinar {BIO 17146197 <GO>}

Great, thanks.

A - Marc Grandisson {BIO 4369887 <GO>}

Thanks, Yaron.

Operator

Thank you and our next question comes from Meyer Shields from KBW your line is open.

Q - Meyer Shields {BIO 4281064 <GO>}

Thanks, I also wanted to ask about the U.K. acquisition. Once you get past the steady run rate for earned premiums. Is there any difference in its loss ratio, expense ratio breakdown and the legacy Arch Insurance segment?

A - Marc Grandisson {BIO 4369887 <GO>}

Well it should. I mean there's a lot of moving parts in the expense ratio. What we're trying to improve on that point, in the U.K. particular and you guys all know about the realities of the London market and that's generally an expensive place to do business in, so that was always one of our objectives here is try to reduce our expense ratio specifically from U.K. side and this acquisition helps us achieve that given it's a more it's a better business model for us and more efficient on that sense. But the counter to that I will say is we're very there's other opportunities, other investments that we're making within our Insurance segment that may offset some of that.

So I we don't have complete visibility on everything we're going to do in 2019. But if you're looking for some view on what the expense ratio may look like for the insurance segment for the remainder of the year, I would say, no question that Q1 was elevated because again the lack of our premium on the UK book and the timing of the share based expenses or competition expenses, by the end of the year we'd like to think that we could bring it down between the 100 basis points and 200 basis points from where it was in Q1, but my overall the business that we've acquired is retail business, as you know, it's not cheap necessarily, it is still there's a lot of commissions as I have to go through, But the problem which means the loss ratio would hopefully be lowered and then comparative E&S portfolio.

Having said all this I think with by virtue of the critical math that Francois just talked about, I think that it should improve the overall expense ratio. But I wouldn't expect it to go to be a significant improvement.

Q - Meyer Shields {BIO 4281064 <GO>}

Okay. No, that's great. Very helpful appreciate it. Looking at mortgage I think Marc you talked earlier about the benefits of the current economy I don't know how to ask this without being too politically charged. But do you see that as being vulnerable to next year's presidential election?

A - Marc Grandisson {BIO 4369887 <GO>}

Well, politics are part and parcels of what we have to deal with all the time. Now we're on the receiving on what's happening out there. The one thing I'll tell you about the politics we've been worrying about this we've been we've had we've asked that question for a long time. But the consistent answer on any kind of any administration that was in place and anybody that runs the FHA, there's clearly a recognition that private market has a place in delivering the product to the homeowners and providing insurance and protection.

So we don't see any major change there, we also don't see any change to the GST, mandate and the way that MI is one of the collateral that's used to bring the LTV down. So none of those core essence things that are really essential for -- to make sure that the market exists has been under siege or will be under siege. I mean there might be some changes to the delivery of the product and we certainly have been participating in some of those new innovations and we will continue to do so for the future, but, the way we think about politics and as it regards to MI is. We are agnostic as to what happens. We will react and are able and willing to help in any way that we can to deliver the product to the homeowners and to the banking system.

Q - Meyer Shields {BIO 4281064 <GO>}

Okay. No understood. Thank you so much.

A - Marc Grandisson {BIO 4369887 <GO>}

Thank you.

Operator

Thank you. And I am showing no further questions from our phone lines. I now like to turn the conference back over to Mr.Marc Grandisson, for any closing remarks.

A - Marc Grandisson {BIO 4369887 <GO>}

So, from Francois and I have a good day and we'll talk to you in the next quarter. Thank you much.

Operator

Ladies and gentlemen, thank you for participating in today's conference, this does conclude the program. You may all disconnect. Everyone have a wonderful day.