S1 2010 Earnings Call

Company Participants

- Andrew Horton, CEO
- Martin Bride, Group Finance Director
- Neil Maidment, Chairman of the Group Underwriting Committee

Other Participants

- Ben Cohen, Analyst
- Chris Hitchings, Analyst
- Eamonn Flanagan, Analyst
- Joanna Parsons, Analyst
- Nick Johnson, Analyst
- Will Hardcastle, Analyst

Presentation

Andrew Horton {BIO 5697110 <GO>}

So welcome to everybody. The crowd as I say, each time seems to get larger and larger. I assume that everybody in the crowd is actually interested in insurance, rather than just people who happen to be passing by and seeing the crowd in our reception area downstairs. It's great that Beazley kicks off the reporting season for our results for the year ended December 31, 2010.

Let's dive straight in. Our disclaimer's got slightly longer based on current disclaimers, in small enough type for you to read at your leisure later.

And if we move on to the contents of what's actually going to happen, I'm going to give you an overview of what's been going on in 2010. Then I'm going to hand over to Martin, our Finance Director, who's going to go through financials, so the performance, the investments, reserves, capital and Solvency II. Then Neil, who looks after our underwriting, is going to do an underwriting review. I'm going to come back with a crystal ball at the end of it all, and then we go to Q&A.

Some of the slides that we historically went through in the presentation we put into the appendix; happy to pick up questions in the Q&A on some of those slides at the end.

So if we look at 2010, what did we actually focus on? Focus on profitability, focus on the people we have, and focus on delivering a great service. Highly competitive environment,

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in our view becoming more competitive, and the economy for the media improving dramatically but from an insurance buying point of view, not improving as much.

And what did that actually lead to? It led to these numbers; profit before tax just over $250 million. We have for the last time, we hope, a foreign exchange impact in that, which was the conversion from sterling to dollars in the First Quarter of the year, so an underlying profit in our view of $217 million, and an underlying post tax return on equity of 19%.

Premiums flat, so down 1%, been difficult to grow in 2010; we'll look at some of the areas where we did manage to grow. Combined ratio, excellent combined ratio in our view despite the New Zealand/Chilean losses. Neil will talk about those later on, combined ratio of 88%.

Rate decreases around 2% where we had rate increases in 2009 of 3%, so rates gently edging down. And the prior year reserve releases a very healthy $144 million. But you will remember in 2009 we had some Political Risk losses and our Property business did not have as many releases as 2010. So 2010 is a more normal year, and we'll see that later on when Martin shows the slide on reserve releases.

Investment income, a conservative approach; again, Martin will go through that, only 1% return on our investments.

Then capital management, in our view all important, increased the base dividend by 7% to give 7.5p for the full year 2010, and then doing a special dividend of 2.5p, which will distribute about $20 million of our surplus capital. Martin will show you that in some detail in a second.

It's a challenge of keeping everything in balance. We think 2011 will be a year of opportunity to potentially look at acquiring people, or books of business or companies. I'm going to hand off central scenarios, we'll see later is a reduction in premiums and we try to keep enough surplus to make sure we can make the most of the opportunities while not retaining too much, which would depress our return on equity.

That leads us into a five year track record; thought we'd look at how 2010 featured against the five-year track record. And top left you can see the gross premiums written, up by about a quarter since 2006, so about 25% from 2006 to 2010, although flattening off over the last year or two. Combined ratio as flat as a pancake up until 2010, when we're down 2 points, and that is not consistent in all lines of business. Again, we'll look at that later on.

Dividends up by over 50%; the base dividend up by over 50% since 2006. Then there's two special dividends; one in 2007 and one in 2010, handing back surplus capital.

And the great thing, return on equity 100%. It just adds up perfectly, not engineered, of course, adds up perfectly to 100% return on equity over a five-year period post tax. Some

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of the volatility in the early years has the foreign exchange distortions in it and, as I mentioned earlier on, we hope we don't have foreign exchange distortions going forwards into 2011.

What did we actually focus on during the year? I mentioned the capital, buybacks; we bought back about 3% of our shares during the year, and then a special dividend at the end of the year. People's really important to us, so Ken Sroka, who is a senior guy -- he's American, who's a senior guy at Zurich, has joined our Board. His expertise is in the Specialty Lines business within the US, so he will complement the Board well.

And Rolf Tolle, who is well known in the UK, who was the Franchise Performance Director at Lloyds for six or seven years, also joined the Board.

And Dan Jones who was on our Board this time last year, stepped down as a Non-Executive Director to head up our Broker Relations function, so putting more focus as a key initiative within Beazley on Broker Relations. The brokers want to deal with fewer carriers going forwards and is important in our lines of business that we partner well with them. And Dan used to run Marsh Europe and was a senior guy at Marsh. He's ideally suited to ensure we are organized to achieve that.

One of my favorite slides from last year, so this is for those people who come every year, was the trees and saplings. I'm not sure many people understood it, but these were the saplings on that slide, so these were the things we planted as things to grow in 2010. John McNally on the reps and warranties, started to gain in traction. We like that line of business, because it has the opportunity of a market that can grow.

US admitted Accident and Health, based out of our Minneapolis office under Paul Gulstrand, will start writing business this year. Everything has been put in place over the past 12 months.

Marine professional liability, a small team of three people that joined us last year, again, growing their business line. And Environmental risk under John Beauchamp in Philadelphia, starting to write business in 2010.

And other growth areas which we saw in 2010, we always wanted to growth our Reinsurance business, both on our own balance sheet and through the sidecar, and we've increased the premiums in our Reinsurance business by over 20% through the combination of that.

Data breach insurance, again, a market that can grow and grow, and some very high profile media comment about breaches within insurance companies from a technology point of view. We have a unique product out there, which is doing incredibly well within the US. We hope at some point it will also take off within Europe.

Then the Life, Accident and Health business that we acquired in 2008, which was mainly a UK business but had a small Australian and US part to it, has grown their premiums by

15%. So that acquisition is growing very, very well.

On that note, I will hand off -- hand over to Martin to go through the financials in a bit more depth.

Martin Bride {BIO 15458196 <GO>}

So a very strong set of financial results; a little bit more detail. The gross written premium top line is flat. As Neil will come on to explain to you, there's still plenty of opportunities to write business at very attractive profitability levels, but in terms of finding new things to do at a gross level, then things have slowed down in 2010.

Nevertheless, at a net level we have managed to keep our premiums moving forward with a more efficient use of reinsurance. In particular, 2009 was the year we acquired First State; 2010 was the year we were able to rationalize reinsurance programs, and Neil might talk a little bit more about that.

The profit, obviously, has moved forward on the headline level, nearly $100 million. We've got improved underwriting accounts for $40 million of that improvement, which is the 90% becoming 88%. Then, obviously, it's FX movements and reduced divestment income that really accounts for the balance of that movement.

NTA per share, always an important measure, and we've moved that forward nearly 20p during 2010 before we take account of dividends, so really a very pleasing set of results.

So investment income, we ended the year with an annualized 1%. Interest rates are quite low at the moment. We carry a relatively defensively positioned portfolio and we're pleased with that result. We did, in the second half of the year, put a little bit more duration on the portfolio.

We are seeing interest rates starting to move up gradually in the currencies that affect us, and as that happens we'll continue to add duration and so you will see that as we go through 2011. At year -end we were at a one year duration compared to an even shorter duration than that at the start of the year.

Just to remind you about our investment strategy, the idea is to carry between 80% and 90% of the assets in a sovereign or high quality credit fixed income portfolio we refer to as the Core portfolio, and at the year-end that was 89% of everything we had, and then to have capital growth assets or alternative assets between 10% and 20%. They're currently at 11%. They had a very good performance in the second half of the year. They delivered a 4.5% yield roughly in the second half of the year, having had a less successful first half of the year. So we were very pleased with the performance of that portfolio overall in 2010.

Prior year reserve releases; a key part of the business model of Beazley is to have consistent and prudent reserving, as and when we see more clearly the development of

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each year. We then release those reserves. So 2010 business as usual from our perspective. Reserve releases at 10% of net earn premiums. All classes of business contributing and the increase of about $40 million compared to 2009 is primarily coming from the Property and Political Risk groups, which had a slightly below average 2009, so 2010 all classes of business contributing strongly.

One of the things I always like to emphasize is, well, where's that going? And our vision -- this graph shows our vision of how much is left in the tank. How do we see the strength of the reserves on the balance sheet? How much margin is in them compared to what our actuaries are saying we need to carry? The answer to that question is 7.9%; very slightly down from last year but to all intents and purposes, that graph remains in the middle of the corridor we're targeting.

For those of you who've already got to the back of the press release and the triangles, you'll see that we opened the Specialty Lines 2010 underwriting year slightly higher than we have opened previous years. And it is absolutely the intention to continue a prudent reserving philosophy as we go forward and keep that line within that corridor, barring very unforeseen events. So continued reserve releases and continuing strength on the balance sheet.

So the capital position, got a few extra lines on this chart to underline the capital action that's taken place this year in Beazley. So taking account of the dividend measures that we've announced this morning, we have -- we will have distributed to our shareholders $108 million of capital in total from Beazley this year in the form of dividends and share buybacks.

So what's permitted us to do that? Well as you can see, we have generated quite a lot of capital this year, and our surplus and available capital position was plus $240 million at the end of the year. We are working in the current environment with Solvency -- some uncertainty around Solvency II, of carrying at least 20% of funds at Lloyds as excess capital, so that's between $150 million and $160 million.

So a vision of our balance sheet at the end of the year is we've got $80 million more than we're targeting to carry. The dividend actions we've taken distribute immediately $60 million of that, and we will, subject to where the share price goes, continue to buy in shares and also, obviously, continue to seek opportunities to grow Beazley.

Our clear preference is profitable growth in our target markets and target products if we can find opportunities, but they have to tick all those boxes, including obviously the target return. So you should expect to see further share buybacks from Beazley as we go through 2011, depending upon opportunities, profitability and the share price.

So obviously no Finance Director gets to stand up, do a presentation without talking about Solvency II. Very well; we're very pleased with our positioning on Solvency II. Just try and give you some flavor around how big is that program. We expect to spend GBP4.6 million externally in the period of 2010 to 2012.

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However, primarily we are trying to execute this program with internal resources. And whilst this doesn't count everyone, there will be 4,000 man days, that's 20 man years, of time dedicated by senior technical and management individuals in Beazley on this program. So that's myself, Andrew Pryde, the Chief Risk Officer, our capital modelers, Neil Maidment etc., so a very, very significant commitment.

And that takes me straight to the third bullet point, in that we are -- if we're going to spend this money and invest this management time, we are determined to do this in a way in which we position Beazley to operate really effectively within the Solvency II regulatory environment and actually get the benefit from this investment. And we're starting to see benefits already and we're very comfortable that we will get to January 1, 2013 with a completely embedded Solvency II regulatory environment within this Company, ready to take on the market.

One further aspect of Solvency II, obviously, is that we're on the lookout for opportunities. There may be companies who need more capital and can't readily access it, or there may be people for whom their Solvency II program doesn't necessarily unfold exactly as they would like. And so we are on the lookout to see whether there are things that will come available to us, in terms of business growth opportunities, as we go through the next 24 months.

Neil?

Neil Maidment {BIO 5232207 <GO>}

Well thank you Martin and good morning ladies and gentlemen. I'm delighted to be able to report to you continued very strong underlying performance for Beazley in the year ended December 31, 2010.

In the next part of the presentation I'm just going to pick out some of the highlights of that performance, look at the market with a review of pricing and claims trends, and then close with a couple of comments about how we've been able to achieve that consistent underwriting result.

So we've covered some of this; the top line, as we've already said, is close to flat at $1.74 billion, but we did achieve some efficiency in our reinsurance programs in 2010, so net premium is actually up 5% at $1.4 billion.

Although the Group top line was flat, a number of our businesses did achieve significant forward momentum, in particular the Reinsurance business, which we grew this year by 23%, mainly due to the additional business written on behalf Syndicate 6107, the special purpose Syndicate we created.

Life, Accident and Health, which we acquired when we acquired Momentum Underwriting in 2008, also continued to progress well and we grew that 15%. They wrote $78 million in 2010.

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Obviously, the highlight of our performance this year though was the excellent underwriting result of 88% combined ratio, which is the best combined ratio we've achieved in the last five years. And this was achieved, not withstanding the competitive market conditions that we're operating in, as well as the significant catastrophes that we've seen during the year. And I think it's a credit to our diversified portfolio, our underwriting strategy, as well as our active cycle management, of which I'll say a few words a little later.

Underpinning that combined ratio performance, our claims ratio improved from 55% to 52%. Obviously, the largest claims events of the year were the two earthquakes that we saw; firstly, in Chile and then in New Zealand. The Chilean earthquake loss for us remains within the estimate that we have previously announced, of between $55 million and $75 million.

Regarding the New Zealand earthquake, we originally estimated a loss for us of between $15 million and $30 million based on a market loss estimate of between $2 billion and $4 billion. More recently we've revised our estimate just beyond the top end of our range at $35 million, because of the increase in the market loss estimate, to between $3 billion and $5 billion.

Now while we're on the subject of catastrophes, obviously recently we've seen the very severe flooding in Australia, and even last week we had Cyclone Yasi, a category 4 storm, make landfall on the North Queensland coast between Townsville and Cairns. It's very early, I think, to put an accurate assessments on these events. But very preliminary indications are that the impact to Beazley will not be not that significant and will be contained within the reserves established for the Property insurance and Reinsurance accounts in 2011.

Turning now to market conditions, let's start with a look at the pricing trend and this is the chart you'll be familiar with from prior presentations. It shows the cumulative risk adjusted rate change going back to 2001 for each of our product lines. Overall, on average we experienced negative 2% rate change for the Group in 2010, and all product lines pretty much were showing the impact of the competitive markets.

What you will notice is that most lines, and in particular the Reinsurance line, are still operating above where they were at the end of the last soft market. Although we do expect these competitive market conditions to continue into 2011.

One positive note is that we saw rate increase for offshore energy following the Deepwater Horizon disaster in the Gulf of Mexico earlier in the year, and we expect that positive trend to continue this year, mainly driven by the increased commodity prices, as well as the heightened awareness of risk.

Turning to claims trend, I've already spoken about the catastrophe loss activity that we've seen, and Martin has covered off reserve development and reserve strength. So to round out the picture, this chart shows the incurred claims development on our Specialty Lines account by underwriting year. The green dotted line at the top shows the ultimate loss ratio which we hold in our reserves, and the bars underneath show the development of our actual incurred claims.

What you can see relatively clearly, I think, from this chart, is that the years 2003 to 2006 compare very favorably with the back end of the last soft market between 1997 and 2000. So in those 1997 to 2000 years, the loss ratio had developed to 114% by the sixth year of development. By contrast, in 2003, after six years of development, the loss ratio was 41%.

You can also see at the bottom the premiums written in each underwriting year, and the way in which we grew the business into the hard market, so in 2001 we were writing $82 million. By 2003, we'd grown that to over $400 million.

You will also notice, I think, that in the more recent years, 2007, '08 and '09, they appear to have developed more quickly at this early stage than the hard market years of 2003 through to 2006. But their development does compare favorably, it still compares favorably, to those difficult years, 1997 to 2000, or even 2001. I think at this stage, although I stress it remains early, they compare, if anything, to 2002.

Notwithstanding changes in the claim trends, and the continued competitive market environment in which we find ourselves, Beazley's underwriting strategy has consistently delivered over the last few years strong performance, and it has achieved that again in 2010.

The foundation of our strategy, of the strategy, is diversification, and this chart, I think, shows the benefits of that diversification. So across the middle, we have the Group result, shown by that red line, at 90% or better for the last five years. Then we can see around that the blue, or perhaps gray lines, showing the individual product performance by team, and the volatility of those individual product lines.

So for example, in 2009, the spike at the top at 112% combined ratio, was the Political and Contingency group, that experienced that loss activity following the credit crisis, but it was balanced by that line at the bottom, our Reinsurance division, which achieved a 62% combined ratio.

By contrast, in 2010, Political Contingency group was actually the best performer, at 66% combined ratio, and that balanced -- I think the high end was probably our Property insurance account, at 97% combined ratio. So balancing the outcomes of these diversified businesses is what gives the Group underwriting result its consistency.

The other element of our underwriting strategy that I just want to highlight is cycle management. Simply put, we look to maximize opportunities for growth, when they -- profitable growth, obviously, when they present themselves, whilst at the same time minimizing the volatility, which can be caused by weaknesses in pricing, or terms and conditions, or changes in the claim trend.

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You'll remember, I think, that we grew our catastrophe businesses in 2009. So we grew Reinsurance, large-risk Property, and offshore energy, as well as buying First State, when we had the opportunity presented by the market, whilst at the same time, we reduced the recession-prone lines of business within our Specialty Lines account.

In 2010, we continued to grow Reinsurance, as well as Life, Accident and Health, as I've already mentioned, because that was where we saw the best margins available, whilst pulling back in directors and officers, where that market became very competitive.

And in 2011, we'll continue with this activity, pulling back in lines of business such as lawyers, and architects and engineers professional indemnity, where the market has become very competitive, whilst still increasing in areas where demand remains strong, such as technology and energy.

It's being able to adjust and optimize our well-diversified portfolio of products that helps us manage the cycle and achieve that consistent underwriting performance for which we would like to be known.

And with that, I will hand back to Andrew for the outlook.

Andrew Horton {BIO 5697110 <GO>}

Great. Thanks for that. What I've got is an outlook of, what are the things we're actually going to be thinking about in 2011, and then how is the business going to respond to it?

So we -- our view, our central view is that the industry still has challenging conditions. Generally, the demand for insurance is on the low side. There's still uncertainty in the global economy, although the view, as I said earlier on, is that it's actually picking up. We're not necessarily feeling that yet.

While that's going on, the market is incredibly competitive, so people are entering lines of business, and our view is that rates will continue their gentle decline into 2011. There's plenty of capital in the industry, and people are entering various lines of business based on, probably, our performance in 2003, '04, '05 and '06.

Inflation is always a question we get, and it's a very difficult one to answer, so I thought I'd have a go at answering it now before I get the Q&A at the end and trying to answering it then. We do think about inflation a lot.

We look at our shorter tail lines of business; Property, Marine, and so on. We may be impacted from a claims point of view from an RPI-type inflation, but they're annual policies, and the premiums should catch up. There should be a natural hedge against inflation to some extent, that interest rates should rise if inflation goes up, and we have our gearing of 4 to 1 assets to equity and, therefore, our profit should come up on that.

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On our Liability business, or Professional Indemnity business, where the concerns seem to come up regularly, generally, claims inflation on that line of business is not linked to RPI. It's linked to tort reform, what's going on with awards within the US, with mainly a US book, and so on. And historically, we've tended to build in claims inflation within our pricing, which over the past few years has proven to be conservative, and we aim to continue to do that.

My final comment, and my colleagues will have heard me say this a lot; I think insurance generally over the past 35 years is probably one of the most ill-disciplined industries on the planet, and yet this is a term that we use regularly, and we couldn't think of a word any better than that, so we thought we'd use it four times in the last four bullet points.

So the aim is to focus, just as Neil has outlined a minute ago, on our underwriting discipline. So that is all about ensuring that we grow the lines of business where there is opportunity in 2011, and manage closely those lines where opportunities are less in 2011, to continue to deliver an underwriting profit.

Expense discipline, I think, in insurance and in Beazley is something we focus on year-in/year-out, so we keep a close eye on our expenses. And we've been investing quite heavily in various platforms over the past few years, and we hope to bear fruit from that over the next few years.

Then capital management discipline, getting the right amount of capital; having enough capital for the opportunities, but not retaining too much capital in these uncertain times.

We believe, based on our results over the past few years, and the previous 20 years prior to those five years, 25 years, that the formula works well, and it is a formula we will continue to apply in 2011 and beyond.

We're now open to questions.

Questions And Answers

A - Andrew Horton {BIO 5697110 <GO>}

Want to go front, Nick?

Q - Nick Johnson {BIO 1774629 <GO>}

Morning all. Nick Johnson from Numis Securities; a couple of questions. Firstly on reinsurance purchase, you mentioned that there were some savings in 2010, partly First State, I think you said. Could you just tell us whether that reflects any change in your US -- or retained US risk appetite to catastrophes? Is there any change in that? And remind us what your risk appetite is in the US following the purchase of First State? And are there any further savings to come through overall on reinsurance spend in 2011?

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Then the second question is really on Political Risk and Contingency, whether or not -- well, can you just give us your thoughts around Egypt, whether that's an event we should be looking at? Thank you.

A - Neil Maidment {BIO 5232207 <GO>}

Well picking out the Egypt, perhaps first, it's obviously a developing situation. We have some exposures within the Political Risk and Contingency account. Within the Political Risk account itself, we have expropriation insurance for assets in Egypt. We don't, as things stand at the moment, expect those to be significantly exposed, although obviously it is developing, the situation, they are well spread throughout the country.

And within the terrorism and political violence part of our account, we also have exposures throughout the country. The -- perhaps the most, what would appear at this stage to be the most exposed part of that would be the strikes, riots and civil commotion coverage, particularly for exposures within Cairo, or the other major cities. Those exposures are relatively modest, and we don't believe they have been materially impaired so far, but it's obviously something that we keep in sight.

Regarding the Reinsurance, the main efficiency was consolidating the program that First State had previously purchased when it was a separate entity with our own, existing property reinsurance program, so it was just an efficiency of putting the two prior US catastrophe programs together.

The risk appetite for the Group as a whole has remained consistent, and you'd be able to see that from the detail in the Report and Accounts. What you'll also notice is the effect of us growing our catastrophe exposed businesses, as I mentioned, during 2009 and into 2010. So on individual loss events, you'll see that our Lloyd's realistic disaster scenarios have increased year-on-year in line with that planned growth.

In 2011, reinsurance market conditions are down at the January 1 renewals, varying by territory and by nature of exposure between, perhaps, minus 5% and minus 7.5% or 10%, and we would expect, as we go through the remainder of the year in our own purchasing, to get the advantage of those market conditions.

A - Andrew Horton {BIO 5697110 <GO>}

Yes?

Q - Ben Cohen {BIO 1541726 <GO>}

Hi, Ben Cohen at Collins Stewart; two things, please. Firstly, on the issue of underwriting discipline, if you look at your account in general, and the loss picks that you had for 2010, and maybe more specifically for the Specialty business, if you add on the expense ratio, whatever it was, 36%, that would look like a combined ratio 109% or so on the Specialty, somewhere above 100% for the business as a whole, in terms of what you're treating[ph] for 2010.

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I was just wondering what you are having to assume in terms of improvements on those initial loss picks, that you're comfortable committing capital at those sorts of ratios, because presumably particularly with -- particularly where interest rates are, there wouldn't be a lot of margin in that, or much RoE in that, where it stands.

And the second question was just on the funds at Lloyd's, the increase -- the small increase that you have in your -- I think in the capital model there. I was surprised that that hadn't risen more, given that interest rates are very low, given that maybe there's less profit in the business looking into 2011, and I was just wondering if you could comment on why that had moved the way that it had?

A - Andrew Horton {BIO 5697110 <GO>}

Let me pick up on the first element, and when I flounder Martin will save me, and then Martin can perhaps make a comment on the funds at Lloyd's.

To start with, the specialized loss pick, if we look at it on an 87% -- the 87% loss ratio you were talking about is on a net of brokerage basis, so the equivalent number on a GAAP basis is in the low 70%s, so once you add on the expense ratio, you should have a combined ratio of just over 100%, in the low 100s for Specialty Lines. You work it through with Martin later to prove what I'm saying is correct.

But Specialty Lines, historically, we were opening very close to 100%, having this conservative reserving, and then we've seen, obviously, 2004 -- '03, '04, '05 and '06 all come down. So we're slightly opening just over 100% in the Specialty Lines' position, with the hope that we're starting with a similar buffer, because we've seen rates come off for two or three years.

We didn't realize 2003 was going to be as good as it was, but now we think it's the time to actually open. We want to keep that buffer at the right level, which Martin was talking about, the 7.9%. We feel we have to pick up a couple of points on the Specialty Lines' side, but it's just over 100%.

You're right, if interest rates stay low at 1%, over the cycle of paying claims five years down the track, and the 100% is correct, it will not have a great return on equity. So our hope is that we're still slightly conservative in the reserving, and the market has to move. And interest rates have to rise at some point. But we're not seeing that at this point in time.

With Specialty Lines business you can't dip in and dip out. It takes you a long time to build up the lines of business we have and, therefore, we have to stay with our core clients, even though the margin may not be as high as the average over the cycle. So that's where we are on the Specialty Lines.

Do you want to pick up the funds at Lloyd's?

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A - Martin Bride {BIO 15458196 <GO>}

Yes, sure. So funds at Lloyd's, I mean, big picture, Ben, our business plan is to write broadly the same amount of business at broadly the same loss ratio. And how do we achieve that? Obviously, by a lot of active cycle management, as Neil's described. So coming in and out of classes of business, sic. we've got broadly the same capital requirement; are one or two things moving.

The way those stress models work is, you are allowed to assume, if you have lower yields, that to some extent the insurance pricing cycle will be less severe, and you can evidence that from the history. In periods where interest rates were very high, combined ratios would go to eye-wateringly high levels; where interest rates are lower, they go less high.

So the way that SL[ph] calculations work, you can take some credit for that, and so I think the combination of actively managing the portfolio to keep the planned loss ratio broadly level and those other effects is why that number is, broadly, similar to the previous year.

A - Andrew Horton {BIO 5697110 <GO>}

Joanna?

Q - Joanna Parsons {BIO 1558226 <GO>}

Joanna Parsons, RBS; three questions, please. You said that you'd seen an average rate reduction of 2% on renewals, and I know you've got roughly about an 80% retention rate. Could you give us a feel for what you're seeing on that 20% of the book?

You also mentioned that you've seen a frequency in liability claims fall. Are you seeing any movements in the quantum, today or in the future? Do you think, although you may be getting fewer claims coming through, that they may be larger in size?

And finally, on acquisitions, inevitable question, could you give us a little bit more color on where you would like to, ideally, add to your business? And of course, if you've got any names, we'd be fascinated to hear[ph].

And prices, yes.

A - Neil Maidment {BIO 5232207 <GO>}

Okay, you get that one, yes[ph].

A - Andrew Horton {BIO 5697110 <GO>}

Let me do the third one first, and then I'll hand over to Neil on the first two.

So the acquisitions. I think we've been relatively clear with our strategy for growth over the years, that organic growth in our view is always a preferred option, and most of what Beazley has achieved, over 25 years, is organic.

We've made two to three acquisitions over the past few years, each one getting slightly larger than the previous one, the largest being First State in 2009, and the First State and MUM acquisitions are the ideal acquisitions for us.

So these tend to be, in the case of First State, a private company, in a line of business we wanted to get into, with a great underwriting track record, where the management wants to stay with the company, and wants to join Beazley. And as we've seen, from the growth in Life, Accident and Health business, it's working well two years in.

First State somewhat different, stress in the system, the Hartford wanted to sell part of their non-core portfolio. But again, a great underwriting track record in a line of business we'd been in for a long period of time.

So our aim is to find things like that, so lines of business we've been in for a long period of time, underwriting track record, people who actually want to stay with the business. Geographic focus, US, Europe, and maybe, as we now have small offices in Hong Kong, Singapore, and Australia in the Life, Accident and Health side, in those three regions. So very much in the areas we're currently in, and in areas we want to grow.

A - Neil Maidment {BIO 5232207 <GO>}

Picking up the other two points, then, Jo, on pricing. I think the point I would make is that we have a pricing strategy for all of our business, not simply for the business that we renew.

So we should apply a consistent benchmark pricing to new business that we write that forms the 20% that we're adding, as well as the 20% that we're letting go. All of that business is designed to achieve the business planned loss ratio for the relevant product line. And obviously, around that 2% we have quite a wide dispersion. Reinsurance, as I mentioned, at probably 5% to 10% negative in 2011. Specialty Lines, although it varies by individual product, is closer to negative 1% or negative 2%.

On the question of frequency, we have seen frequency fall back in those recession-prone lines that we talked about at this presentation last year. And we've included, I think, the recession-prone line frequency chart in the back of this presentation so you can have a look at that later. And we have seen those lines benefit, partly from the recession moving behind us to a degree, and secondarily from the underwriting activity that we undertook in those lines of business to manage those signals when we saw them.

I don't believe in Specialty Lines, we've seen an increase in the severity trend, although that's something that we obviously keep a closer eye on as well.

A - Andrew Horton {BIO 5697110 <GO>}

Chris?

Q - Chris Hitchings {BIO 2034501 <GO>}

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Chris Hitchings, KBW, thanks; a couple of things. Just for the record, one of your quoted competitors said that they had received a number of approaches. Would you be on that list?

A - Andrew Horton {BIO 5697110 <GO>}

No.

Q - Chris Hitchings {BIO 2034501 <GO>}

No. Thank you. Just more specifically, you talk about how there's a 7.9% full reserve cushion, I'm looking at how most of the reserve releases have come out of the old years. If you were trying to allocate that 7.9% for the remaining reserves of the old years, is it still 7.9% for that?

And more particularly, how much are you building in as a potential -- how much of that 7.9% is related to the reserves you set up for '09 and 2010 business?

A - Martin Bride {BIO 15458196 <GO>}

That's a great question. That's a detail that we don't actually disclose.

Q - Chris Hitchings {BIO 2034501 <GO>}

I know. That's why I'm asking the question.

A - Martin Bride {BIO 15458196 <GO>}

We're not going to start disclosing it to that level, Chris. So the logic of our peer review is -- the process of the peer review is going for consistency by line of business and underwriting year. So it's quite difficult to be inconsistent.

So we look at each year during a quarterly review. The Specialty Lines business is chaired by Nick Furlonge and all the other businesses are chaired by Neil and we're ensuring consistency of reserving actuarial versus where we are. Then it throws out the number.

So we do have all the detail broken up by re-underwriting year in every single line of business. It's not something we're going to disclose. All I can do is assure you the aim is consistency and what we're showing you is the output of that detailed review and the consistency in the top line position of 7.9% versus 8.3%.

So we're not trying to skimp the later years and hold reserves for the earlier years. And that's one of the reasons why in Specialty Lines we increased the reserving in 2010. If we'd wanted to make our profits look better we could have kept it at the same level and kept our fingers crossed and hoped over the next five years it was going to be fine. We don't think that's consistent, because that reserve measure would start falling.

Q - Chris Hitchings {BIO 2034501 <GO>}

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But presumably simply because the quantum of your -- your 7.9% is of your reserve base and presumably the quantum of reserves in your books for the old years, '03/'04, is so much smaller than what's in your books at the moment, a large slug of that 7.9% must be on the recent years rather than the old years.

A - Martin Bride {BIO 15458196 <GO>}

Yes, (inaudible), it does and a fair chunk is in Specialty Lines as opposed to the other lines, because we hold the reserves in Specialty Lines for longer.

Q - Chris Hitchings {BIO 2034501 <GO>}

And another detailed thing on reserves, there seems to be a deterioration in your Property account on the '07 year. Is there something specific there?

A - Andrew Horton {BIO 5697110 <GO>}

Did we mention it? (multiple speakers)

Q - Chris Hitchings {BIO 2034501 <GO>}

It would seem odd to see a -- if I look at the gross triangles, and I'm afraid being a tedious sod I have, you'll find that there's a slight increase in gross ratio for the Group and it's entirely in Property and breadth for '07.

A - Martin Bride {BIO 15458196 <GO>}

It's in -- there's a note, Chris, under the Property section; there's an engineering loss.

Q - Chris Hitchings {BIO 2034501 <GO>}

Engineering, okay. Finally, you did refer to how this Australian loss is within your cat budget for -- you said for 2011. Just in general, what -- how much of your Group earned premiums would you suggest is a cat budget for Beazley?

A - Neil Maidment {BIO 5232207 <GO>}

We don't tend to disclose it. It's going to vary to some extent, isn't it, obviously about what we're writing, so it's not consistent year on year, and where we think the rating environment is.

All we've done is flag that the Brisbane loss will be absorbed within it, based on our knowledge at this point in time, based on our estimate of what it could end up being. But that's also based on very little information.

So we don't have a number that we're going to quote of how much is our cat budget each year and, therefore, what is attritional loss. It's a level of disclosure we're not going down to.

Q - Chris Hitchings {BIO 2034501 <GO>}

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Do you accept that for a lot of people trying to analyze this sector, it's useful to know what -- because one should look at cats and say, okay, fine, that's used 30% of the Group's cat budget; I don't need to change my forecast for that. That's used 120%; I do need to change my forecast.

A - Andrew Horton {BIO 5697110 <GO>}

I think it's --

A - Neil Maidment {BIO 5232207 <GO>}

We're going to the attritional; then going to the balance of[ph] the attritional; how is the attritional accurate? So it just puts the pressure on to the attritional level, doesn't it? So that takes a presumption the attritional's right and the cat budget is being used to and I'm not sure that is correct. If we knew exactly where our attritionals were going to be every year it would be fantastic, because we'd know exactly where our reserve's going to end up and we don't. So therefore, we have to come up with one which is a combination of the two and then we look at the two elements.

A - Andrew Horton {BIO 5697110 <GO>}

You can get some historical perspective by going to the triangles in cat-free years.

A - Neil Maidment {BIO 5232207 <GO>}

That's true.

Q - Chris Hitchings {BIO 2034501 <GO>}

I do that. I'm just wondering -- I was trying to check the answer.

Q - Will Hardcastle {BIO 16346311 <GO>}

Morning guys, Will Hardcastle from Macquarie. I think it's actually going back to the very first question on the Reinsurance purchase and you touched on the risk appetite and the RDS. I think you said the RDS has slightly increased year on year. Can you give us -- and I apologize if it's in the report, can you give us an indication of what sort of percentage they are?

A - Neil Maidment {BIO 5232207 <GO>}

Well Martin's leafing through the report so he can find it. The Lloyd's RDSs are cut somewhat earlier in the year so they are reflecting the growth that we'd previously discussed at this meeting last year and I think they've grown in the region of 20% to 25%, which was in line with the growth of our catastrophe-exposed businesses during 2009. So that's what's reflected in the Lloyd's RDSs.

Our Group catastrophe budget has remained flat since we grew it in 2009. It remained the same in 2010 and it is the same in 2011.

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A - Andrew Horton {BIO 5697110 <GO>}

The only problem with these numbers is they're cut too early in the year, isn't it? So if you do make it to page 121 of the Report and Accounts you'll find how the exposure's grown.

Eamonn?

Q - Eamonn Flanagan {BIO 14018002 <GO>}

It's Eamonn Flanagan at Shore Capital. Andrew, just -- or it's actually Martin made a comment he was pleased with the 1% investment turn. I'm sure that's right[ph], I'll check at 2.30 that's what you said. I'm surprised by that. I suspect he might be somewhat embarrassed over the next couple of weeks based on[ph] the results from the other quoted companies. I'm just interested in what plans you might have to get the guys to perform a little bit better.

Then secondly, it appears that the fees are round about 25 basis points in the funds. There doesn't appear to be any performance link. So the fees issue around about 25% of the total income. Is that not a bit too much for the pretty poor -- the Group outcome for the year?

A - Martin Bride {BIO 15458196 <GO>}

Well thanks, Eamonn; a very balanced question there. Investment performance clearly is -- on the fixed income portfolio that's almost pure sovereign, the investment yield is, frankly, a pure function of duration. So we took a positioning decision to have a short duration. That meant we had very low volatility and risk during the year and the yield was commensurate with that.

Obviously, there were other companies; they've had a longer duration. They carried credit. They have a different investment yield. So I don't really view that from a perspective of I'm pleased or I'm displeased with my Investment Manager. The yield on fixed income is a function of duration.

As far as the capital growth assets are concerned, they delivered more than 400 basis points above risk-free rates. Risk assets delivering those types of return, that's very good if that is sustained. So we're pleased with that.

In terms of fees, Falcon do have performance-related fees, but we've made sure that those performance-related fees do not have a cliff in them, so that they build up gradually. They need to get above their long-term target benchmarks for those fees to operate fully. But they -- as I say, it's a gradual build up.

In terms of the absolute level of fees, around about 25 basis points to have assets managed with a very significant amount of expertise in the different classes we're in, we would consider that to be relatively normal. The way our agreement with Falcon is structured is that it can get, or it will get rebased to market rates as we go forward. So we have thought about that in the way we've set the thing up with Falcon.

A - Andrew Horton {BIO 5697110 <GO>}

Anything else? Excellent. Well thank you for joining us this morning.

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