Lancashire Holdings Limited Proposed Acquisition of Cathedral Capital Limited Conference Call

Company Participants

- Alex Maloney, Group Chief Underwriting Officer
- Charlie Mathias, Chief Risk Officer
- Darren Redhead, Head of Lancashire Capital Management
- Elaine Whelan, Group CFO
- Jonny Creagh-Coen, Head of IR
- Paul Gregory, Chief Underwriting Officer, London
- Richard Brindle, CEO
- Unidentified Speaker, Unknown

Other Participants

- Andrew Broadfield, Analyst
- Andrew Ritchie, Analyst
- Angela Gu, Analyst
- Ben Cohen, Analyst
- Christopher Hitchings, Analyst
- Maciej Wasilewicz, Analyst
- Tom Dorner, Analyst
- Unidentified Participant, Analyst

Presentation

Jonny Creagh-Coen {BIO 20677871 <GO>}

Good morning, all. Thank you for coming at such short notice and I apologize for the clash with other insurance companies. But as time is of the essence (technical difficulty)

Without further ado, I've got on the call today, Richard Brindle, by phone, our CEO; Alex, our Chief Underwriting Officer; Elaine, our Chief Financial Officer; Charlie Mathias, our Chief Risk Officer; and Paul Gregory, our Chief Underwriting Officer in London.

I'm going to ask Richard to give an overview of why we've done this transaction and what goes with it and then the rest of the team will speak to their respective slides. If I could ask you to wait for the Q&A until after the presentations, that would be great.

So Richard, can I ask you to kick off please?

Richard Brindle {BIO 1983776 <GO>}

Yes, Jonny, with pleasure. Thank you very much, everybody, for coming this morning. We are the opposite of M&A junkies as I hope you will realize by now.

In the eight years that we've had Lancashire and previously in my career, I've had all sorts of opportunities coming across my desk for this and that and we set the bar pretty high in terms of interest level in acquiring other companies.

Having said that, we've always had an eye on Lloyd's. Contrary to some views, we've always had a positive view of Lloyd's. But we've never found a way to make it work for us.

We got so far as to actually have detailed discussions with them at one point a few years back. But it never quite worked. As you guys know, it is, to all intents and purposes, very, very difficult to start a new syndicate in Lloyd's now.

The incumbents are pretty negative about new entrants to the market and tend to make it de facto, pretty much impossible to get in. So the only real way into Lloyd's these days is via acquisition.

So when we looked at Cathedral, we took a second look, we took a third look and we very much liked what we saw. When we think about Lloyd's, we think about very much a two-tier market. We think about some of the big very strong players, the Hiscox, there's XL, which are very good companies and we respect them and we've always been nice about them, if you will.

Then we think there's a lot of Tail End Charlies. Most of them aren't publicly quoted and we don't need to get into names. But I think what we are critical of is the full-follow syndicates, the guys who just sit in Lloyd's writing 2% lines at the end of the slip and we question -- using this year's buzzword of relevance, we question what the relevance is of these sort of entities.

Now, Cathedral are emphatically not like that. They are small and, therefore, digestible for us. Of course, we're not big enough to go and buy Hiscox or Amlin or whatever. So they're small enough for us to digest. But they are very much masters of their own destiny.

This is an extraordinarily sticky group of people. They've been together for a very long time; they've been together 13 years at Cathedral and, in most cases, another seven or 10 years prior to that in their previous home.

When they moved to Cathedral, they basically took all the business with them. So the business itself is very sticky. The business is different from ours, albeit it shares the short-tail characteristics that we prize. We're not casualty underwriters and we try to stick to short to medium-tail business.

On the property cat side, they write small regional business, whereas we write nationwide and super-regional business. So there's really pretty much zero overlap there.

They write D&F and they write it extremely well. Obviously, a question you guys are going to have is well, why are these guys buying a company with a large D&F, when they pulled out of D&F last year? Well we need to be humble enough to recognize that we don't get everything right. I think we've written most of our classes of business very successfully throughout our eight years of existence. But D&F, we never really found the right sweet spot.

We made money, which was fine. And we did better than most. But these guys, frankly, have a superior D&F track record to us. Again, very different to what we used to do. We used to write big lines on Fortune 500's insureds, the account was quite lumpy and prone to atypical losses. Their average line of size is $3 million; they buy a lot of reinsurance, not just on D&F. But across the book. So their retentions are very low so their earnings are pretty even.

Their track record is very good in terms of not coming out of the top of their programs, even in Katrina, unlike most Lloyd's entities, they stayed within their program.

Also on the D&F side, about one-third of their book is binding authorities and these are relationships that go back decades. So again, obviously, we're wary of the incursion of third party capital into our industry. We had a very, very close look at the stickiness of the business and we're confident that it's going to be there.

In terms of the people, sometimes you see acquisitions, we've seen one recently, where a lot of the people just left. So we have concentrated very hard on the social issues.

I think it's fair to say both management teams struck up an excellent relationship from the start and the discussions, as Peter Scales references in his remarks and I do in mine in the public release today, were characterized by their cordiality and it was a thoroughly enjoyable process for all of us.

We're all London market people. I think they were wary of selling to non-London market people because they're very proud of what they've built and they want to have a new owner who respects that and who will allow them to continue to do what they do, albeit under new ownership and with some small changes to ensure that we all achieve what we need to achieve.

We've put in place a retention and incentivization package, which means that they leave some skill in the game. And then they get an upside which is partly calculated on Cathedral metrics. And partly on a Lancashire share grant.

Elaine and I are very keen that everybody in the Group is a Lancashire shareholder. So they'll be getting an RSS award next spring. We're also committed to our philosophy that everybody, from the receptionist upwards, has shares. Interestingly, they have exactly the same philosophy. So that will be implemented across the Group now. And we're excited about that.

But just broadly in the lens as to why we've done this, I think I need to explain to you certainly what's been in my head for a while now. We have been incredibly faithful to our IPO business plan for eight years now. So much so that even one of the rating agencies recently said to us. And they're not exactly known for being reckless, don't you think you guys might need to just evolve a little bit.

The danger I feared is that if we go into a prolonged soft market. And that's a scenario that's on everybody's lips these days, what do you do, as a company, to stay relevant. How do you navigate your way through those waters?

Well first of all, we're in a miles better position than pretty much all of our peers because, of course, we have a combined ratio that's still so low, that there's a lot of fat on the bone, if you like, if we have to go into some lean times.

But what I try to do is -- and indeed, we've already seen peers producing negative returns for Q2. And combined ratios, in some instances, getting very close to, or even going over, that critical three-figure mark.

But whilst I keep an eye on the performance of peers, my job is to make sure that Lancashire actually makes a decent return in its own right. So whatever the rest of the industry is doing.

I am conscious of the fact that if we had two or three more years of this sort of market, Lancashire, as a business, could start to look a little narrow.

We do write a limited number of lines of business. Indeed, we're the victims of our own diligence in some respects, in that we have exited parts of the business. Very aware, as you know, a lot of companies talk the talk. Not many actually walk the walk.

So we stopped writing D&F as we used to write it. We've stopped writing retro. And that's all well and good. And indeed, those decisions have saved us money. But you reach a point where you become arguably too narrow. And you cross that invisible line from being an exotic boutique specialty underwriter, which is probably where we've been positioned in people's minds, to being a little bit odd. And we don't want to get to that point of being viewed as odd.

My job is to look out across the waters and try and anticipate all the possible scenarios that could sit in front of us as a business. And not play catch up.

So I think it's a defensive move in a sense that it does position ourselves for that sort of a long-term, soft market. But I think it's also an offence in the sense that if there is a big event, we will be even better placed than we are now to access post-loss business through multiple platforms.

We have been very aware of the other big emerging trends in our business over the last couple of quarters. Third-party capital, as you know, we take seriously. We're not in the camp of just closing our eyes and wishing it would all go away.

Nor are we in the camp of panicking and thinking we have to trash our core business in a desperate attempt to attract and deploy third-party capital, as some people seem to be doing.

We've chosen the middle path, which is to acknowledge that this stuff is here to stay. Some of it might go away after a loss. But others might double down. We do think there are signs of a bit of a pullback.

There's already litigation on several ILWs. We think if you stick a big loss in, you're going to have a gulf of understanding between the capital providers and the purchasers, which will inevitably end up in the courts.

We also think the traditional market is showing signs of a bit of a fight back. Indeed, we've been part of that fight back ourselves on our property cat book, as we've explained to you guys. But we can't just wish this stuff away.

We've hired Darren Redhead and Mathieu Marsan, highly experienced individuals. They're running our Kinesis Capital Management division now.

So post this transaction, we see Lancashire as having gone from being a single-pillar entity, highly successful, yes. And highly disciplined. But arguably just a little bit too narrow. And that is my concern to be candid with everybody, to a three-pillared entity with Lancashire, Kinesis and Cathedral and we're excited by that.

So that's really my high-level summary.

Jonny Creagh-Coen {BIO 20677871 <GO>}

Thanks, Richard. Alex, if I can now pass over to you to talk about the proposition.

Alex Maloney {BIO 16314494 <GO>}

Yes, sure, okay. We see this transaction as adding a book of core business. We talk a lot about core business at Lancashire. By that, we mean suites [ph] that can provide adequate returns over the cycle.

So we just see it as adding a big book of core business to what we already have. There's relatively little overlap with what we have. But they do write classes of business that we understand.

So when we went through the due diligence process, everything seemed to make sense to us. It's a business we understand. As Richard said, their D&F book is very different the way wrote the D&F account. But their results are very good across the board.

So we're adding a core book of business. At the same time, we're bringing in 14 higher-quality underwriters in (technical difficulty) where all their department heads are basically partners in the business. They've been together for a long time. They've got a proven track record.

So from our point of view, I think it's fair to say when Richard and I were (technical difficulty) our first meeting, we were walking across London Bridge thinking is this the right thing to do; is it a waste of time. Then, from the first meeting when we met the guys, they very much spoke the same language as us.

So again, as Richard said, they're London-market people. They're people that I didn't know them personally. But you know their reputations. They think the same way as what we do, albeit in a Lloyd's framework, which is slightly different to what we're used to.

The deal is accretive to ROE in its current form. But we do feel we can slightly amend that. We do think -- it's definitely not a broken business. So there's not loads of surgery to do. But there's things that we can bring to the table.

We're going to add the Lancashire specialty lines. We'll have to get Lloyd's approval for that. But that shouldn't be a problem. Richard's already spoken to Tom Bolt about that.

So we'll be bringing in energy and terrorism and political risks. And all the things that we currently do at Lancashire. That will give us another platform to see business. There will be business we don't currently see in the Lloyd's environment. So we're excited about that.

We will be more active on capital management. To be fair to them, they weren't public. So capital management wasn't exactly at the top of their agenda. But we will, obviously, seek to bring in a lot of the Lancashire values into the business.

We don't see any change to our overall lives if you like. Our capital management philosophy will be the same. Everything at Lancashire has always been about increasing book value per share. That won't change. We only want to do things that make sense. And we wouldn't even be looking at this deal unless we thought we could increase our ROE over time.

We believe that Cathedral gives us more opportunity. If anything, it makes us more nimble. Again, as Richard said, we're in a reasonably difficult market. And we just need some more flexibility. A Lloyd's platform very much gives us that.

In the past, we have stuck to big-ticket items. But, quite frankly, there's only so much of that business you can write. And I think having a Lloyd's platform does allow you to look at maybe smaller books of business in the future.

So there's probably people in -- there's always people in our market, in any class of business, that can make money; and there's probably people that, over time, we can bring to the syndicate that may have like a small book of business, that may have, say, $30 million of business, that performs well. It's much easier to bolt that onto a syndicate than what it would be outside of the syndicate.

So we just think it gives us more opportunities; it makes us more nimble. As Richard said, we've got the Lancashire mother ship, we've got Kinesis and we've now got the syndicate. So we think that gives us a platform in each arena.

Jonny Creagh-Coen {BIO 20677871 <GO>}

Thanks, Alex. Charlie, if you can talk about why they're the ideal partner, that'd be great.

Charlie Mathias {BIO 16185351 <GO>}

Yes. Obviously, as CRO, my job is to try and ask awkward questions and look at the downside. So what we've tried to do here is think about how this would help us develop; what the obstacles for that development might be.

In the first instance, the kind of business they write, it's all lines that we're familiar with. These are things we know; property we know, marine we know, aviation we know. But they are writing niches within those lines that aren't the same as ours.

So to Alex's point, there isn't that overlap with what we do. But we're not going into areas that we don't know or understand.

It's all short-tail business. It's been very much -- as Richard said, this is an underwriter-led and an underwriter-focused company. So it's got that same approach to business that we have.

In terms of the -- how they would operate within Lancashire, as I think Paul is going to talk about, their line size structure's very different from Lancashire's. They write small lines on the whole. They buy a lot of reinsurance. So very much a traditional Lloyd's approach to the business.

And so we don't envisage them being part of our daily underwriting call. But we do very much see them being part of our risk and return committee, that fortnightly meeting that looks at capital and strategy.

Simply put, the size of lines that they will not individually move are RDS or PMLs. That isn't the case at Lancashire. We're writing big lines which, in themselves, can have an effect on PMS and -- PML and RDS. So it's appropriate for the Lancashire book to go through the daily call. But appropriate for Cathedral to come to our risk and return committee.

It will not affect our ability to do our capital management. Elaine's going to talk about some capital efficiencies that we think we can find there. But our approach to capital management is not going to change.

The extra distribution that Alex has mentioned, again, one of the things we like about Lloyd's is footfall. You've got several hundred brokers in there each morning and afternoon, looking to place business. And being close to those brokers and having access to them is definitely an advantage to us.

The strong rating of Lloyd's is an advantage to us, as are the worldwide business licenses. There are regions that we would like to do business in, that the bureaucracy of setting up our own access to is just too high a hurdle for us to leap on our own.

So all those things, we've looked at the issues, we're satisfied that they are issues that we can deal with.

Then, their underwriting expertise. Again, as we've said, this is an underwriter-led business. If you look at their CVs, these are guys with long experience; good, strong following from the brokers and clients. Richard has talked about that stickiness of the business. That's very important to us when we're making this first acquisition; we don't want to buy something and find the business disappears.

So Richard talked about when these guys moved to their home at Cathedral, they brought all except, I think, on the cat side, all except two of their clients came with them.

They've built this business up over a long period. Their D&F book, I saw Chris raise his eyebrows when we mentioned D&F. As the CRO, my concern about D&F was about parameter and tail risk. We were making money writing D&F. And good money. But the tail risk, in particular, was a big drag on capital. And the parameter risk that our modeling of those big excess lines might be wrong was something of a concern.

Their book, with small lines, lots of reinsurance, does not give us that parameter and tail risk. So we're much more comfortable about writing business in that way. And they do a really good job of writing that book.

I think where we are -- we like their diversification, their lines. Paul's going to talk to you about that. Management's had a lot of skin in the game there. They've had 37% ownership in it.

They have been somewhat constrained by their private equity ownership. And being private, not having access to the markets post-loss. So they've been very conservative about how they've managed capital, how they've managed reserves. We can help them open their shoulders a little bit and take that business forward.

Richard mentioned that they're very proud of their record. And they're absolutely right to be very proud of their record. But they're also very ambitious to take the business forward. We think we can help them do that, both by working to expand their own lines and, as Alex mentioned, bring some of our own business in as well.

Jonny Creagh-Coen {BIO 20677871 <GO>}

Thanks, Charlie. Business, can I hand over to you?

Paul Gregory {BIO 16314515 <GO>}

(technical difficulty) made up of (technical difficulty) business lines, the majority of which they write through Syndicate 2010. And then they write marine cargo through their wholly-owned Syndicate 3010.

About 75% of their current premium comes via the property sectors, whether that be through their reinsurance (technical difficulty). And the balance of the portfolio is within aviation, marine cargo and contingency.

As Alex alluded to earlier, a large proportion of their business is core. And this is something, as you can imagine, resonates quite strongly with us at Lancashire, it's something we talk about quite a lot; as does the stickiness of their portfolio, which emanates primarily through their 20 year-plus relationships that the underwriters have with their clients.

Both of these were key considerations for us when we were looking at the deal.

All their classes have performed incredibly well through the cycle which they've managed to successfully navigate significant market losses of recent years, demonstrating not just the quality of their underwriting team. But also their ability to create, place and structure reinsurance programs. But also their strong underwriter-led culture within the business.

These three things are things that we identify very strongly with at Lancashire. Charlie and Alex will talk a bit later about their underwriting results and their specifics about their underwriting team.

Moving on to one of the key attractions of the proposition was the relative limited amount of overlap with our current portfolio, which both Charlie and Alex have alluded to.

The Property Treaty portfolio occupies a very different space to the Lancashire Treaty portfolio. Their niche focus on smaller regional programs, both in the US and internationally, complements our preference for the larger limit, super-regional and nationwide programs that benefit our larger line size.

A lot's been spoken about the D&F portfolio, for obvious reasons. As Richard mentioned at the outset, the way they underwrite and their approach to D&F is very different to how we did it.

We obviously focus on this quite a lot, given our recent exit from the class. But what we found was that they run a very profitable business in the D&F sector.

Very simply, our approach used to be large lines at the top of programs and the Fortune 500 companies. Their approach is significantly smaller lines on a broader client base, which does include an element of binding authorities.

But probably as importantly, sitting behind this is a very well structured, significant reinsurance program that has allowed them to remain profitable right throughout the cycle.

In essence, it's probably on the D&F side this through-cycle nature of their portfolio that best differentiates their approach from ours.

As Charlie mentioned, we were okay at D&F and we made money. And our approach worked in a hard market. But in a slightly different market, those larger line sizes, with the parameter risk, the impact that that has on our PMLs and the drag on capital that that can have, becomes less viable.

The way they write it. And probably as importantly, the way they reinsure their portfolio, doesn't give us those issues. Instead, what we get is access to a profitable through-cycle portfolio of business.

In the other lines, there's limited amount of overlap, or really no overlap at all. We do write aviation. But their portfolio is treaty based. We access our aviation premium through the direct clients. And we don't write marine cargo and have very little contingency exposure. So overlap there is negligible.

Jonny Creagh-Coen {BIO 20677871 <GO>}

And Charlie, I leave it to you to have a quick chat about the numbers please.

Charlie Mathias {BIO 16185351 <GO>}

Yes. Very quickly, there's the underwriting record. They've got a mean result of 91.4% over the last five years. Very consistent across all their lines of business. Obviously, 2011, with those major international cat losses, they did pick up some loss there. They've restructured a bit after that. And we're satisfied that they've addressed issues there.

As Paul's mentioned, outwards reinsurance, Mark Wilson, their buyer, recognized one of the best and canniest reinsurance buyers in the market. And that's certainly an area where we would look to learn from them.

Additionally, the combined Company's reinsurance spend will be north of $100 million. And that's going to give us a lot of clout with brokers. And again, we hear a lot about relevance at the moment. Believe me, having that kind of spend gives you a lot of relevance with brokers.

Reserving; very prudent. Again, with that private equity backing, they had -- they took a very, very prudent approach to their reserving. There might be some benefit for us in there.

Investments; again, Elaine will talk to you more about that. But very same attitude as us; make the money through the underwriting, just try not to lose money on the investment side.

On the funds at Lloyd's, there is redundancy. They've noted that redundancy in their annual report. And again, that might give us some leeway.

And they've got -- on their Solvency II, they, Lloyd's has been very thorough in its preparation. And they have green light status from Lloyd's on that. So very well prepared, well run, well situated.

Jonny Creagh-Coen {BIO 20677871 <GO>}

Thanks, Charlie. Alex, do you want to just have a quick chat about --?

Alex Maloney {BIO 16314494 <GO>}

Yes, sure. Obviously, what's been quite obvious from everyone's comments, that we think this is the right cultural fit. I think from my point of view, that was the most important part of this deal. Obviously, the business had to make sense, that we need to have a good working relationship with these guys.

Their management team speak plain English, like we do. They're very open in their approach, we like that. And as I said earlier, from our first meeting, the (inaudible) was high.

Their underwriting philosophy's the same as ours as well. But you have to understand they're in Lloyd's, their combined ratios will never look like ours. And they had a PE owner as well. So as we've mentioned earlier, we think these guys have got the track record and the ability to take Cathedral forward.

We think there's lots of things we can do with them. As I said earlier, we've just added 14 high-quality underwriters to our team. This deal is digestible for us, it's not a big company. There's only about 60 people.

One thing that we've been very aware of from day one is that Lancashire is a tight bunch, some may even call it a cult. And they're very similar to us. They're very defensive of their people.

As Richard said, they've been together for a long time. Most people at Lancashire have all been here for a long time, if not from the start. So we're very aware of the culture issues. We think it works. If we didn't think the culture issues could be fixed, we wouldn't even look to the deal. So we're very positive about working with them in the future.

Jonny Creagh-Coen {BIO 20677871 <GO>}

I'm going to hand over to Elaine. I won't call her what Richard (inaudible).

Elaine Whelan {BIO 17002364 <GO>}

Thanks very much. I think we've probably heard most of it. But let me wrap it up in the numbers for you and our approach to this. We have done a lot of modeling in the numbers, I think our advisors might agree with that one.

Having looked at it a number of different ways and done stress testing and our test on that. So our base case for just now, if you like, is looking at it from the current market outlook. And with that current market outlook, we think that it adds about 2% or 3% to our leads. That's assuming that we're in a softening market. And that continues for a while.

Obviously, if we are in a harder market environment, then we get incrementally more benefit from it as we're able to leverage off of both platforms. So there's a benefit from it there.

Charlie made (inaudible) earlier. And we think the licenses will give us access to markets where we've found the bureaucracy's too much to cope with up until now.

In terms of capital efficiencies, Alex mentioned it as well. It's a private company, it's partly owned by management. This is very conservative the way capital stands. So there are (inaudible) which we can strip out.

There's also things that we can do just by virtue of being the Lancashire book, in order to try and structure them a bit more efficiently for capital. We can re-insure them within the Group. We can bring them into our UK tax (inaudible) for example. And we get some benefits from that too.

Charlie mentioned that theirs is a short-term book of business, we understand it very well. We have a high degree of confidence in the numbers. We think that there is an excess there, (inaudible). So we can strip out some of that as well.

What we haven't done is assume that there's any cost synergies. We didn't make an acquisition decision by assuming that we would end up (inaudible) and cutting back (inaudible). As you've heard, we want to keep the underwriting team and also want to keep the backlog of teams. They have the experience of the Lloyd's environment. And we value that quite highly.

There may be some synergies over time. But we certainly haven't assumed it when we were making the decision about whether to buy the company or not.

And I think probably the last point on that slide, is a fairly important one. We've been talking the last couple of quarters about how much excess capital we've got. And how we thought that we'd end up returning earnings later on in the year, once we were in season.

We are financing this through a part equity placement, part cash. That allows us to keep (inaudible) and obviously (inaudible) that hedging there. So there's every possibility that we'll still end up paying a special dividend later this year if nothing changes in terms of our outlook.

In terms of what all the cash will (inaudible) structurally means for Cathedral, it means that once we've gone through the process of putting that in place, after the deal completes, then there's a possibility that we might end up paying a further dividend in the First Quarter of next year, when we're trying to do something about that excess capital.

And going forward, the view I think you've heard from a couple of people is it's exactly the same. We'll be sticking to the small ordinary (inaudible) and if anything changes (inaudible) again to returning capital.

So I've mentioned the financing already, we're going the cash box route. We are paying 1.6 times March 31 value, which is essentially 1.5 times the June net tangible assets. We do think that that represents value. We've seen Lloyd's people go for 2 times book in the past. And we think that we're buying quality of operations, short-tail business, which is well understood. Again, with it being short tail, there can't be too many skeletons in the closet.

In terms of the process from here on in, our circular should be out later on this week. And then, it's a case of having our SGA which will be early September (inaudible).

Jonny Creagh-Coen {BIO 20677871 <GO>}

Thanks, Elaine. Richard, maybe you just want to close our comments before we take the Q&A.

Richard Brindle {BIO 1983776 <GO>}

Yes. Sure, Jonny. Yes, I think what I really want to do is reassure everybody that we haven't stopped being Lancashire. We are still the same people. We will still be extremely nimble in the marketplace. We will still look to pay large special dividends, results allowing.

We will continue our remorseless focus on underwriting profitability, low investment risk. But I think it is -- although it's arrogant, if you like, to just persist with a certain business model, regardless of the cycle. And we have to acknowledge that we face certain headwinds in the market. And as a management team, we need to take measures to mitigate the headwinds that we face.

I want to be very clear, had we not found a really quality partner in Cathedral, we would not have done a Lloyd's acquisition for the sake of it. We do believe that most of the smaller Lloyd's operations are small for a very good reason, because they don't really bring any unique selling points to the party.

And indeed, we feel that the Tail End Charlies, as you might call them, are facing, frankly, an existential threat to their relevance and existence. But Cathedral is very, very different from that. We think they're a tremendous bunch of people.

They have a tremendous track record over many, many years. And we look forward to working with them. And we hope you guys will welcome this transaction as a sensible move for the Group.

Jonny Creagh-Coen {BIO 20677871 <GO>}

Thanks very much, Richard. We'll now do Q&A. We'll take the room first. And then we'll take Q&A from the line afterwards. So it's probably best over to you people.

Questions And Answers

Q - Tom Dorner {BIO 15847486 <GO>}

Tom Dorner, Citi. Just two questions. The first is on the rationale for doing the acquisition. So you said that one of the challenges that Lancashire would face over time, is it might be a bit not relevant enough and too narrow. But in a prolonged softening market, you've got to assume that's how things play out.

Why does adding this business improve the situation for Group? And isn't it better to be narrow in a prolonged soft market?

Then the second question is you might not be able to give this right now. But you mentioned a couple of areas of upside, like tax and extracting funds at Lloyd's and doing something on reserving. Can you give any numbers around those?

A - Richard Brindle {BIO 1983776 <GO>}

Okay, Tom, why don't I deal with the narrowness point. And then Elaine can deal with the second part of that. I think our point about narrowness is that if we face two years or three more years of these sort of market conditions. And we're really only writing four or five specialty lines, we could come under pressure from brokers, to clarify to them, our relevance in the marketplace.

If we have multiple platforms, multiple lines of business, as Alex mentioned, a sharply increased reinsurance spend, then when he and I sit down with a great case, or a down glazer at Aeon or Marsh and discuss the state of the world, we just have a lot more weaponry at our disposal.

It further insulates us from discussions about writing broker facilities. It's fair to say we have not come under pressure to write those to date. Because of our leadership status on most of our business. And our large line size, we're not an obvious target for those sort of conversations. Again, it is the Tail End Charlies who are in the headlights for those sort of conversations.

But it just gives us additional clout in the marketplace. And I am concerned that three years down the line, Lancashire, however successful we are, just writing four or five specialty lines of business, I'm just concerned that we simply look too exotic and too narrow.

But Elaine, perhaps you could talk about the second bit?

A - Elaine Whelan {BIO 17002364 <GO>}

Sure. In their financial statements for last year, they've got disclosure in there about their funds at Lloyd's. And their capital requirements. They had about GBP170 million in funds at Lloyd's and about GBP138 million of capital requirements. And that's in sterling. So there's your excess [ph] there for a start on that one.

On the other stuff, we've modeled it and they've looked at the numbers, that some of it will be a case of once you get in there and get a closer look at it, (inaudible) we will adjust for their patterns and want to keep their [ph] excess. They do have an excess over their external actuaries which might (inaudible) out. But that's going to be a bit more of a drip over a couple of years more than likely.

Tax-wise, we do plan on reinsuring the corporate members to Bermuda which gives us the benefit of consolidating our investment portfolios in Bermuda. And there's also a tax benefit from that.

And final level numbers forward, there are --

Operator

Apologies for the interruption conference, this is the operator speaking. Can the speaker in the room please readjust their microphone? The audio is not coming through.

A - Elaine Whelan {BIO 17002364 <GO>}

(inaudible) costs that relate to the (inaudible) pressures that have been redeemed as part of this transaction, you can back that out straight away. Then I would add on some efficiencies that you can get between underwriting portfolios, (inaudible) a bit more of a runway on that.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Maciej.

Q - Maciej Wasilewicz {BIO 16462204 <GO>}

Maciej Wasilewicz, Morgan Stanley. So I'm just on the numbers again, my first question. Roughly, if we take out the tax that Cathedral paid. And then you also add back in the GBP9 million, if there was something in the mid (technical difficulty) in terms of what you paid last year.

If you add a couple of million for underwriting efficiencies. And then maybe you take off GBP30 million off the purchase price, the ROE of the purchase, it still looks to be round about 10%. I've heard the figure that the ROE actually that you're expecting is much, much higher than that from the acquisition. So I was just wondering if you'd take me through the missing bits in my logic to get to the figure?

The second question I had is on the management incentives. You've already mentioned that you'd give shares to the incoming management in Lancashire which gives them a long term -- aligns that long-term incentive with Lancashire. But importantly, within that as well is, if they're given shares and can walk away straight away and sell them, it doesn't actually provide them with necessarily a reason to stay.

Obviously, they might be ambitious about and excited about the opportunity. But I'm just wondering, just on the financial side of the incentive structure, what is in place to give them an incentive to stay during the transition to the new situation for them?

And finally, just on the size issue, you've already mentioned that broadening the number of lines is an important factor to remain relevant. I'm wondering if, just looking at the amount of capital that you hold. And in particular, I guess maybe in the property catastrophe business, you might need a certain size to remain relevant.

I'm wondering if, over time, that benchmark for the minimum size you need to be to be relevant, that market has been increasing? And if so, does that create a long-term pressure for you to grow a bit in terms of your capital through acquisitions or retaining capital? So in the long run, you can't be -- you can't just do what you've done in the past, you just stay where you are and give away dividends in the run, you'll have to be a growing Company. Is that -- those are my three questions.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Richard, why don't you -- no, I mean, sorry, Elaine, take the first one on ROE.

A - Richard Brindle {BIO 1983776 <GO>}

Sorry, Jonny, I didn't catch that. What did you say?

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Probably the second one on the tax issue and then, Richard, if you can look at the last one.

A - Richard Brindle {BIO 1983776 <GO>}

Yes, sure. I think probably to expand on my previous answer, if I understand the question, you're saying is it viable for us just to continue to shrink back in an ever-softening market. And perhaps I should have included this in my previous answer to Tom's question.

The short answer is no. Elaine can give you more detail. But you reach a de minimis position where you cannot reduce your capital any further. So the denominator, being the capital, stands in the way of your ROE and you simply can't reduce it any further. So I think that's an important point in favor of our argument about how we needed to reposition ourselves for a prolonged soft cycle.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Thank you, Richard. Elaine?

A - Elaine Whelan {BIO 17002364 <GO>}

Yes, on the missing bits, it's more about what we can do in the underwriting side of things, it's more about adding in new business lines, it's about looking at their loss slips, which has been very conservative. And looking at (inaudible) what we think our experience and knowledge base is on that.

It's about reassessing the capital base, pulling out those excess reserves and streamlining our capital base. So we look at it, we tend to look at it from a rating agency perspective and there's much less capital needed for the rating agency perspective than they've been carrying. So we can look at ROE by (inaudible) trimming down the capital.

So when we look at it on the rating agency basis with the capital that we need to carry, we're seeing in excess of 20% returns on that. Now obviously, you put a bit of headroom on that. So it's obviously that a bit. But that's where we're seeing it coming in.

On the management incentives, there is a (inaudible) component of the consideration which runs out for three years for all of the partners. And for some of the other individuals that hold stock and (inaudible) in pref shares in the organization. And they've also put in place an ISF [ph] scheme which is based on (inaudible).

That's a form of invest over three years and then there's a further two-year time vest on that. So we're kind of locking them into that three-year to five-year time horizon with that.

Q - Angela Gu {BIO 18078706 <GO>}

Angela Gu, UBS. I have three questions. The first one is if you're issuing equity to fund this acquisition and then planning on returning a portion of the capital related to this afterwards, why don't you use debt issuance rather than -- why do you take money from shareholders and then return it back to them after the acquisition?

My second question is related to the first one. So on special dividend, I just want to clarify. So in this year, in November, you might disclose your plan for capital return for this year and there is no change in the outlook. Then, in next year in Q1, you might consider another special dividend related to the acquisition. Is that correct?

Then on the third one, I just want to get understanding of your business mix after the acquisition. Are you potentially just having to recall the first one is the regional Lancashire and you write large size and there is no change in that? Then that's just playing defense at the current softer market. Then you have a special -- a new development in the Lloyd's market. And then you keep the business mix relatively unchanged from their previous plan and basically just operating two operations? Thank you.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Okay. Thanks, Angela. I think the first two probably is Elaine and then, Richard, the last one please.

A - Elaine Whelan {BIO 17002364 <GO>}

Sure. On your second question, yes, you're exactly right on that one. Why equity and not debt? We don't get credit in the rating agencies models (inaudible) 20% leverage and (inaudible). So arguably, there's service charges. But it doesn't count so we weren't interested in that.

Equity allows us to carry excess headroom through wind season. It also allows us to (inaudible) given where we're trading and then it means that we can assess our outlook for the next year without having to think about raising cash towards the end of the year. So it gives us that security there.

So if we do (inaudible), it's because our outlook hasn't changed but it means if something does happen, we still have that excess there to use for this year.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Richard? I think we've lost Richard. But, Alex, can you take that?

A - Alex Maloney {BIO 16314494 <GO>}

Yes, sure. I'll take that. I don't think you should look at it like we're going to be defensive at Lancashire and aggressive at Cathedral. I think that one of the things we like about these guys is they think like we do. But obviously, within a Lloyd's framework there's --.

Q - Unidentified Participant

Hi, have we lost Richard? Hello?

Operator

Hello, it's the operator.

Q - Unidentified Participant

Is everything okay?

Operator

No. I'm afraid the sound from your sound is virtually non-existent. We cannot hear what's going on, on your side. And the speaker, Richard, has also disconnected. I believe he's reconnecting now.

Q - Unidentified Participant

Okay, perfect. Nothing has changed. Has it just happened in the last few minutes?

Operator

It's been most of the conference I'm afraid, most speakers.

A - Richard Brindle {BIO 1983776 <GO>}

Yes, hi. Sorry, I lost the line there for some reason.

Q - Unidentified Participant

Okay, let me see if I can adjust things. It's just too low is it?

Operator

It's too low, yes. We can hear you, Richard. Richard, can you please not place your phone on hold. It gets broadcast to the conference.

A - Richard Brindle {BIO 1983776 <GO>}

Can I please what?

Q - Unidentified Participant

If you cannot put your phone on hold, Richard, because every time you do, we hear a machine telling us that you're on hold.

A - Richard Brindle {BIO 1983776 <GO>}

Oh okay, okay.

Q - Unidentified Participant

Okay. Thank you. I'm going to try and see if I can make this louder for you, Richard.

A - Richard Brindle {BIO 1983776 <GO>}

Put me back in the conference now please.

Q - Unidentified Participant

Okay, no problem.

Operator

You are live to the conference now.

A - Alex Maloney {BIO 16314494 <GO>}

(inaudible) adding new lines. They've got a better relationship with Lloyd's. If you're in Tier 4, Lloyd's won't really allow you to do anything so even if it's a great opportunity, they're going to load your capital, you're going to have to buy more reinsurance, you're just not going to get the opportunity. So we think within the Lloyd's framework, for their size, they're as good as you can be within Lloyd's. So that will give us options.

Q - Angela Gu {BIO 18078706 <GO>}

Then they will remain in Tier 2. So you're not going to expand them?

A - Alex Maloney {BIO 16314494 <GO>}

I don't know enough about Lloyd's to be totally honest if we can -- if we expand, we get to Tier 1, I don't know what their criteria is. But maybe.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Charlie?

A - Charlie Mathias {BIO 16185351 <GO>}

Yes, just particularly as we've got Darren here, I think we ought to be reminding people, this doesn't make us a two-legged stool. We're a three-legged stool now. We've got Kinesis as well.

Darren's been working been very hard at that. We've very pleased with how that's developing. So when both for the soft market and for the hard market, we now have got three different ways of approaching that market and selling capacity to people. So I think that's important to recall.

Q - Angela Gu {BIO 18078706 <GO>}

Thank you.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Christopher?

Q - Christopher Hitchings {BIO 2034501 <GO>}

Christopher Hitchings, KBW. Cathedral has two syndicates at Lloyd's, one wholly owned, one --

Q - Unidentified Participant

Has the quality improved any better? Are you still finding it hard to hear things?

Operator

It's still quite low from my observations.

A - Richard Brindle {BIO 1983776 <GO>}

Guys, please don't interrupt when I'm trying to listen to the questions.

Q - Unidentified Participant

Okay, sir.

A - Alex Maloney {BIO 16314494 <GO>}

(inaudible) interact with the guys at Cathedral. Some of the -- there's some real benefits from having the wholly owned syndicate. But at the moment, the capitalization within that is relatively small.

There are things you can look at about bringing the syndicates together but that would involve some agreement of the names within 2010 which we'll look at and these are all the things that basically we'll look at it with them. They're the guys with the experience within Lloyd's and find the best possible way for us to develop our specialty lines.

It may be that it's bringing the syndicates together. It may be we do it within 2010. But it will need to be on a basis where we've got a reasonable line size in areas such as energy and terror --

A - Richard Brindle {BIO 1983776 <GO>}

If I can just add to that, for someone like Darren, it's very exciting as well, because of the names' capacity; for Kinesis, it's another subsidiary that we think has some good potential for (inaudible) there as well.

A - Elaine Whelan {BIO 17002364 <GO>}

And just in terms of the number side of things there on model benefits. So they're about the future benefits we can extract outside of all the plans we currently have.

Q - Christopher Hitchings {BIO 2034501 <GO>}

And just also, you talked about how you might move some of Lancashire's business into the syndicate. Was that --?

A - Paul Gregory {BIO 16314515 <GO>}

No. I think it will be more of a case of accessing the same lines of business within Lloyd's. I don't think it will be a case of we'll be transferring lines of business into the syndicate. I think, as Richard said, we'll see much more passing trade. I'm sure there's a lot of middle market business we don't see, some of it will be attractive, some of it won't be. But I don't think it's a case of shifting business out of Lancashire into Lloyd's. I think it's just another outlet there.

Q - Christopher Hitchings {BIO 2034501 <GO>}

No. Yes. But there's not a possibility that there's going to be the guys on the box, on the Cathedral box are going to be capable of writing for Lancashire as well as the syndicate?

A - Paul Gregory {BIO 16314515 <GO>}

Yes.

A - Richard Brindle {BIO 1983776 <GO>}

And I think, Paul, you're going to be spending a lot of time integrating between them and us as well aren't you?

A - Paul Gregory {BIO 16314515 <GO>}

Yes. Yes, especially on the specialty lines.

A - Alex Maloney {BIO 16314494 <GO>}

Yes, yes. And again, as Jonny said, there will be scenarios where Lancashire will get presented with, say, a risk in Brazil, which we can't currently write. So that will have to go through Lloyd's and I'm sure if they get offered an opportunity that doesn't fit the Lloyd's model, we can put that through Lancashire. Obviously, anything that goes through Lancashire will go through our conference call. So we'll have to agree the deals that go through Lancashire. But again, it just gives us flexibility.

A - Richard Brindle {BIO 1983776 <GO>}

And I'd also, just to remind you, we've just employed Joe Smooth [ph] who's been in Lloyd's for how many years, P.G.?

A - Paul Gregory {BIO 16314515 <GO>}

15.

A - Alex Maloney {BIO 16314494 <GO>}

About 14 years ago [ph].

A - Richard Brindle {BIO 1983776 <GO>}

So (inaudible). So there's going to be a lot of overlap and a lot of discussions to be had.

Q - Christopher Hitchings {BIO 2034501 <GO>}

And finally, I don't think, Elaine, you answered an earlier question about how you reconcile the ROEs that you claim in the press release of 26% (inaudible) of your ROE (inaudible) basis and yet you somehow got a net tangible assets acquired, in which the equity has (inaudible), you've added preference shares and other debt instruments to the equity.

A - Elaine Whelan {BIO 17002364 <GO>}

Yes. It's the design of our capital structure. So they've got -- at the end of December, they had GBP151 million of net tangible assets and just over GBP50 million of that was actual common stock. The rest of it's the loan at the pref shares, which sit in the liability side on the balance sheet. But it counts as capital for their model. It's essentially designed that way because of the private equity ownership. So that whole amount falls into capital. But when you're looking at return on equity, it'll be smaller.

Q - Christopher Hitchings {BIO 2034501 <GO>}

But those aren't net tangible assets. It strikes me that you've made this out to be a 27% ROE business that you're buying at 1.6 times NTA. And I don't think those figures are comparable.

A - Elaine Whelan {BIO 17002364 <GO>}

I think the way that I would think about it is that we need to (inaudible) to our ROE and that's very much the way that we look at it.

Q - Christopher Hitchings {BIO 2034501 <GO>}

But you agree that the ROE quoted and the price at NTA quoted are not on a comparable basis and therefore, we shouldn't think you're buying a 27% ROE business on 1.6 times NTA?

A - Elaine Whelan {BIO 17002364 <GO>}

I wouldn't count it as a 27% ROE business personally, as some of the margin (inaudible) was done in conjunction with their business partners. Lloyd's have a different way of looking at it. If you think about it in terms of adding 50 points on to ROE, giving in excess of 20% return in terms of our rating agency capital (inaudible), I think that's a fairer way to think.

Q - Christopher Hitchings {BIO 2034501 <GO>}

But in terms of the NTA you're buying, it is correct; it's about an 11% return business. I think that would be the (multiple speakers).

A - Elaine Whelan {BIO 17002364 <GO>}

It's about 13% or so, I think for 2012.

Q - Christopher Hitchings {BIO 2034501 <GO>}

Thank you. So much.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Ben?

Q - Ben Cohen {BIO 1541726 <GO>}

Ben Cohen, Canaccord. Can I ask -- you mentioned in terms of the size of the lines that Cathedral is writing, that any individual deal doesn't really impact your PMLs or RDS. Could you talk in an aggregate basis as to if you'd absorbed them already where they would stand, how much of an increase there would be?

And is this a business that you would have reinsured yourselves? I take it you don't reinsure them. And have their re-insurers made similar returns as Cathedral has over time? Or have there been arbitraging the re-insurers?

A - Paul Gregory {BIO 16314515 <GO>}

The best example is their D&F book. If you look at our D&F book, our maximum line was GBP75 million. Probably at average it was GBP35 million/GBP25 million. Cash exposed, as Charlie said, could be volatile.

We did make money on that basis. It's very much when we started writing D&F, it was a great market. But equally, that's where you need the conference call. We have our conference call because we write big tickets. As Charlie said, you could write Wal-Mart and that could move your capital if you write a big enough line size.

If you look at Cathedral, I think their average line size is $3 million. So for those guys, they're typically writing like the second layer of a program. So 25 over 25. We were typically writing the 100 over 100. They write a lot of business. About 40% of that is buying the business as well. And they buy a huge amount of reinsurance.

So it's a very different animal. It's a transactional account. Part of the issue we had with D&F was customer loyalty and they will openly admit that that's still an issue in the D&F market, albeit because of those guys' track record, they do have a lot of loyalty from the brokers and they're quite entrepreneurial. But it's a very, very different beast.

If you look at their reinsurance, no-one at Lancashire would write their reinsurance program. If you look at the spend versus recoveries, it's quite breathtaking how good they are at purchasing and reinsurance. There's -- I think their loss ratio on their reinsurance was like 90%. So no, we don't write their reinsurance.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

And Darren, you're probably the best person (inaudible) as well?

A - Darren Redhead {BIO 17995744 <GO>}

Yes, I mean when would we reinsure them? Probably not because they're very good purchasers. But to say do they overcharge [ph] the market, that meant (technical difficulty)

Q - Ben Cohen {BIO 1541726 <GO>}

And just on your (inaudible)

A - Unidentified Speaker

(inaudible)

Operator

Hello, it's the operator. If the main room is able to hear us, we cannot hear the audio coming from your side. Please adjust your microphones.

A - Unidentified Speaker

(inaudible)

A - Elaine Whelan {BIO 17002364 <GO>}

(inaudible) in the document the cover in that period. There isn't a material adverse condition clause in there. But we're going to come forward to the view that some of the business given the short tail to look at what we've got in there.

A - Richard Brindle {BIO 1983776 <GO>}

You just have to look at their book at Katrina. I mean look how well they've --

A - Paul Gregory {BIO 16314515 <GO>}

Well we're getting (inaudible) because they'll buy so much reinsurance as well, it's hard to lose that material amount of business.

Q - Andrew Ritchie {BIO 18731996 <GO>}

Andrew Ritchie, Autonomous. Just one question on the financials. The fee and commission income I'm assuming is the profit commission from the names' participation. So presumably that was depressed in 2012 because is reflects some of, I guess, the weaker of the heavy cat years 2010/2011? Is that --

A - Elaine Whelan {BIO 17002364 <GO>}

Yes. That is that. Yes. There's a lag on that as well.

Q - Andrew Ritchie {BIO 18731996 <GO>}

And is there anything unusual about the profit commission arrangements versus standard launch [ph]?

A - Elaine Whelan {BIO 17002364 <GO>}

No. And we're quite happy to have that extra income stream there as well.

Q - Andrew Ritchie {BIO 18731996 <GO>}

And the other question, just to be clear. I think you said there's no plans to write more of existing Lancashire's business within the Lloyds platform. But in theory, if you did that, there would presumably be significant capital synergies, or capital relief from writing some of your existing Lancashire business within a Lloyd's structure.

A - Elaine Whelan {BIO 17002364 <GO>}

Yes, I mean, we'll be assessing what makes sense in each platform; that's the beauty of having them both sharing a --

A - Richard Brindle {BIO 1983776 <GO>}

I think the point we're missing here is that we have a wonderful energy portfolio as it is right now. The fact that we have the clout and the market presence is no reason subject to Lloyd's giving us the ability to do it, is to build out that a little bit more within a much more capital friendly structure being in Lloyd's.

So you'll just expand those with the relationships in the book we already have, plus, don't forget, James Blube [ph] comes in and he'll bring us new opportunity, that may well fit much better in there. So there's lots of things we can do and we will do.

Q - Unidentified Participant

It might be terrible timing actually, referring to the acquisition costs of GBP266 million, just working out the funding on that. You've got the placing for GBP130 million, you've got Lancashire's earnings this year, you seem to -- there's a bit of surplus cash in (inaudible). Then is there anything to do with your cash flow requirements? Is there any moving parts in that year-on-year? You cut your retro and D&F. So I'm just trying to work out previous expectations is 100% payout this year, I'm assuming we should be expecting it's slightly less than 100%, it's just trying to get to that sort of area.

A - Charlie Mathias {BIO 16185351 <GO>}

Yes. The capital management philosophy doesn't change. So if we generate profits that we cannot deploy into the business, we will pay them back to the shareholders. So that doesn't change.

I think Angela raised the point earlier about splitting that special, as we did this year over Q4 and Q1. That is likely, both because -- with the completion of the deal and then the Lloyd's business planning process, it is likely that we will have to do two and I think Jonny's preference, having spoken to a lot of our shareholders, is to do two now in future.

But in terms of our ability to fund those specials, yes, we certainly do expect to be paying out on the same basis. Can't deploy it in this business, we pay it out.

Q - Unidentified Participant

And on current assumptions, do you --

A - Richard Brindle {BIO 1983776 <GO>}

Your assumption is getting close. I don't think it will be 100%. But it'll be very close to.

Q - Unidentified Participant

Okay. And just to be clear, when you're talking about Q1, you're talking about full-year announcements?

A - Richard Brindle {BIO 1983776 <GO>}

Yes. So similar to last year. November, when we have our Board meeting, we'll have had time, we'll be able to assess what's happening with the storm season. These guys, along with our new partners, will assess what they think the market's doing and all the other bits and pieces. And we'll make a decision then.

Then, we've already said it's prudent to carry a little bit more capital through that last six weeks, seven weeks, eight weeks of the year. Again, you get a proper view of the market, a proper view of what we can do with some parts of Cathedral and then we'll reassess again as we did this year in the First Quarter.

A - Paul Gregory {BIO 16314515 <GO>}

And we will be more weighted towards one/one, their books weighted towards one/one. So the sort of two/two specials will be even more important for us.

A - Richard Brindle {BIO 1983776 <GO>}

Are there any questions on the phone line please?

Operator

(Operator Instructions) Andrew Broadfield, Barclays.

Q - Andrew Broadfield {BIO 7273415 <GO>}

I'm sorry the line wasn't terribly good. So if I ask a question that's already been asked then answered, I apologize.

Just one question on Cathedral and the reinsurance buying performance, which you've mentioned a few times. And I'm only -- I may be looking at the wrong data. But it looks to me that the gross to net performance has been tremendous, as you point out.

I just wondered whether that's sustainable. It clearly has been sustained for a time. One of your Lloyd's peers also used to have a tremendous reinsurance buying performance until the key person left and it somewhat deteriorated after that.

I just wondered how much of Cathedral's tremendous performance has been because of that buying capability and, therefore, the fragility of that performance going forward, if that's such a key part of their overall performance. Just your thoughts on that.

A - Richard Brindle {BIO 1983776 <GO>}

Yes, I think I'll take that one, Jonny. I think it's a very good question. Look, we can't lock these guys up in handcuffs. They're individual people and they will do whatsoever they want to do with their lives. But I think it is fair to say there's an extremely good social mix between the two management teams.

I think this is why we prevailed over the other bids. I don't we were actually the most expensive bid. We worked hard at delaying sales (inaudible) incentivization package.

These guys enjoy what they do and they're very good at what they do and we want to create an environment where there's every reason for them to stick around, both financially and socially for the long haul.

So I can't guarantee to you that nobody's going to leave. But I think it's highly unlikely and we're going to work very hard to keep the team together.

Q - Andrew Broadfield {BIO 7273415 <GO>}

And just to come back slightly on that. And clearly, that's the key, you can't lock these guys up forever. But I guess it's more a question of quality of the underlying.

If the gross performance has been somewhat less impressive than the net, then that raises a question about the core sustainability of the business.

The reinsurers might walk away one day, I don't know what those programs are. But it does raise the question as to the underlying quality versus what perhaps they've managed to achieve with that reinsurance.

A - Richard Brindle {BIO 1983776 <GO>}

Yes. No. I understand the question. Perhaps Alex or Paul, you could talk about the growth in that?

A - Paul Gregory {BIO 16314515 <GO>}

Yes, sure. I think the way you need to think about it is, these guys are very joined up on their front and in their reinsurance buying. So you're not going to get a situation where if they can't place the reinsurance, they're not going to write the exposures.

You have to think as well that as the direct to writings reduce, as the market softens, the reinsurance market is softening at the same time. With the arrival of third-party capital, that has gave them opportunity; they've actually -- they buy a core program with the kind of people that we would buy reinsurance of. And then they trade round the edges and they buy it opportunistically from some of the new capital that's arrived in our market.

So these guys are very, very tuned into their front end versus their back end. There's not going to be a scenario where if they can't place the reinsurance, there's not going to be a huge book of business that they continue to write; they'll just adjust their writings. And yes, look, they have a great reinsurance buyer but that's not the only person within the Group that's got experience in buying reinsurance.

So as Richard said, we can't guarantee that everyone's going to be here forever. But we do have a number of high-quality individuals that are used to purchasing reinsurance for the Lancashire Group already.

Q - Andrew Broadfield {BIO 7273415 <GO>}

That's very clear. Sorry, can I just add one more question as well? Just going back to some of the historical comments you've made around Lloyd's. You've talked about concerns around the cost base of Lloyd's and the perhaps lack of flexibility if you're within Lloyd's because actually, you've got a pretty intense supervisor watching you to make sure you're performing in the way that they want you to.

How does that change -- none of that changes now in reality. But clearly, your perception of the benefits outweigh that now. Do those concerns still weigh, or do you look at it slightly differently now?

A - Richard Brindle {BIO 1983776 <GO>}

I think first of all there's, if you'll forgive me, a slightly inaccurate impression that we've become an anti-Lloyd's in the past. We never have been. I was in Lloyd's for many years. I've actually gone on record as saying I think the Lloyd's market has done a tremendous job of getting its act together since the late '90s when I was in Lloyd's.

I think there's some really excellent businesses in there, mainly the larger ones. But as I said earlier, I think Cathedral is something of a gem amongst the smaller syndicates.

And yes, the flexibility is more limited. I spoke, along with the CEO of Cathedral, with Tom Bolt yesterday. And we talked about some of our initial thoughts about what we might do with the Lloyd's platform. And he said, look, yes you're going to have to make a persuasive case to us if you want to introduce new lines of business. But he said, having said that, Cathedral has a high standing in the eyes of the Lloyd's authorities; their track record and their team are testament to that. And he said. And you guys at Lancashire have an extremely impressive track record. So if you bring us a well-argued and persuasive case, we're going to listen to you.

So I think it will be incremental. And we're not looking for sudden growth in Lloyd's. We very much view this as a mature business which we will augment around the edges rather than fundamentally play with the DNA of it. And I think it's also fair to say that the real nimbleness and flexibility will continue to be, with Lancashire itself, where we're not subject to the Lloyd's supervision.

I think you've seen with other companies they operate effectively with a Lloyd's and a non-Lloyd's platform. And all we're doing is replicating that. But we would argue that we have market-leading underwriting statistics within Lancashire and we will augment that with the Lloyd's platform. So yes, the growth in Lloyd's will be incremental and the main nimbleness will be in the Lancashire platform.

Q - Andrew Broadfield {BIO 7273415 <GO>}

Okay, that's very helpful. And sorry, just one more question if I may. The flexibility in capital between Lloyd's and non-Lloyd's platforms now, presumably that's not one of the flexibilities you're going to gain particularly from this; it's much more flexibility within the two portfolios rather than flexibility across the portfolios?

A - Charlie Mathias {BIO 16185351 <GO>}

Yes. That's right. We wouldn't -- it's not really a question, certainly in the short term, of moving capital around the Group. It's really about where we most appropriately write the business.

Q - Andrew Broadfield {BIO 7273415 <GO>}

Okay, very clear. Thanks ever so much.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Do we have any more phone questions?

Operator

There are no further questions on the telephones at this time.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Okay. So Richard, would you just say a couple of words to wrap up then please?

A - Richard Brindle {BIO 1983776 <GO>}

Yes, sorry the line hasn't been great. But thank you very much, everybody, for coming in. We'll take any questions at any time.

We think this is a great move for our Company; we appreciate it may have come as something of a surprise to some of you but we think there's a strong logic behind it.

We think we can put these companies together and achieve even better results than the separate entities have achieved to date. And we go forward with great confidence.

A - Charlie Mathias {BIO 16185351 <GO>}

Great, thank you. Jonny and I and the rest of the management team will be available throughout the day and possibly the night. So do call Jonny first with any questions. Thanks very much.

A - Richard Brindle {BIO 1983776 <GO>}

Thanks.

A - Jonny Creagh-Coen {BIO 20677871 <GO>}

Thank you.