S&P Capital IQ

CONTENTS

Markel Corporation NYSE:MKL

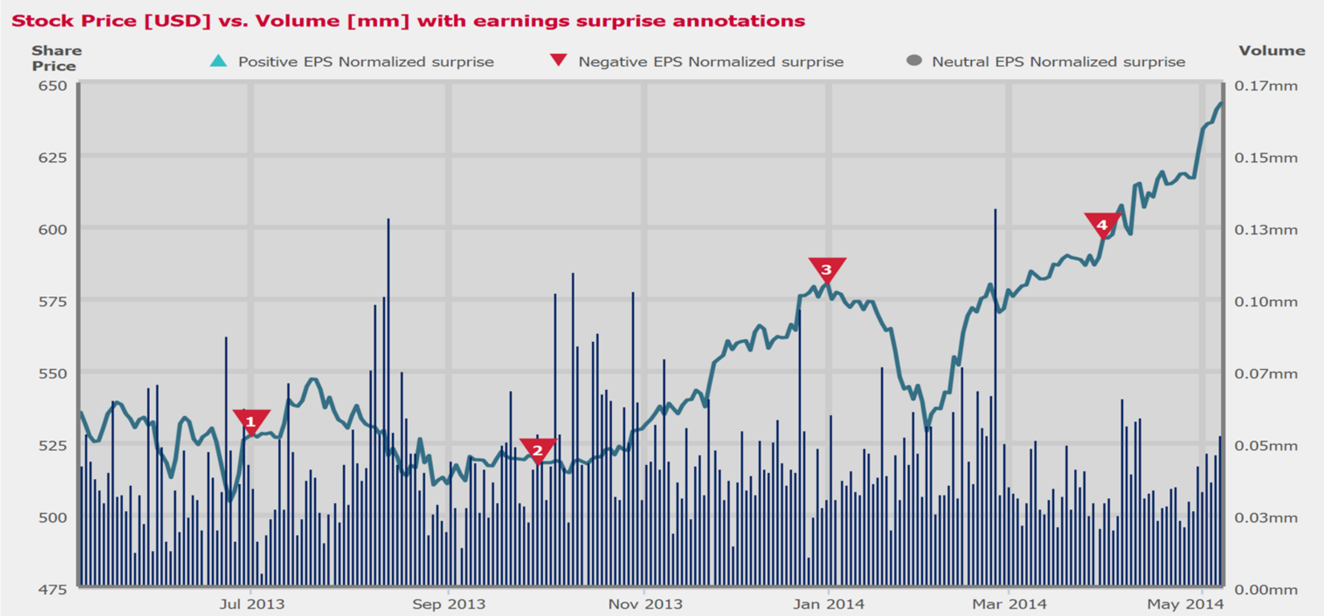
FQ2 2014 Earnings Call Transcripts

Thursday, August 07, 2014 2:30 PM GMT

S&P Capital IQ Estimates

	-FQ2 2014-			-FQ3 2014-	-FY 2014-	-FY 2015-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	5.75	2.47	(57.04 %)	5.73	22.55	25.51
Revenue (mm)	1214.94	1258.97	3.62	1251.86	4991.88	5279.81

Currency: USD
Consensus as of Aug-06-2014 11:55 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2013	5.83	5.13	1 (12.01 %)
FQ3 2013	6.14	4.67	2 (23.94 %)
FQ4 2013	5.77	5.54	3 (3.99 %)
FQ1 2014	5.74	5.32	4 (7.32 %)

Call Participants

EXECUTIVES

Anne G. Waleski
Chief Financial Officer and Executive Vice President

Richard R. Whitt
Co-Chief Executive Officer and Director

Thomas Sinnickson Gayner
Co-Chief Executive Officer and Director

ANALYSTS

Charles Gold

David McKinley West
Davenport & Company LLC

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

Robert Myers
SunTrust Robinson Humphrey, Inc., Research Division

Presentation

Operator

Greetings, and welcome to the Markel Corporation Second Quarter 2014 Earnings Conference Call. [Operator Instructions] As a reminder, this conference is being recorded. I would now like to turn the conference over to your host, Mr. Tom Gayner, President and Chief Investment Officer from Markel Corporation. Thank you. Mr. Gayner, you may begin.

Thomas Sinnickson Gayner
Co-Chief Executive Officer and Director

Thank you so much. Good morning, and welcome to the Markel Corporation second quarter conference call. We're glad that you're with us, and we look forward to discussing our results from the first half of 2014 as well as our thoughts about the business.

Joining me this morning is Anne Waleski, our Chief Financial Officer, who will review the overall financial results for the corporation. Mike Crowley is unable to be with us this morning, so my co-President, Richie Whitt, will cover all of the insurance operations. Then I'll return to discuss our investments and Markel Ventures activities.

Before we get started with the business of the call, we'll proceed with the incantation known as the Safe Harbor statement.

During our call today, we may make forward-looking statements. Additional information about factors that could cause actual results to differ materially from those projected in the forward-looking statements is included under the captions Risk Factors and Safe Harbor and Cautionary Statement in our most recent annual report on Form 10-K and quarterly reports on Form 10-Q. We may also discuss certain non-GAAP financial measures in the call today. You may find the reconciliation of GAAP to these measures in Form 10-Q.

With that, let me turn it over to Anne.

Anne G. Waleski
Chief Financial Officer and Executive Vice President

Thank you, Tom, and good morning, everyone. We had a solid first half of the year. I think the numbers speak for themselves, so I'll jump right into the results.

Our total operating revenues grew 35% to $2.5 billion in 2014 compared to $1.9 billion in the first half of 2013. The increase is due to the inclusion of 6 months of underwriting revenues from legacy Alterra product offerings in 2014, higher revenues from the Hagerty business and higher investment income due to our larger investment portfolio. Also contributing to the increase, other revenues were up 15%, $380 million from $330 million last year, primarily due to revenue growth within Markel Ventures.

Moving into the underwriting results. Gross written premiums were $2.7 billion for the first half of 2014 compared to $1.8 billion in 2013, an increase of 47% due to including 6 months of premiums from legacy Alterra products in 2014 versus 2 months of legacy Alterra premiums in 2013.

Net written premiums were $2.2 billion in the first 6 months of 2014, up 40% from the prior year, and earned premiums increased 42% to $1.9 billion for the same reasons I just mentioned.

Net retention was down in 2014 and 82% compared to 86% in 2013. The decrease, which is in line with our expectations, is primarily due to higher use of reinsurance on certain insurance products previously underwritten by Alterra.

Our consolidated combined ratio for the first 6 months was at 98% for both 2014 and 2013. However, as a reminder, the 2013 combined ratio included transactions and other acquisition-related costs of approximately $62 million or almost 5 points related to the acquisition of Alterra. The combined ratio in 2013 also included approximately $25 million or 2 points of catastrophe losses.

Excluding the impact of catastrophes and transaction and acquisition-related costs from the 2013 combined ratio, the combined ratio for 2014 increased 6 points compared to last year. The increase was primarily due to less favorable developments on prior year loss reserves in 2014 compared to 2013. Less favorable development of prior year loss reserves is primarily attributable to our U.S. Insurance segment due in part to adverse developments on our architects and engineers and brokerage excess and umbrella product lines. Additionally, prior year losses for the 6 months ended June 30, 2014, include $27 million of unfavorable development on asbestos and environmental exposures within our Other Insurance Discontinued Lines segment. There was no comparable unfavorable development during the 6 months ended June 30, 2013.

The consolidated combined ratio for the first 6 months of 2014 included approximately $167 million of favorable development from prior year loss reserves compared to $204 million of favorable development for the same period in 2013. The benefit of the favorable development on prior year loss reserves had less of an impact on the combined ratio in 2014 than in 2013 due to higher earned premium volumes in 2014.

I'll take a minute now and discuss our asbestos and environmental reserve review, which we completed in the second quarter for 2014.

Typically, we complete an annual review of asbestos and environmental exposures during the third quarter of the year unless circumstances suggest an earlier review is appropriate. This year, we've got unexpected activity on a small number of claims early in the year, which we believe warranted accelerating our annual review. During this year's review, we increased our expectation of the severity of the outcome of certain claims subject to litigation and, as a result, increased prior year loss reserves by $27 million. During our 2013 annual review, which was completed during the third quarter of last year, our expectation of the severity of the outcome of claims known at such time also increased. As a result, prior year loss reserves for asbestos and environmental exposures were increased by $28 million during the third quarter of 2013.

The need to increase asbestos and environmental losses in each of the past 3 years demonstrates that these reserves are subject to significant uncertainty and volatility resulting from an unpredictable and unfavorable legal climate.

Excluding the impacts of transaction and acquisition-related costs from 2013, the decrease in the consolidated expense ratio in the first half of 2014 was driven by higher earned premiums in each of our ongoing operating segments compared to 1 year ago.

Now I'll talk about the results of Markel Ventures. During the first 6 months of 2014, revenues for Markel Ventures were $355 million compared to $314 million 1 year ago. Net income to shareholders from Markel Ventures was just over $5 million in 2014 compared to $10.5 million for the same period in 2013. EBITDA was $35 million in 2014 compared to $40 million in 2013.

For the 6 months ended June 30, 2014, higher revenues attributable to our acquisition of Eagle Construction were partially offset by a decrease in revenues from our manufacturing operations as a result of fewer shipments and orders in the first half of 2014 compared to 2013. Net income to shareholders and EBITDA from our Markel Ventures operations decreased for the first 6 months of 2014 compared to the same period of 2013 primarily due to less favorable results in our manufacturing operations, partially offset by favorable impact from our acquisition of Eagle construction.

Turning to our investment results, investment income was $179 million for the first half of 2014 compared to $143 million in the same period last year. Net investment income for 2014 was net of $33 million in amortization expense from adjusting Alterra's fixed-maturity securities to a new amortized cost basis at the acquisition date. The benefit of holding a larger portfolio was partially offset by lower yields.

Net realized investment gains for the period were $26 million compared to $34 million 1 year ago. Included in net realized gains were $1 million of other-than-temporary impairments as compared to $4.6 million in 2013.

Looking at our total results for the year, our projected effective tax rate was 24% in the first half of 2014 as compared to 28% a year ago. The decrease in the effective tax rate in 2014 is due to anticipating a larger tax benefit related to tax-exempt investment income in 2014 as compared to 2013.

We reported net income to shareholders of $128 million in the first half of 2014 compared to $117 million 1 year ago.

Comprehensive income was $481 million for the first 6 months of 2014 compared to $109 million 1 year ago. And as a result, book value per share as of the end of June 2014 was $511.28, an increase of 7% since the end of 2013.

Finally, I'll make a couple of comments about cash flows and the balance sheet. Net cash provided by operating activities was $237 million for the first 6 months of 2014 compared to $240 million for the same period of 2013. The decrease is due to higher tax payments for our International operations, partially offset by higher cash flows from underwriting and investment activities due to the inclusion of Alterra.

With that, I'll turn it over to Richie to talk about the insurance operations.

Richard R. Whitt
Co-Chief Executive Officer and Director

[indiscernible] sales in Specialty divisions as well as certain products written by our Global Insurance division. Year-to-date gross written premiums in the U.S. Insurance segment have increased 19% over the prior year. The increase was due in large part to Alterra lines of business that are now included in this segment. Excluding these lines, premium volume is up approximately 5%, mainly driven by higher volumes from the Hagerty business, which was new in 2013, in addition to growth in our casualty, environmental and other lines, which more than offset decreases in our brokerage property writings.

The combined ratio for the first 6 months of 2014 was 98% compared to 92% in 2013. As Anne said, the increase in the segment combined ratio was driven by less favorable development on prior accident year loss reserves due in part to adverse development in the architects and engineers and on excess and umbrella lines of business. Partially offsetting this impact was the lower year-over-year expense ratio. The improvement in the expense ratio was primarily due to higher earned premiums from including the legacy Alterra product as well as the Hagerty product lines in 2014 versus 2013.

Market conditions remained competitive for the Wholesale and Specialty divisions. However, we continued to achieve rate increases during the second quarter in the 2% to 3% range, which was actually slightly up from the first quarter.

Market conditions in the Global Insurance division remained extremely challenging with rate decreases in most classes. Property business and larger -- large casualty accounts are the most competitive and are showing the largest rate decreases in our Global Insurance division.

So the Wholesale and Specialty divisions continue to work to reduce their overall producer base, allowing our underwriters and staff to focus on those producers that are giving us the best opportunities to write profitable business. In a competitive market such as this, it's important to quote our best opportunities and not spend time practice-quoting.

Moving on to International Insurance. The segment includes all direct and facultative business written in our non-U.S insurance company and comprises the insurance underwriting results of our Markel International division as well as that portion of our Global Insurance division underwriting results written on non -- on our non-U.S insurance company.

During the first half of 2014, gross written premiums in the International Insurance segment increased 20% to $653 million, and the combined ratio improved 5 points, coming in at a 93%. The increase in premium writings was primarily due to the Global Insurance division, which was created after our acquisition of Alterra and contributed 6 months of business in 2014 compared to the 2 months that were contributed in 2013. The improvement in the segment's combined ratio was driven by a 6-point improvement in the expense ratio and a lower current [ph] accident year loss ratio, partially offset by less favorable development of prior accident year loss reserve. As a reminder, last year's expense ratio for the first 6 months included approximately 3 points of cost associated with the Alterra acquisition. Additionally, the 2014 expense ratio was favorably impacted by higher earned premium from the Global Insurance line of business, which carry the lower expense ratio due to lower acquisition costs. The impact of higher earned premiums from the Global Insurance division, however, had an unfavorable impact on our current accident year loss ratio since the Global Insurance product offerings generally have a higher attritional loss ratio than other products in the International segment.

To finish up, I'd like to discuss the results of our Reinsurance segment, which includes all treaty reinsurance programs written across our company either by our Global Reinsurance division or the Markel International division.

Gross written premiums for this segment was $793 million for the first 6 months of '14, which was up from $241 million 1 year ago. The increase in premium writings was primarily due, again, to including 6 months of writings of products previously written by Alterra in 2014 compared to only 2 months of writings included in our 2013 results. The combined ratio for this segment for the first 6 months was a 97% compared to 118% last year. Last year's combined ratio included approximately 12 points of catastrophe losses, there's really no significant catastrophe losses in this year's results, and approximately 19 points of costs associated with the acquisition of Alterra. Excluding these 2 items, the increase in the segment's combined ratio in '14 is due to higher contributions of premium from products previously written by Alterra. Alterra's reinsurance portfolio included a significant portion of casualty reinsurance, while the legacy Markel portfolio was largely property reinsurance. Casualty reinsurance, by its nature, is inherently more volatile and is a long-tail product. And as such, the impact of applying Markel's more conservative loss reserving philosophy had a more significant impact on '14 compared to the '13 numbers.

Reinsurance market conditions are, without a doubt, the most challenging of any areas of the insurance marketplace. Pricing is down in most reinsurance lines of business, and this is clearly being led by property reinsurance where rates are down anywhere from 10% to 30% in some cases.

Summing up all the results of Markel's insurance operations, we had a good start to the year, a good first half of the year. Despite competitive market conditions, we believe the Markel brand, our strong balance sheet and more meaningful market position has produced and will continue to produce additional profitable underwriting opportunities for Markel. At this point, I'll turn it over to Tom.

Thomas Sinnickson Gayner
Co-Chief Executive Officer and Director

Thank you, Richie. As we've noted before, one of the great things about Markel is that we've got several methods to build the value of this company for you as our shareholders. Insurance, investments, our industrial and service businesses and capital management activities all work together to produce comprehensive income and value for you.

As is usually the case, not every cylinder in the engine of Markel will be firing at the same rate. The good news is that with our multiple cylinders, the engine keeps moving the car down the road at a pretty good rate of speed. Specifically, as Anne noted earlier, that shows up on the speedometer as comprehensive income of about $480 million-plus through the first half, an increase of 7.2% in the book value per share. The longer term and more meaningful rolling 5-year rate of return of comp annual [ph] growth rate of book value per share continues to be in the teens, and was 13% as of June 30.

During the first half of 2014, we enjoyed excellent returns in our investment activities. The total return from the portfolio was 4.6% with equity up 8.6% and fixed income up 3.5%. Both of these measurements are more than satisfactory on an absolute and relative basis, and I'd be happy to sign up for them indefinitely into the future. Sadly [ph], that option is not available, so we continue to come to work every day and make the best decisions we know how to make to produce good results going forward, as we've done for a long time, and I'm confident that our time-tested investment discipline will continue to work well for you as our shareholders.

I'm also happy to report to you that the recasting of the investment portfolio we picked up in the Alterra acquisition is largely complete. We've reset the fixed-income portfolio, largely eliminated the high-cost alternative investment activities and continued the process of building up the equity investment in keeping with our traditional investment discipline.

As of June 30, equities represented 51% of shareholders' equity, up from 48% at year-end, and we continued to methodically build the equity portfolio. We've enjoyed a roughly 700 basis point addition to our total return when we allocate money to equities compared to fixed income over the last 25 years. We'll look to continue to maximize the amount of equity exposure that we can given our comprehensive view of the state of our business, our balance sheet position and the opportunities we see [ph].

Turning to Markel Ventures. We picked up some steam in the second quarter after a slow start in the first part of the year. Revenues rose 13% from $313 million to $354 million. More importantly, our share of EBITDA from the Markel Ventures operation was $35.1 million, a decline of 13% from the $40.3 million we earned in the first half of 2013. For the second quarter, EBITDA was flat at $21 million versus $21 million 1 year ago.

As we've stated before, the manufacturing operations within our Ventures group are lumpy businesses, where big orders come irregularly and make a big difference on the bottom line. The first half of 2013 was a particularly robust period, and the first half of 2014 was a bit light. Fortunately, we picked up steam in the second quarter compared to the first, the order books are in pretty good shape and I'm optimistic about the balance of the year.

Also, I'm pleased to announce that after the quarter ended, we completed the acquisition of Cottrell, the leading manufacturer of car hauls. The initial consideration for Cottrell is $130 million, and this is the largest transaction yet for Markel Ventures.

With the addition of Cottrell, the run rate for the Markel Ventures company now rounds to $1 billion. I continue to expect double-digit EBITDA profitability from the group, and this is becoming a more meaningful contributor to the earnings and the value of Markel.

We continue to see and review a meaningful number of opportunities at Markel Ventures. We're picky about choosing our partners, and we've got the alternatives of publicly traded equity securities, privately held businesses and our own stock as daily [ph] choices for how we allocate capital.

To sum it up, those that are sitting around this table have 2 jobs. One, we've got to run our existing businesses to the best of our ability and earn good returns on the capital. Second, we've got to make good capital allocation decisions with the money we make from doing job one. I'm pleased to report that we're producing good results for you on both fronts, and we look forward to the challenge of continuing to do so. With that, we're delighted to take your questions. [indiscernible] open it up.

Question and Answer

Operator

[Operator Instructions] Our first question comes from the line of Mark Hughes from SunTrust.

Robert Myers
SunTrust Robinson Humphrey, Inc., Research Division

This is Rob Myers on for Mark Hughes. Just 2 questions. One, this dip in favorable prior year loss development we saw in the quarter. Is that kind of a blip? Or is this something we should expect to continue going forward?

Anne G. Waleski
Chief Financial Officer and Executive Vice President

Mark, I think we've said in years past that history does not dictate the future, particularly in this arena. So creating an expectation around prior year reserves based on history is not something that we've typically encouraged. That said, what we would expect for this year is something that will probably be slightly less than last year but not dramatically less. So I think some of the adverse developments that you saw this quarter, we're hoping that we have taken care of this quarter and won't repeat.

Robert Myers
SunTrust Robinson Humphrey, Inc., Research Division

Okay. That's very helpful. And then lastly, just I was wondering if you guys had an update on pricing competition, loss trends in the med now [ph] workers' comp space?

Richard R. Whitt
Co-Chief Executive Officer and Director

This is Richie, Rob. In terms of med now [ph], it's still a pretty tough market right now. Just looking at our most recent rate monitoring, we're slugging it out and getting a couple percentage points of price increase on that business, but it's incredibly competitive. In terms of workers' comp, that's probably the strongest part of the market, and I did mention that in my comments. But in workers' comp, we're sort of probably mid-single digits in terms of increases on workers' comp business. And in California, that could be significantly more depending on the class and depending on the geography in California. So those 2 markets are on the sort of the better end of the scale of where our various products are in the industry.

Operator

Our next question comes from the line of Jay Cohen from Bank of America Merrill Lynch.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

A couple of questions. I guess the first one is on the Reinsurance segment. I mean, you guys have been very up front about moving the old Alterra business on to your reserving methodology, and that puts some near-term upward pressure on loss ratio. I've seen that with past deals, so it's not surprising. I guess looking forward in that business, maybe we have 2 potential opposing forces. One is the market conditions, all else being equal, would suggest loss ratio get worse. At the same time, as you have already moved this business or at some point will have moved this businesses into your own reserving methodology, you'd expect to see some improvement down the line. My question is, do you think you can hold those margins flat? Or will the pricing dynamics kind of overwhelm whatever changes you're making on the reserve side?

Richard R. Whitt
Co-Chief Executive Officer and Director

Jay, obviously reinsurance is incredibly competitive right now. The -- and to extent we're still writing accounts, we believe the pricing supports the margins we want to produce on the business. And honestly at this point, I'm not particularly -- I'm pleased with the business we've put on to the books this year. The big question to me is, what's going to happen next year, January 1 and forward. If people are looking for price concessions next year, I'm not sure that it's there. I think this market should be, quite honestly, at the bottom as people are being disciplined about what they're doing. So I feel very good about the business we've put on the books this year. I feel good about what we believe the margins are going to be. As you know, as you say, we've been putting Markel's sort of level of conservatism and margin of safety on the reserves. So everything -- I feel good about everything this year. The unknowable is where does the market go from here. I believe we're -- as we reinsurers have given all we can give, it will be interesting to see what the competition is willing to do as we go into '15.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Let's hope we find some sort of floor. The other question I had was, regarding the comment about, I guess, culling to some extent the producer base within Wholesale and Specialty. What's the argument? I mean, should we expect, because of that action, top line growth to slow down?

Richard R. Whitt
Co-Chief Executive Officer and Director

We're always managing our producer base, and we're always trying to -- it's sort of the 80-20 rule. It's interesting. The top 20% of your producers probably give you 80% of your business. And then you've got to decide what that -- the rest of that group, do they have potential, though, to move into that other group? Or do you need to move on and spend your time elsewhere? So you're always managing your producer base. Our -- in the past, what we've seen is when we focus more on the people who truly are producing the business for us, volume goes up. We don't tend to take a step back. We tend to continue to move forward. And in fact, we're seeing -- when you back out what's happening on the property book, where pricing -- where we've had to reduce because of pricing, we're up in most of the other lines of business in Wholesale. And in the lines where we're not in some sort of pricing action, on Specialty, again we're seeing decent growth. So no, I think it's just a healthy thing that we're always doing, and I think we'll continue to see modest growth as we go forward.

Operator

Our next question comes the line of Mark Dwelle from RBC Capital Markets.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

A couple of questions. Did you have any losses that you're identifying as catastrophe losses in the quarter?

Anne G. Waleski
Chief Financial Officer and Executive Vice President

Nothing to note.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

And any even uptick at all in weather-related or non-cat losses that is worth highlighting?

Anne G. Waleski
Chief Financial Officer and Executive Vice President

Nothing at all worth highlighting.

Richard R. Whitt
Co-Chief Executive Officer and Director

Nothing at that we -- you have a threshold for a named catastrophe, Mark. And really, we did not have anything that would have hit the threshold for any of the named cats. So it was a very quiet first half of the year. Now it's not to say we didn't have some attritional losses. We certainly did. But nothing that rose to a level of significance.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

Okay. A question for Tom. It's just a -- not being able to hear and write quickly enough question. In the context of Markel Ventures, you said that something is now at a $1 billion rate or amount. What was that thing?

Thomas Sinnickson Gayner
Co-Chief Executive Officer and Director

The revenue line going forward at the -- our Markel Ventures group.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

Got it. And my last question. Now there was -- now that you've had Alterra for a full year, the amount of premium that you retained from that franchise, how does that compare relative to your very initial expectations? From my perspective, it seems like relatively more premium was retained than maybe was initially expected. But I'd be interested in your thoughts.

Richard R. Whitt
Co-Chief Executive Officer and Director

Mark, this is Richie. Yes, I'd agree with you. I would say we've retained more of the premiums than we would have expected initially. I think if you look at our 10-Q, we have a pro forma gross written premium numbers in there for the quarter and year-to-date. And I think actually in the quarter, we were ahead of that pro forma number; and for the 6 months, we were basically flat to that number, which -- some of that is growth in legacy Markel products, but I have been very pleased with the amount of premium we've held on to from the acquired products of Alterra.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

Would you say that the underlying quality of the book has been better than initial expectations? Or it's just the way the market conditions have developed allowed you to retain perhaps more than you might would have initially judged?

Richard R. Whitt
Co-Chief Executive Officer and Director

I think the quality has been about what we thought when we went into the deal. I think the most important thing in any acquisition, and I think I've said this before on the call, is being able to keep the talent, keep the people, and we have done a very nice job there. The people have stayed. And I think I contribute the success we had to the fact that the talent has stayed with us. I think the quality of the business is about what we assumed.

Thomas Sinnickson Gayner
Co-Chief Executive Officer and Director

Mark, I'd add one point to that. And that is, the marketplace acceptance of Markel, which is a bigger balance sheet that has the talent that Richie spoke of that has gone well. We didn't exactly know how to pencil and paper that going into it, but we certainly believe that the combined entity will be more attractive as an insurance partner for the world, and that's proving to be the case.

Richard R. Whitt
Co-Chief Executive Officer and Director

Yes, -- and that's a really good point that Tom makes. People like to talk about synergies in acquisitions, and we've tried to stay away from those words. But it is fair to say we've seen a number of large accounts, particularly on the Reinsurance side and in the Global Insurance side, where the Markel brand and the balance sheet strength and the relationship that Markel has throughout the industry have made a difference in terms of business coming to us. So clearly, that has happened.

Operator

[Operator Instructions] Our next question comes the line of Charles Gold from Scott & Stringfellow.

Charles Gold

Tom, I'm hoping you would go through an exercise with me and get at the back of an envelope and it's a Markel Venture question. Now that the run rate and revenue is $1 billion, looking at 2015, let's say, if the -- and also factoring in that the metrics you were looking at when you bought companies was roughly 6 to 7x EBITDA, so the assumptions I would use on the back of my envelope would be next year's revenue sans an acquisitions, $1.1 billion, that the companies we bought may not have lived up to the 6 or 7x EBITDA, so I used 8x. So I multiplied the $1.1 billion times 12.5 and get $137.5 million of EBITDA. And I bring half of that to the bottom line in net income and get just under $5 per share in earnings on an annual basis. Is that in the right ballpark? Or am I thinking incorrect?

Thomas Sinnickson Gayner
Co-Chief Executive Officer and Director

Well, if this wasn't [ph], I think I'll go home and say 2015 is done. But you're right. Your back of the envelope and thought process is directionally correct. The thing that we can't take for granted is that these things are always easier to say than they are to do, so that we have an immense amount of work to make that happen. But those sort of rough, rough back of the envelope calculations are directionally correct [indiscernible].

Operator

Our next question comes the line of Jay Cohen from Bank of America Merrill Lynch.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Yes, I guess first, just maybe a follow-up on Markel Ventures. I'm looking at just a simple calculation just the margin on the nonmanufacturing businesses. And they went down fairly dramatically from first half '13 to first half '14, and I don't know if that's a business mix issue with some of the different businesses, but I'm wondering if there's a reason why they went down so much.

Thomas Sinnickson Gayner
Co-Chief Executive Officer and Director

Right. On the nonmanufacturing margins, I don't have the numbers in front of me, but directionally what would be happening is probably the biggest swing is in our health care area. And there are 2 things going on there. One, the immense changes that are happening in the health care area have proven to be tougher challenges than what I would have expected to begin with. We're addressing them, we're making the best that we can of it. But let's just say that, that has been more of a challenge than what I expected. Secondly, within the health care, there are things that we're doing where we're funding and we have our foot on the gas to grow rather quickly, and we're expensing new offices openings and this is specifically in the realm of [ph] PartnerMD and the recurring front-end expense that we think produces wonderful returns on investment, but we are spending that money right now. And realistically, I would say it's this time next year before you'll start to see whether those initiatives are indeed bearing the fruits that we expect from them. And the bottom line, just like in the insurance business, either they will be bearing the fruits that we expect or we'll stop doing it. One or the other.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Got it. And then maybe a question on the reserves. So the adverse development in the architects and engineers book and the, okay, the excess and umbrella lines, what were some of the key underlying trends that you were seeing that drove that change? Was this a severity issue? And were there any -- so one, what were the trends? And two, were there any particular classes of business within the excess and umbrella area?

Richard R. Whitt
Co-Chief Executive Officer and Director

In terms of -- I'll start with architect. It's a relatively small line of business for us. And I think if you were to go around and look at the industry, everybody's been struggling a little bit with architect. Probably since 2008 with the credit crisis, architects and engineers got pulled into a lot of new and different ways of seeking recovery post-2008. So it's been one we've been chasing a little bit. And the bottom line is we either get it right or we're going to write a whole lot less architects -- and starting -- we don't write a whole lot to start with, but it could be a whole lot less if we don't feel like we're getting the right rate for it. On excess and umbrella, that class has been a terrific class for quite a while. We've seen a little bit of early development recently, and we've probably seen some auto losses, which is not surprising. And we tend see some heavy auto in excess and umbrella, but we've seen a little bit of auto losses and we've seen a little bit of early losses. The team, again, is on top of it, and we're making some changes to address it. And again, we either we get it straight or premium volume will decrease.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

That's great. I think you were pretty proactive in that book.

Richard R. Whitt
Co-Chief Executive Officer and Director

We try to be.

Operator

Our next question comes the line of Dave -- David West from Davenport.

David McKinley West
Davenport & Company LLC

In the other revenue, other expense tables on the insurance side, you have your MG up, MG&A operations, and then the line item life and annuity. And I thought most of the Alterra life and annuity was in discontinued operations. Can you dig down and tell me what that life and annuity line is associated with?

Anne G. Waleski
Chief Financial Officer and Executive Vice President

David, it is in discontinued, and it is related to the Alterra discontinued life and annuity book. It's just not underwriting.

Richard R. Whitt
Co-Chief Executive Officer and Director

Right. Right. And I guess on the revenue side -- I don't have the schedule in front of me. The revenue side, which is the -- some small premium adjustments, I think it's a relatively small number,

They -- that drove -- it'll be a few thousand dollars each quarter. They are always -- are constantly adjusting premiums. And then on the expense side, that's just the amortization, the accretion of the discount on those life and annuity reserves. So that will be a feature that shows up from now and for the next 50 years on a decreasing basis.

David McKinley West
Davenport & Company LLC

Right, okay. Decreasing basis, I think, or...

Richard R. Whitt
Co-Chief Executive Officer and Director

Right, right, just as that amortizes off.

Operator

There are no further questions in the queue. I'd like to hand the call back over to management for closing comments.

Thomas Sinnickson Gayner
Co-Chief Executive Officer and Director

Thank you very much. We appreciate you joining us. We look forward to chatting with you next quarter. Take care.

Operator
Ladies and gentlemen, this does conclude today's teleconference. Thank you for your participation. You may disconnect your lines at this time, and have a wonderful day.