S&P Capital IQ

CONTENTS

AXIS Capital Holdings Limited NYSE:AXS

FQ3 2009 Earnings Call Transcripts

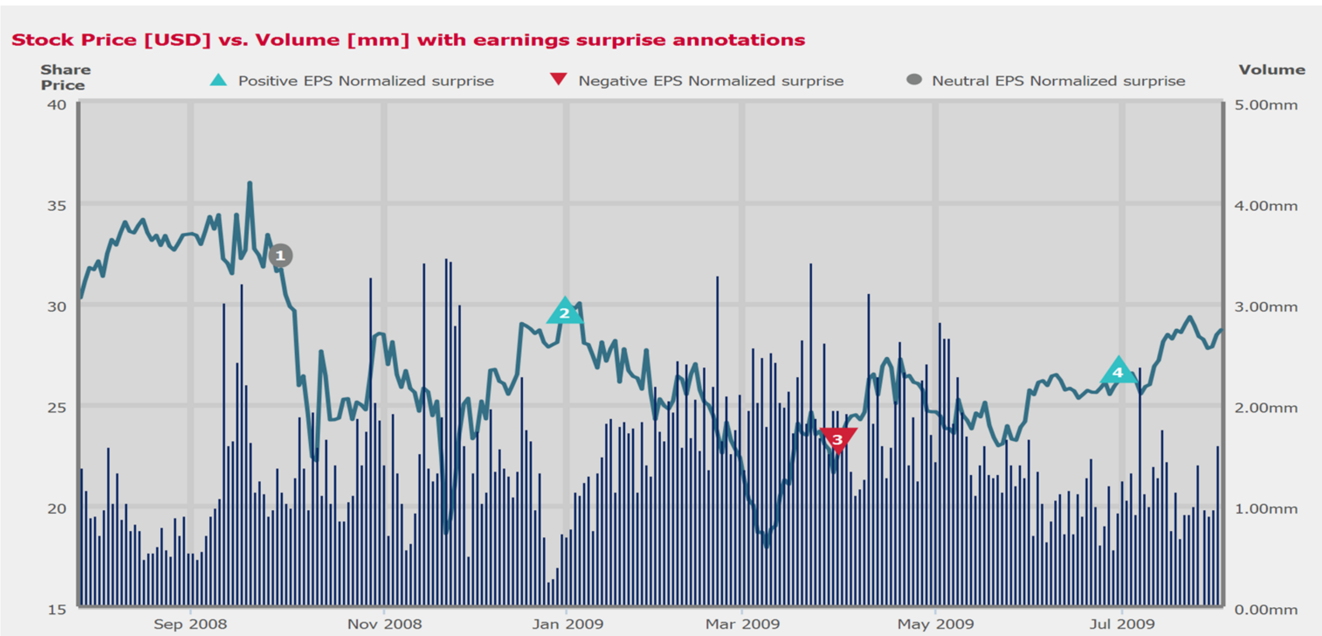
Tuesday, November 03, 2009 1:00 PM GMT

S&P Capital IQ Estimates

	-FQ3 2009-			-FQ4 2009-	-FY 2009-	-FY 2010-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.80	1.05	▲31.25	1.20	4.28	4.46
Revenue (mm)	562.50	595.14	▲5.80	339.13	2781.14	2899.56

Currency: USD

Consensus as of Nov-03-2009 12:03 PM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ3 2008	(0.97)	(1.22)	NM
FQ4 2008	0.99	1.09	▲10.10 %
FQ1 2009	1.11	1.05	▼(5.41 %)
FQ2 2009	1.17	1.22	▲4.27 %

Call Participants

EXECUTIVES

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

John R. Charman
Former Director, Chairman of Axis Re and Chairman of Axis Specialty Europe

Linda Ventresca

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Presentation

Operator

Hello and welcome to the Third Quarter 2009 AXIS Capital Holdings Ltd. Earnings Conference Call. [Operator Instructions] I would now like to turn the conference over to Linda Ventresca. Please go ahead.

Linda Ventresca

Thank you, Andrea and good morning, ladies and gentlemen. I am happy to welcome you to our conference call to discuss the financial results for AXIS Capital for the quarter ended September 30, 2009. Our earnings press release, financial supplement and quarterly investment supplement were issued yesterday evening after the market closed. If you would like copies, please visit the Investor Information section of our website, www.axiscapital.com. We set aside an hour for today's call, which is also available is as an audio webcast through the Investor Information section of our website. A replay of the teleconference will be available by dialing (877) 344-7529 in the U.S. The International number is (412) 317-0088. The conference code for both replay dial-in numbers is 434229.

With me on today's call are John Charman, our CEO and President; and David Greenfield, our CFO. Before I turn the call over to John, I'll remind everyone that statements made during this call, including the question-and-answer session, which are not historical facts may be forward-looking statements within the meaning of the U.S. Federal Securities Laws. Forward-looking statements contained in this presentation include, but are not necessarily limited to, information regarding our estimate of losses related to catastrophes, derivative contracts, policies and other loss events, general economic capital and credit market conditions, future growth prospects and financial results, evaluation of losses in loss reserves, investment strategies, investment portfolio in market performance, impact to the market place with respect to changes in pricing models and our expectations regarding pricing and other marker conditions. These statements involve risks, uncertainties and assumptions, which could cause actual results to differ materially from our expectations. For a discussion of these matters, please refer to the Risk Factor section in our most recent Form 10-K on file with the Securities and Exchange Commission. We undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

In addition, this presentation contains information regarding operating income, which is a non-GAAP financial measure within the meaning of the U.S. Federal Securities Laws. For a reconciliation of these items to the most directly comparable GAAP financial measure, please refer to our press release, which can be found on our website. With that, I'd like to turn the call over to John.

John R. Charman
Former Director, Chairman of Axis Re and Chairman of Axis Specialty Europe

Thank you, Linda and good morning to you all. I'm pleased to report that during the third quarter 2009, AXIS benefited from a very good P&C underwriting results, as well as a strong recovery in asset valuations throughout our investment portfolio. Importantly, our underwriting operations produced a combined ratio of 73.2%. While the combined ratio have benefited from a low-level catastrophes, it continues to demonstrate our strong performance for the year and the consistency of the underwriting performance through what has been so far, a very challenging phase of the underwriting cycle.

Our results are particularly strong, given the impact of the global economic crisis on a number of our important product lines over the last couple of years. Our results this quarter were adversely impacted by an increase in the fair value liability of our only insurance derivative contract. Despite this adjustment, we were still able to deliver an increase in diluted book value per share of 10% in the quarter and 22% for the year-to-date. For the third quarter, our consolidated net premiums written were up 8%, largely due to the continued success of our reinsurance segment in accessing good underwriting opportunities. At this time, the reinsurance market continues to remain the most disciplined and attractive area at the global P&C marketplace.

In our insurance segment, we have continued to maintain a very defensive posture overall. While rate improved across our insurance portfolio during the third quarter of 2009, this improvement was somewhat muted, relative to the first half of this year. As we have demonstrated in the past, when necessary, we will sacrifice top line growth to preserve underwriting profit. As we work diligently through this challenging phase of the underwriting cycle, we have continued to invest in broadening our franchises capabilities. This includes the expansion of distribution capabilities and new target markets, including global accident and health. We expect these efforts to generate significant return to the shareholders, over time.

And with that, I will turn the call over to David to discuss our financial results for the quarter, in more detail.

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

Thank you, John, and good morning, everyone. As John mentioned, we are pleased with the underlying performance of our business this quarter. As we announced a few weeks ago, this quarter's results were adversely impacted by an increase in the fair value liability for the insurance derivative contract we wrote in 2006, primarily exposed to longevity risk. Despite this adjustment, which I will cover in a more detail in a few minutes, our otherwise strong underwriting results and strong investment results enabled us to achieve an annualized operating return on average common equity for the quarter of 13% and 14.7% for the year-to-date. This, combined with the significant improvement in asset valuations across our investment portfolio contributed to the 10% increase in our diluted book value per share to $31.58 in the quarter.

Since the start of the year, diluted book value per share increased 22%. We recorded a net loss for the quarter of $96 million or $0.70 per diluted share, compared with a net loss of $249 million or $1.79 per diluted share for the third quarter of 2008. After-tax operating income, which excludes the impact of realized investment gains and losses was $152 million or $1 per diluted share, compared with an operating loss of $161 million or $1.15 per diluted share for the third quarter of 2008. The Main driver of the difference between the operating income and a net loss is the impairment charge on medium term notes recorded this quarter.

For the first nine months of 2009, net income was $179 million or $1.19 per diluted share, compared with $220 million or 1.40 per diluted share in the first nine months of 2008. After-tax operating income improved substantially to $490 million or $3.26 per diluted share, from $273 million or $1.74 per diluted share for the first nine months of 2008. Before I move on to a broader discussion of our results for the quarter, I would like to cover the operating item in our recent announcement.

During this quarter, we reported an adjustment to our only indemnity derivative contract that is exposed to longevity risk. This contract is accounted for on our fair value basis and consequently, we are required to review the valuation each quarter. The fair value is determined based on an internal model, which incorporates a number of assumptions that are inherently uncertain.

Based on a review of the valuations this quarter, we reported a negative fair value adjustment of $136 million. To provide a better understanding of the adjustment in this quarter, I will take a few minutes to review the fundamentals and history of this contract. In 2006, we were presented with an opportunity to invest in a note backed by a portfolio of life settlements. We viewed this new opportunity at that time, as also having the potential of creating a new portfolio of diversifying profitable business.

As general background, life settlement securitizations involve polling and repackaging of cash flows from a group of life insurance policies into a bond or bonds. A trust buys life insurance policies from a group of individuals and assumes the responsibility to pay the policy premiums when due and the right to receive the policy benefit when the covered individual dies. In our transaction, the purchased insurance policies were pooled and subsequently repackaged into one note. The payment of debt service on the note was linked to the projected mortality of the policy holders.

When we evaluated the original block of life policies, we simulated expected cash flows based on a range of mortality scenarios and believe we would achieve an attractive return commensurate with the risk.

This was particularly attractive, given the diversification provided relative to our other enterprise risks. The fair value of the investment was updated from quarter-to-quarter and changes in the fair value of the investment were included in other investment income.

In the quarters leading up to the September 2007, we experience volatility in the quarterly valuation due to interest rate movements and to a much lesser extent, lag in mortality experience. Given our interest in longevity exposure alone, we undertook to restructure the transaction to significantly reduce the interest rate risk we assumed and maintain longevity exposure. The transaction was restructured into an insurance policy accounted for as a derivative. Through this insurance contract, we agree to indemnify the holder of a $400 million note with a 10 year term in the event of nonpayment on the principle of its investment at maturity in 2017. The restructuring resulted in a reset of the transaction at September 2007, with fair value beginning at nil.

Since that time, the actual mortality experience has mostly lagged our expectations. As the policy was in its early stages, we generally held to our original assumptions. The change in valuation in this quarter was the result of adjustments to our original life expectancy assumptions for the lives in the pool. Until this quarter, our valuation model maintained the life expectancy assumptions in place at inception of the insurance contract. These assumptions were a function of data and information accumulated by a certain life settlement industry service providers and reviewed in conjunction with third-party life insurance actuarial support.

Because of the high debt benefits for the lives in this pool and the small population of the same pool, at that just under 200 lives, the early lag in mortality experience was not to believed to be indicative of experience that should be expected for the broader pool. Because of the persistency of this lag over the last two years, we now believe we should assign a statistical significance to the actual experience thus far, in the pool. The combination of this lagging mortality experience and recent life settlements market data indicating increased life expectancy in a much larger sample of lives, led us to reflect an increase in life expectancy in our valuation model this quarter. This is sometimes referred to as unlocking the mortality curves.

Our latest valuation announces suggest we can reasonably expect to provide an indemnity, close to $400 million in 2017, and a very high probability of providing indemnity in 2017 in excess of $300 million. The fair value of $228 million at September 30, 2009, would represent nearly a full loss to the contract with an indemnity payout, close to $400 million in 2017. Going forward, we can have further fair value adjustments upward or downward on this contract until its maturity in 2017.

If our current assumptions hold true, you would expect the valuation to move towards the ultimate expected payment over the next eight years. Of course, it is unlikely, actual experience will mirror what has been modeled and the actual adjustments will not be predictable. What I can say today is we do not expect any further significant negative adjustments. Finally, as noted in our announcement, we continue to review our legal rights and obligations and have reserved our rights under the contract.

Turning now to our top line, our consolidated gross premium is written increased 7% to $775 million for the quarter and 5% for the first nine months of 2009. Growth in gross premiums written for the quarter and the year-to-date were driven by our reinsurance segment, which increased 12% for the quarter and 16% for the year-to-date. For the quarter, growth in our reinsurance segment was 22% after adjusting for the impact of reinstatement premiums. Gross premium is written for the quarter in our reinsurance segment, which totaled $361 million, benefited from selective opportunistic expansion of our business due to market dislocations, improving and underlying primarily business and the continuing fight to quality.

Specifically, we were able to grow our property, trade credit and bond, casualty and professional liability reinsurance lines. Growth in our casualty reinsurance premiums was driven by an opportunistic cap surplus relief contract for $25 million of premium, covering a capital constraints specialty company. For the quarter, gross premiums written in our insurance segment were $414 million, up 3% from prior year quarter. The increase was driven by growth of our professional lines business, primarily emanating from new business opportunities in our D&O lines. We continue to see rate improvement in other parts of our insurance portfolio this quarter, notably our energy and property lines.

However, the impact of great improvement in our insurance portfolio was largely offset by our effort to reduce our peak zone catastrophe exposures in favor of deploying cat capacity in our reinsurance segment, where underwriting margins were much more favorable. Consolidated net premiums written increased 8% in the quarter and 6% for the year-to-date, reflecting the previously mentioned growth in gross premiums written. In line with these changes, net premiums earned increased 2% in both the quarter and the nine-month period.

Moving on to our underwriting results, total underwriting income for the quarter were $71 million, compared with an underwriting loss of $186 million in the third quarter of 2008. While this quarter represented a very light catastrophe quarter, our underwriting results for the third quarter of 2008 included net losses incurred from hurricanes Ike and Gustav of $386 million, net of related reinstatement premiums earned. The year-over-year underwriting results improved slightly when taking into account the impact of the indemnity derivative contract this year and the hurricanes last year. We believe these underwriting results are excellent, when viewed in the context of extreme competition throughout most of the primary insurance marketplace.

Our combined ratio was 73.2% this quarter, compared with 128% in the prior year quarter. Our consolidated accident year loss ratio in the quarter was 61.4%, which represented a reduction of nearly 52 points from the prior year quarter. As previously noted, the decline was primarily driven by the absence of major catastrophes this quarter. For the year-to-date, our consolidated accident year loss ratio was 66.4%, compared to a 83.3% for the first nine months of 2008. Our insurance segment's accident year loss ratio decreased nearly 33 points to 59.8% for the quarter. Our insurance segment benefited from limited catastrophe and other large loss activity of this quarter, compared to the prior year quarter, which included 39.2 points of net loss related to hurricanes Ike and Gustav.

Due to higher claims activity related to our credit and political risk point, there was some upward movement in the accident year loss ratio relative to the same period last year. This is consistent with the first two quarters of this year and in line with our expectations. Our reinsurance segment's accident year loss ratios decreased to 66 points to 62.4%, also reflecting a lower level of catastrophe activity. The third quarter of 2008 included net losses on hurricanes Ike and Gustav of 73.7 points. This reduction was partially offset by an increase in European wind storm activity, together with some crop losses this quarter. As we have seen in the last few quarters, I'll update you on the status of loss activity in reserving for our lines of business impacted by the financial crisis. Trade credit and bond reinsurance, professional lines insurance and reinsurance. And credit and political risk insurance.

Before I provide the details for the 2009 accident year, I would like to note that there was no material deterioration in the quarter for prior year reserves related to the these lines of business. We continue to monitor loss of information and default potential closely, and believe the information are showing anticipated stabilization in each of these lines, and even improvement in some areas.

We remained cautious about the outlook for the global economy and therefore, we continue to take a conservative approach in our estimates of ultimate loss. Starting with trade credit and bond reinsurance, as a general comment, loss experienced in this line continues to remained purely frequency-driven at this point. Our estimated 2009 accident year combined ratio for the trade credit and bond reinsurance line now stands at 128%. As far as earlier accident years for this line is concerned, I would like to emphasize the fact that this line has primarily short-tail characteristics, and therefore, we are comfortable that the 2007 and 2008 loss ratios are reasonably well-developed. For professional lines insurance, our estimated 2009 accident year combined ratio stands at 100% for 2009. For professional lines reinsurance, our estimated accident year combined ratios stand at 111% for 2009.

Finally, in our credit and political risk line, our estimated 2009 accident year combined ratio is 128%. Loss activity has been in line with our expectations for this year. The impact of credit political risk loss activity was approximately 11 points on the insurance segment's loss ratio and just over four points on our consolidated loss ratio. Because the average length of policies is longer in this line of business, approximately five years on average. It's important to consider not only IBNR but also unearned premium reserves. Together, these reserves are approximately $500 million at September 30, 2009.

During the quarter, our estimate of net reserves from prior accident years continued to develop favorably, with overall reserves reduced by $122 million this quarter. Of this amount, $55 million was from our insurance segment, representing a positive impact of almost 20 points on the segments loss ratio. In our reinsurance segment, we recorded $67 million in net favorable prior year reserve development, representing a positive impact of 15.6 points on the segment's loss ratio.

Approximately half of the net favorable reserve developments this quarter was generated from our short-tail lines. The balance came from our medium and long-tail lines, and largely from accident years 2004 and 2005. Our own experience continues to be become more actuarially significant in the analysis of historical accident year ultimate loss assumptions in certain of these lines. I do want to continue to emphasize that we have not released reserves for casualty lines with longer tails in any meaningful way.

Moving on to expenses, our acquisition cost ratio increased three points to 16.1% this quarter. The increase was driven by business mix changes and non-recurring adjustments to prior year Seed in Commissions. Our general and administrative expense ratio for the quarter was 13%, in line with the third quarter of 2008. I do want to remind you that we are continuing to invest in new initiatives, such as our new A&H position, and it has the potential to introduce some upward movement in this ratio in the near term.

During the quarter, we generated $442 million of positive operating cash flows. This, along with significant improvement in asset valuations contributed to a 7.5% increase in cash and investments during the quarter. We ended the quarter with $11.8 billion in cash and investment. The total return on our cash and investments portfolio for the quarter was 4.3%. This was comprised of debt-investment income of $135 million, a positive change in net unrealized gains and losses of $613 million, and net realized losses of $253 million. The investment results for the quarter were aided by the continued contraction in corporate and mortgage-backed yields spreads and the strong equity markets. Our net unrealized position across all our portfolios is now showing a gain in excess of $100 million. The total return on our cash and investments portfolio year to date is 7.5%.

Net investment income for the quarter of $135 million, represented an increase of $23 million or 20% relative to the second quarter of this year, and an increase of $84 million relative to the third quarter of 2008. Investment income from fixed maturities and cash and cash equivalence was $99 million this quarter. This compared with $103 million in the second quarter of this year and $120 million in the third quarter of 2008. The decrease, relative to the prior year quarter, primarily reflects the impact of lower short term and intermediate maturity interest rates. The primary driver of the increase in net investment income for the quarter, relative to the second quarter of this year and the third quarter of last year is the improved performance of our other investments portfolio.

As a reminder, our other investments portfolio is accounted for a fair value with the change in fair value recorded in net investment income. I emphasize this point because this presentation in income statement is not consistent amongst companies in our peer group, and differences in presentations should be carefully considered in any comparable analysis. Net investment income from other investments was $39 million in the quarter. This represented an increase of $27 million relative to the second quarter of this year and was substantially better than the loss of $66 million reported in the same period last year. The return on our other investments was 7.1% this quarter and 11.3% year to date.

During the quarter, we incurred net realized investment losses of $253 million, compared to net realized investment losses of $89 million in the prior year third quarter. Net realized investment losses for the quarter included $279 million of impairment charges, primarily comprising of $263 million from medium-term notes. While we no longer expect full recovery of the value for the MTN holdings to their original costs, we currently see value in continuing to hold these investments given their current valuations.

During the third quarter, our net unrealized position moved from an unrealized loss of $530 million to an unrealized gain of $103 million at September 30, 2009. Excluding the impact of OTTI charges on this movement, we experienced a $354 million positive valuation movement on our investment portfolio this quarter. This was primarily due to tightening of credit spreads on corporate debt and non-agency mortgage-backed securities. And to a lesser extent, improved equity market performance.

In the first nine months of 2009, we reduced our holdings in U.S. agency residential mortgage-backed securities in favor of Investment Grade Corporate Debt, and to a lesser extent, U.S. Treasury and agency debt securities. These changes reduced extension risk, while taking advantage of attractive valuations in the corporate bond market. This rotation of corporate is largely complete and given current spreads unlikely to increase significantly from current waitings. We are maintaining relatively low cash reserve balances given current and projected money market rates and expect to continue to redeploy cash in the short duration, high-quality liquid investments with higher yields. We believe we are better positioned for the increase in interest rates we expect over a longer period.

At September 30, 2009, we held cash and cash equivalent balances of $1.2 billion or 10% of total cash and investments. Our fixed maturity investment portfolio, which represents 82% of total cash and investments is well diversified, with a weighted average credit quality of AA+ at quarter end, and an average duration of 2.8 years. Our other investments represents 5% of our cash and investments portfolio at September 30, 2009. We are maintaining our limited exposures to alternatives and loan-only equity strategies, and are monitoring opportunities to carefully increase our exposure to these areas.

With respect to foreign exchange, during the quarter, changes in exchange rates and changes in net currency exposure resulted in foreign exchange losses of $7 million, compared to a gain of $8 million in the prior year quarter. However, from a book-value perspective, these losses were more than offset by the currency-related depreciations of our available-for-sale investments, which is recorded in other comprehensive income.

Total capitalization at September 30, 2009 was $5.9 billion, including $500 million of long-term debt and $500 million of preferred equity. Common shareholder's equity increased $489 million to $4.9 billion during the quarter. Our financial flexibility is very strong, with debt-to-total capital at 8.5%, debt and preferred to total capital at 16.9%, and total capital well in excess of rating agency requirements. We remained strongly capitalized for the risks we hold and the risks we are targeting, and continue to prioritize deployment of capital in underwriting opportunities.

We have accreted significant capital this year through our strong underwriting results and recovery of the financial markets, and are in the midst of our planning process for 2010. Naturally, as part of that process, we will review our capital levels. As a reminder, we currently have $212 million remaining in our share buyback authorization. If we feel that returning capital is in the best interest of shareholders, we believe share repurchase could be attractive given current valuations.

Critical to our business is the clear understanding that AXIS is a reliable and financially secure partner of our clients. We have decided therefore, to increase transparency related to major areas of risk at the company with the intention of supporting client's efforts to assess our security. Earlier this year, we began providing quarterly updates with respect to catastrophe aggregates of the company, which represent our greatest risk of shop loss. In our quarterly financial supplement, we have updated information with respect to our group PMLs and associated estimates of industry losses as of October 1 at various return periods.

We remained within our tolerance levels for these risks. The European wind aggregate have increased due to inclusion of additional non-model losses related primarily to our offshore energy insurance business. These exposures are not included in the third-party proprietary catastrophe models, yet we believe that they should be taken into account when assessing our group-wide catastrophe aggregates. We adopt a similar approach across all of our catastrophe business to create a more informed view of the risk.

In this quarter, for the first time, we have provided comprehensive disclosures of our 2008 global loss development triangles, which correspond to 100% of our reserves and include information from 2002 through the end of 2008. As you know, under reserving has been a major factor and insolvencies in our industry, and we believe our consistent conservative reserving policies and practices, demonstrate a healthy respect that we have for reserving risk. We believe this new disclosure, which we expect to update on an annual basis provides excellent insight into the reserving classes presented for both our clients and investors. With that, I'd like to now turn the call back to John.

John R. Charman
Former Director, Chairman of Axis Re and Chairman of Axis Specialty Europe

Thank you, David, I think he's pretty done now. I would like to start my commentary with the discussion of two operational items. First, unless we have discussed regularly over the last several quarters, the past two years have presented understandable stresses to the credit exposed underwriting areas at AXIS.

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Thank you, David. I would like to start my commentary with the discussion of two operational items. First, and as we have discussed regularly over the last several quarters, the past two years have presented understandable stresses to the credit exposed underwriting areas at AXIS. We view this period as a welcome test not unlike those we have faced time and time again in our catastrophe-exposed lines of business. Our performance continues to be very good when measured against the scale of the global financial crisis. Our emphasis on underwriting emerging market, Political and Credit business was the appropriate one.

We continue to believe that our Credit-exposed businesses, offer significant profitability over an economic cycle. Secondly, our experience with our any life settlements transaction was a direct result of a significant and unexpected shift in life expectancies. As background, an investment opportunity was presented to us in 2006. And the fundamentals of success with respect to this investment needed to be determined by our evaluation of longevity exposure for a group of elderly individuals.

As part of this evaluation, we delivered our underwriting resources and supplemented this with contracted traditional life industry third-party actuarial support. Of course, since the time we took on this transaction into 2006, we've been monitoring and evaluating the exposure very closely. Our restructuring of the transaction in September 2007 as described by David, capped our downside and we are now in a position to put this behind us.

We are in the risk business. And losses must be accepted or sometime or another in the various lines of business that we underwrite. They usually don't all happen at the same time, though. But when the few of them do converge, we believe we are still well-positioned to deliver a meaningful return to shareholders that we have just demonstrated.

For the first nine months of 2009, we have earned an annualized operating return on average common equity just short of 15%, which is still a great outcome, considering the stresses faced by various parts of our business. Now, let us move on to more positive areas of our business contributing to this return.

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For the insurance segment, the story for the most part is one of stabilization relative to the prior quarter, but remains unsatisfactory on the whole because of the overall state of the marketplace. Rate change is still largely positive across our insurance portfolio, but rate changes stalled and in some cases weakened in some product lines this quarter, relative to the first two quarters of this year. However, this combined with loss costs better than original expectations and stabled terms and conditions still translates to good levels of underwriting profitability.

I have said for sometime now that the market cannot continue to erode primary pricing in the way it is. As a general comment, large accounts remain the most competitive across the board. Also, opportunistic business has been slowing. Property rates have been influxed due to the introduction of updated assumptions with respect to North American earthquake related loss in the industry CAT models. We have characteristically cautious about models and significant model change. And therefore, remained conservative with our Californian earthquake exposures.

Further, that AXIS because of primary industry pricing deficiencies, we have de-risk US wind exposure in our insurance segment. In the Aviation business, third quarter renewals did see a positive great movement, although not as high as warranted. And we expect this trend to continue through the fourth quarter. The oversupply of unprofessional, naive capacity in the aviation market is slowing the recovery of pricing. In professional lines, the market for non-financial institutions, commercial business remains competitive. An increase is a security concerns around certain market participants have abated.

Traditional D&O inside an DIC remained highly competitive with newer markets quoting aggressively to win business. The Financial Institution business, rate increases half for the most part, stabilize at attractive levels. The most competitive area remains Casualty Insurance business. Reductions in exposure due to the current economic conditions is resulting in a fewer new business opportunities and lower available renewal premium. This effect is compounded by the competitive pressures around this weakened premium base. We have been extremely defensive in casualty insurance lines for some time, but premium levels tracking well below the peak level in 2005.

Overall, rate in the reinsurance lines we target is at a minimum stable, and in the best cases, increasing meaningfully. As David noted earlier, business flowed to our reinsurance segment has been increasing steadily and we continue to bind good opportunities with quality savings. We continue to directly benefit from the concerns over the financial strength of distressed reinsurers or dislocation in the wake of our competitors' de-risking activities. We expect the reinsurance market to remain disciplined and positive as we enter 2010. And our earlier indications from the various industry forums in the last week support stability and consistency.

Also, the January 1 renewal date will be our first major renewal date for our Continental European reinsurance business with the A-plus financial strength rating from S&P in hand. And we expect this will enhance our position as an even more desirable counterparty. Some of the strongest areas in the reinsurance market will be those affected by dislocation or loss activity. Such as trade credit reinsurance business and financial institutions exposed professional liability reinsurance, as well as Catastrophe Exposed business.

Starting with Catastrophe Exposed business, rate reductions for North American earthquake exposure should be roughly in line with exposure reductions indicated by changes in two of the major catastrophe vendor models. This should result to the minimum and expected margins in line with our expectations. We believe the market dynamics around U.S. wind, support stable margins going into 2010. These factors include stable to increasing demand for wind coverage. Also, the depopulation of larger Florida insurance companies. The increased fertility of Florida wind-exposed companies due to inadequate capital in premium for attritional losses and the Florida Hurricane Catastrophe Fund pushing limit into the private reinsurance market.

In Europe, a few CAT-exposed placements have been biased downward, but wind margin has remained stable. While proportional property business is suffering from rate decline in underlying primary business, our limited proportional property reinsurance account has a strong catastrophe bias and therefore, is holding up well. For Property Risk Renewal business, we expect higher attachment points and pricing as the reinsurance market has been exposed to relatively high frequency experience over the last couple of years, in both the U.S. and Europe.

For the U.S. casualty reinsurance market, the July 1 renewal period showed modest improvement in the reinsurance terms. Reinsurance rates and terms were hardest for professional liability reinsurance business with the financial institutions exposed component was up significantly.

I have said before that it is blindingly obvious that pricing needs affirm across most parts of the primary marketplace. Investment income potential is at all-time blows and loss costs a poise to increase as they remained at relatively benign levels and a number of lines over the last several years. The insurance industry has continuously sacrifice underwriting margins over the last three years, but importantly, the reinsurance industry has not subsidize this margin erosion. Also compounding this issue, is the introduction of explicit government support to a certain industry balance sheet where those parties should have been allowed to fail. The dramatic improvement in the capital market has also bailed out substandard businesses.

Absent to global industry catalyst, we're not at all optimistic about a meaningful hardening of the markets. We believe that stabilization of these pricing levels is just not appropriate, given the amount and severity of risk that is being retained. Our greatest potential against an even greater challenging backdrop is to continue to use our well-placed business structure to exploit opportunity wherever and whenever it arises, that is the most capable survival and prosper. As always, our focus will be on underwriting discipline and margin preservation, which often comes with the sacrifice of some growth. We believe we have demonstrated ample willingness and ability to do this.

In addition, we continue to seek opportunities in areas less correlated to the most cyclical parts of our P&C business. We have in fact, invested significantly over the last couple of years in attractive areas including global accident and health, and small specialty commercial business. These are areas with the lead-in time but ultimately, we expect significant returns to shareholders from these initiatives.
In summary, we are confident in the strength of our balance sheet. And the success we have had positioning ourselves to be the beneficiary of any market opportunities that may arise. Thank you and we are ready to open the line for questions.

Question and Answer

Operator

[Operator Instructions] Our first question is from Vinay Misquith of Credit Suisse.

Vinay Gerard Misquith
Crédit Suisse AG, Research Division

On the Credit Insurance and the Political Risk business, thanks for your update. Could you give us a sense for what trend you're seeing in terms of the claim? And since we've seen a stabilization in the credit markets, should we see a lower impact on the loss ratio next year? This year, I believe, it was 11 points on the insurance and four points on the consolidated. So should we see a lower impact next year?

John R. Charman
Former Director, Chairman of Axis Re and Chairman of Axis Specialty Europe

Well, I think that we said, Vinay, that we believe that stabilization has impacted our portfolio fortunately, which we expected. And I have said, well, really over the last year to 18 months, that the years that would be affected were 2007, 2008 and hopefully, with 2009 that would be the end of it and we would return to a much more stabilized pattern of losses. So I'm pretty comfortable with what I said in the last quarter and the quarter before that and the quarter before that about the outlook for this line of business. I didn't think it is quite the plague that some people think it is, but I'm as comfortable today as where we were in terms of the level of our reserves and the loss activity we've experienced.

Vinay Gerard Misquith
Crédit Suisse AG, Research Division

So what is the normalized combined ratio that you would normally arrive this business to that we could maybe expect in the next few years?

John R. Charman
Former Director, Chairman of Axis Re and Chairman of Axis Specialty Europe

As I've said to you before, Vinay, many times, I don't expect a significant amount of loss ratio from this underlying business in normalized years. I won't go back how far I've been writing this business but if you look at AXIS from 2002 through to 2007, there was hardly any loss activity at all in those years. As the economic crisis started to develop naturally, we saw a loss activity increasing in 2007 through 2008 and peaking into 2009. And as liquidity has increased globally and as the global crisis has abated, we have seen a dramatic impact on the portfolio. So we don't expect a lot of lost activity during normalized years.

Vinay Gerard Misquith
Crédit Suisse AG, Research Division

Second question, a more basic question, on capital management, I was curious as to what your views are for next year.

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

Well, I think I would just remind you the comments I made earlier, Vinay. I mean, we do have an authorization available to us of about $212 million where we find the opportunities aren't in the markets in terms of growing our business. We might deplore our capital in terms of repurchasing shares, obviously. We think that's the most effective way to manage our capital as I said. In terms of 2010, I'm not going to comment on our plan for '10 at this point.

Vinay Gerard Misquith
Crédit Suisse AG, Research Division

Just because of the destock trading in 91% of book, it seems that the more attractive opportunities when this market will be repurchasing stocks. I think that right now with pricing not improving, I was hoping that you would maybe be more willing to buy like you're stuck at these levels.

John R. Charman
Former Director, Chairman of Axis Re and Chairman of Axis Specialty Europe

That's certainly going to weigh heavily on our minds than...

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

Yes, I wouldn't take away that we're not willing. I think you have to go back to the comments I made.

Operator

Our next question comes from Brian Meredith of UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

First, on the structure settlement loss going forward, if everything kind of remains stable here, does that mean we should see about an $8 million hit from that contract per quarter up through 2007 change?

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

No, that wouldn't be correct. A couple of things, and I already went through quite a lot in the prepared remarks, but it's a fair value accounted for contract. So it's not a discounted valuation model. It's fair value. So you can't just normalize and amortize the number to date to the 400 in the future. Secondly, the amount of loss that we have recorded to is not a full loss on the contract. It's nearly a full loss but not a full loss. And we wouldn't amortize to a full loss unless we viewed changes in the underlying assumptions. Having put all that aside for a moment and I know a lot of you were trying to figure out what might happen in the future, if you think about your discounting models, all else being the same and no change in our view on the loss and our markets moving in a very straight line of fashion, you'd get a much smaller adjustment on a quarter-to-quarter basis. But again, that's not the way we're going to account for it, we're accounting for in a fair value basis.

Brian Robert Meredith
UBS Investment Bank, Research Division

And then second, John, your alternative investment strategy, obviously, things have improved nicely the last couple of quarters. And I guess, given the volatility we've seen in the alternate investment strategy, what is your kind of thoughts on that going forward? I mean, you've got enough volatility in the liability side. Do you really need the volatility in the asset side?

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

Brian, I think on the alternatives, I mean there are small portion of our overall portfolio roughly about 5%. We do monitor it very, very closely and carefully. We do believe that investments we're holding are appropriate for our overall company and as I said in my remarks earlier, we will continue to look at opportunities there if we think that they make sense relative to our overall company's exposures.

John R. Charman
Former Director, Chairman of Axis Re and Chairman of Axis Specialty Europe

But Brian, you're on the right track in terms of the fact that we take risk on the liability side. And we want to make sure that whatever risk we're taking on the asset side is acceptable in the light about the totality of that balance sheet. And I do not want to go through another year like last year and this year if that gives you an indication.

Operator

[Operator Instructions] Our next question comes from Ian Gutterman of Adage Capital.

Ian Gutterman
Adage Capital

I want to follow-up, I guess, on Brian's question on the settlement. If I'm just doing some quick math here, if you're recognizing the liability at 228 and if that's being discounted from something in the high three hundreds, I'm getting about a 7% discount rate. A, is that right? And B, why is it so high given that interest rates are so low today?

John R. Charman
Former Director, Chairman of Axis Re and Chairman of Axis Specialty Europe

Well, Ian, a couple of things. I'm trying to go at pains to say this is not a discounted cash flow model, it's a valuation model. Your numbers are not off by much, but I don't think you would discount a long-term liability like that, an eight-year liability based on today's spot rate. So even though interest rates are low today, that doesn't mean that will be the rate for the next eight years.

Ian Gutterman
Adage Capital

I guess, what I am wondering, if rates stay low for a while, is there a chance you're going to have to take that discount rate down over time and that could, what I am calling a discount rate? If that could lead in a given quarter, maybe it gets marked up by more than we get expected because if rates stay low?

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

Sure, a persistent low-rate environment has all kinds of problems for the industry, not only this contract. But the one thing you're probably also keeping out of the equation is that we do have inflows on this contract as well, future premiums that are expected to be received and probably not model.

Ian Gutterman
Adage Capital

And so from now until maturity then, is that sort of $150 million to $175 million difference between where it works more currently in the limit that's going to show up in the income statement overtime, it's just a matter of how much was up each quarter depending on where the underlying assumptions are? Is that fair? But the whole amount will show up over time, it's just a matter of what the timing is.

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

That's correct, assuming that the assumptions, the conservative assumptions that we've now move to hold up and the actual performance meet. As I said in my remarks, if the actual performance actually meets what we've modeled today, which is likely not to be the case, then your theory is correct.

Operator

[Operator Instructions] We have Mr. Gutterman back on the line.

Ian Gutterman
Adage Capital

On the medium-term notes, I'm showing in the investment supplement that you have an amortized cost now of $361 million, much I assume is what it was written down to. Can you tell me what par is?

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

They're $625 million. I think it was the original par.

Ian Gutterman
Adage Capital

And what's the risk? How much concern should I have that the $361 million might need to get written down further in the future?

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

Well, I mean, I can't -- as we were just talking, we can't predict where are rates and everything are going to go in the future. But that's based on today's market. So we've seen quite a lot of activity in the last several months and spreads coming in and interest rates staying very, very low. So I can't tell you we won't have any further deterioration in the price there, but I got to believe it's highly unlikely that we'll see much given what...

John R. Charman
Former Director, Chairman of Axis Re and Chairman of Axis Specialty Europe

Well, the default rates haven't moved to the extent that they've been modeled in so...

Ian Gutterman
Adage Capital

And then my last one, David, I am looking at the, this is, I guess, Page 15 of the financial supplement, you show your top financial holdings and you break it up by government guarantee and non-government guarantee. And I look at things like BVA or city where most of it is non-government guaranteed and then you also show somewhere else that those are essentially at par right now. I guess I'm wondering for institutions that aren't necessarily in a greater shape and you don't have a government guarantee on most of the debt and they're trading you to par, why would you keep holding those at this point? Or at least reduce some that are not such a large part of the portfolio?

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

I mean, those investments are mainly at the very high level, very senior debt levels. So we think that they provide good potential or a good profit for the portfolio. And I think that they're withholding. That's our current view anyway.

Ian Gutterman
Adage Capital

And you don't worry about concentrations? Just you have a lot of -- I don't know any individual positions are likely to add up where you are and sort of too big to fail [ph] (1:01:32) banks, it becomes a meaningful position.

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

Yes, I mean, we do look at that in terms of our overall risk management, and I would say no, we're not that concerned about that concentration at this point.

Operator

Our next question comes from Steven Labbe of Langen McAlenney.

Steven R. Labbe
Langen McAlenney

Recognizing that the absolute numbers aren't large, can you elaborate on the lines of business you are riding in the liability insurance and liability reinsurance segment where you had premium increases this quarter?

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

I'm pleased that you explained it in the way that you did because we have historically, I've been very consistent in our approach to casualty business in both the insurance markets and the reinsurance markets, and just to put some color around our current casualty writings, which are -- if you take out professional lines, the peak casualty writings we had were in 2005, which was just over $285 million. Just to give you a flavor for year-to-date, we're just under $160 million. So we're averaging around about $50 million, third quarter in our casualty business. And this quarter's increase was really due to some MGAs coming on line. It was nothing special about it. We've remained extremely conservative about the casualty lines. It is heavily reinsured. We approach it with caution and we will continue to approach it with caution. On our reinsurance segment, again excluding professional lines, we're excess underwriters, don't forget. And again, we have been very cautious in our approach. We look very carefully at Cedense [ph] (1:03:39). We audit their underwriting, we audit their claims. And the reinsurance portfolio was affected this quarter by one of opportunistic reinsurance contract, as David mentioned, which was at $25 million. There was nothing to read into at all this quarter, the increase in the liability premiums.

Operator

This does concludes today's question-and-answer session. At this time, I'd like to turn the conference back over to management for any closing remarks.

John R. Charman
Former Director, Chairman of Axis Re and Chairman of Axis Specialty Europe

I would just like to thank you all for taking the time to listen in to us today and I look forward to addressing you with the fourth quarter results. Thank you all.

David B. Greenfield
Former Chief Financial Officer and Executive Vice President

Thank you.

Operator
The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.