

# Everest Re Group, Ltd. NYSE:RE

## FQ1 2015 Earnings Call Transcripts

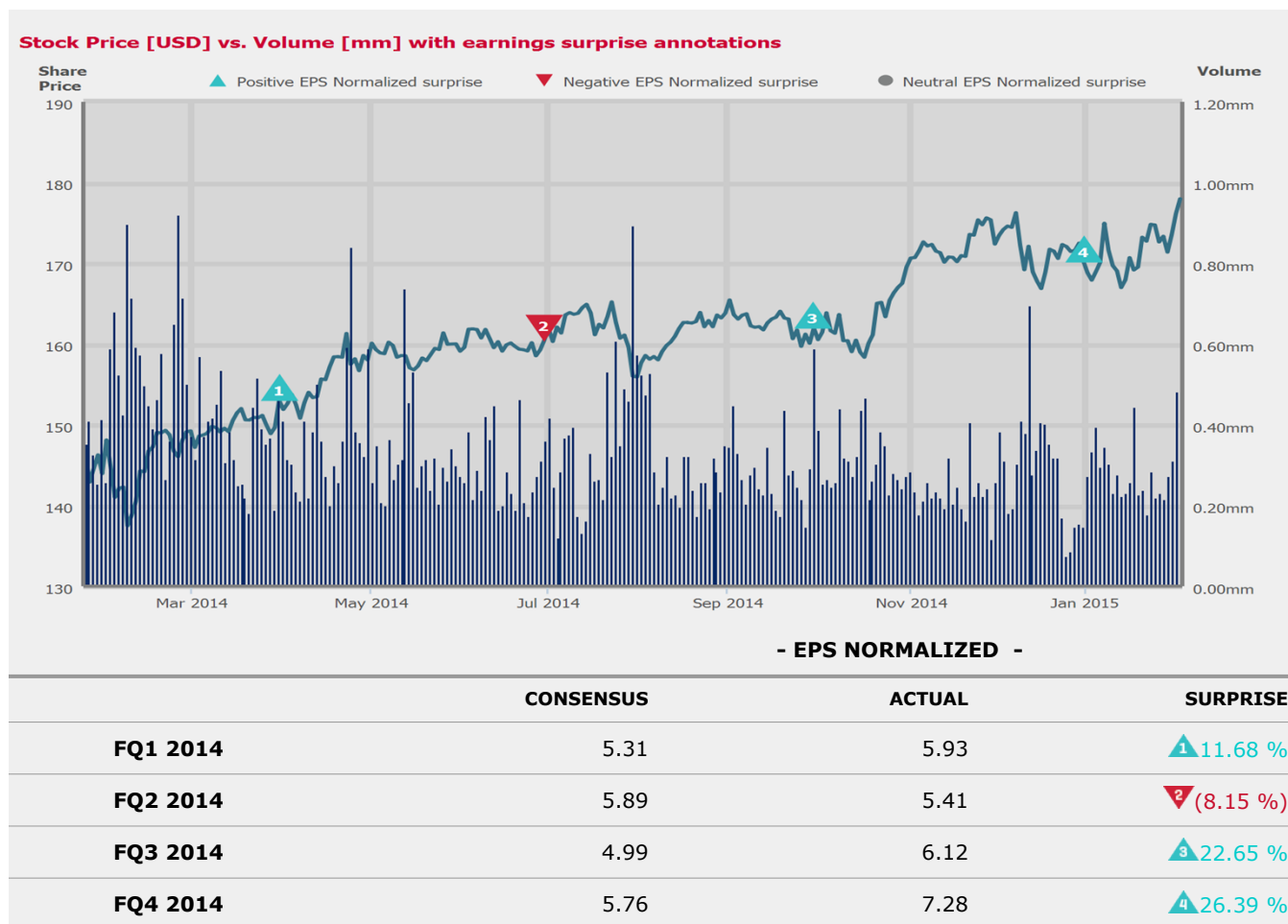
Tuesday, April 28, 2015 2:30 PM GMT

### S&P Capital IQ Estimates

	-FQ1 2015-			-FQ2 2015-	-FY 2015-	-FY 2016-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
<b>EPS Normalized</b>	5.86	7.34	▲25.26	5.13	19.86	19.84
<b>Revenue (mm)</b>	1248.10	-	▲2.87	1247.05	5370.30	5521.67

Currency: USD

Consensus as of Apr-28-2015 3:00 PM GMT



# Call Participants

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## EXECUTIVES

**Craig W. Howie**

*Chief Financial Officer and  
Executive Vice President*

**Dominic James Addesso**

*Chief Executive Officer, President  
and Non-Independent Director*

**Elizabeth B. Farrell**

*Vice President of Investor  
Relations*

**John P. Doucette**

*CEO & President of the  
Reinsurance Division*

## ANALYSTS

**Amit Kumar**

*Macquarie Research*

**Brian Robert Meredith**

*UBS Investment Bank, Research  
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**Joshua David Shanker**

*Deutsche Bank AG, Research  
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**Kai Pan**

*Morgan Stanley, Research Division*

**Meyer Shields**

*Keefe, Bruyette, & Woods, Inc.,  
Research Division*

**Michael Steven Nannizzi**

*Goldman Sachs Group Inc.,  
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# Presentation

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## Operator

Good day, everyone, and welcome to the First Quarter 2015 Earnings Call of Everest Re Group, Ltd. Today's conference is being recorded.

At this time, for opening remarks and introductions, I'd like to turn the conference over to Ms. Beth Farrell, Vice President of Investor Relations. Please go ahead.

## Elizabeth B. Farrell

*Vice President of Investor Relations*

Thank you, Jim. Good morning, and welcome to Everest Re Group's First Quarter 2015 Earnings Conference Call. On the call with me today are Dom Addesso, the company's President and Chief Executive Officer; John Doucette, our Chief Underwriting Officer; and Craig Howie, our Chief Financial Officer.

Before we begin, I will preface our comments by noting that our SEC filings include extensive disclosures with respect to forward-looking statements. In that regard, I note that statements made during today's call, which are forward-looking in nature, such as statements about projections, estimates, expectations and the like, are subject to various risks. As you know, actual results could differ materially from current projections or expectations. Our SEC filings have a full listing of the risks that investors should consider in connection with such statements.

Now let me turn the call over to Dom.

## Dominic James Addesso

*Chief Executive Officer, President and Non-Independent Director*

Thanks, Beth, and good morning to all. We are pleased to report another excellent quarter, in fact, a record quarter in operating earnings as a result of a strong underwriting result.

All segments of our business contributed positive margin in the underwriting account. Quarter-over-quarter, underwriting income was up slightly, even though the combined ratio slipped to 81.9% from 80%. This was a result of higher earned premium in this year's first quarter compared to last. The increase in the combined ratio was solely in the Reinsurance segment, where competitive conditions are continuing to push rate slower and commissions higher.

Nevertheless, we have maintained our margins with our strategies of: first, moving our capacity to better-priced layers; two, diversifying our exposure; three, expanding capabilities in new lines of business; four, using capital market outlets; and finally, maintaining an extremely competitive expense structure.

Offsetting the increase in the reinsurance combined ratio was an improvement of over 2 points in the insurance combined ratio. This is due in part to a primary rate environment, while stable overall is increasing in certain classes.

A more significant factor in this improvement has been the success of efforts over the last couple of years to wind down portions of the portfolio and reshape the insurance operation.

To build that out of new classes of business, along with expanding certain others, is beginning to pay dividends as growth quarter-over-quarter was 48%, reaching \$340 million in 2015.

We still have much more to do in this segment, and we have bolstered our management and underwriting ranks so that we may continue to progress. In addition, we have embarked on a process to begin to build out our international insurance presence.

Overall, while operating income was positively impacted by underwriting results, there were other factors contributing to the record results for the quarter. Foreign exchange negatively impacted our premiums

written, but it had a positive impact on earnings as our foreign currency denominated liabilities, or loss reserves, were converted to the stronger U.S. dollar.

Also, as Craig will explain, income taxes quarter-over-quarter were lower by \$12 million. Investment income quarter-over-quarter was flat. But given where current yields are, we believe that to be a reasonable result and certainly not unexpected.

Looking forward, the market will remain challenging as competitive pressures persist. Market movements are difficult to predict, and therefore, we rely on our flexibility to respond accordingly and modify our tactics as appropriate.

These include, as I mentioned previously, nimbly shifting our capacity, seeking new business opportunities using third-party capital, buying in stock and staying expense-conscious.

As a result, we have been able to maintain a strong ROE, which at 18% is at a meaningful spread to the market. Consequently, we are uniquely well-positioned to manage through market weakness, and therefore, maintain returns above our cost of capital, while others may not.

Market turn would seem inevitable should it drift down to this level. Until then, we will maintain our competitive position and continue to be identified by clients, brokers and analysts as a core lead market reinsurer and meaningful trading partner. In fact, one rating agency recently cited Everest as 1 of 4 reinsurers best positioned to succeed despite the prevailing market conditions.

This attribute is one that has been earned over the last several years as we have evolved our culture and the portfolio.

New capital and operating income, as a result of intelligent underwriting by our teams, has built our capital base to a size where we can deploy meaningful capacity. At the same time, while building towards \$7.7 billion of equity, plus third-party capital of \$1.7 billion, we have returned \$3.5 billion of capital to shareholders since 2006. This is a record we are proud of, and one that deserves the market's attention.

Thank you. And now to Craig for the financial report.

### **Craig W. Howie**

*Chief Financial Officer and Executive Vice President*

Thank you, Dom, and good morning, everyone. Everest had another strong quarter of earnings, with aftertax operating income of \$330 million or \$7.34 per diluted common share for the first quarter of 2015. This compares to operating income of \$281 million or \$5.93 per share for the first quarter of 2014.

Net income for the first quarter was \$323 million or \$7.19 per diluted share compared to \$294 million or \$6.21 per share in 2014. Net income includes realized capital gains or losses, and represents an annualized return on equity of 18%.

Solid underwriting results, sizable foreign exchange gains and a lower income tax rate relative to the first quarter of 2014 contributed to these strong results. All segments reported underwriting gains for the quarter. Neither this year nor last year included any catastrophe losses in the first quarter.

Total Reinsurance reported an underwriting gain of \$205 million for the quarter compared to a \$215 million underwriting gain last year.

The Insurance segment reported an underwriting gain of \$11 million for the quarter compared to an underwriting gain of \$4 million last year. Each year reflected an underwriting loss for crop insurance in the first quarter due to the seasonality of crop premium against the full quarter of expenses.

And Mt. Logan Re segment reported a \$21 million underwriting gain compared to a \$10 million underwriting gain in the first quarter of 2014. Everest retained \$5 million of income, and \$16 million was attributable to the noncontrolling interest of this entity in 2015. The overall underwriting gain for the group was \$237 million for the quarter compared to an underwriting gain of \$228 million in the same period last year.

Our reported combined ratio was 81.9% for the quarter compared to 80% in 2014. The overall current-year attritional combined ratio of 82% was up from 80.4% at the first quarter of 2014, but equal to the 82% at year-end 2014. This measure excludes the impact of catastrophes, reinstatement premiums and prior period loss development.

The first quarter commission ratio of 22% was slightly up from 21.5% in the first quarter of 2014, but remain stable compared to year-end 2014. Our lower expense ratio of 4.6% continues to be a major competitive advantage for Everest.

On reserves, our overall quarterly internal reserving metrics remain favorable. For investments, pretax investment income was \$123 million for the quarter on our \$17.8 billion investment portfolio. The investment income was essentially flat compared to 1 year ago. Despite the declining rates, our investment portfolio continues to perform well. The pretax yield on the overall portfolio was 2.9%, with a duration of just under 3 years.

The quarter reflected \$7 million of net aftertax realized capital losses compared to \$13 million of capital gains last year. These losses were mainly attributable to impairments on the fixed-income portfolio in 2015.

Foreign exchange is reported in other income. For the first quarter of 2015, foreign exchange gains were \$47 million compared to \$2 million of foreign exchange losses in the first quarter of 2014. This reflects the strengthening of the U.S. dollar compared to other world currencies, and equates to about \$1 per share this quarter.

There were \$200,000 of derivative losses during the first quarter compared to \$2 million of derivative losses last year. This is related to our equity put options and is mostly a function of the change in interest rates during the first quarter.

On income taxes, the 12% effective tax rate on operating income is on the lower end of our expected range for the year. The low rate is primarily related to foreign exchange, the geographic region where the income was earned and higher foreign tax credits.

Stable cash flow continues, with operating cash flows of \$455 million for the quarter compared to \$367 million in the first quarter of 2014.

Shareholders' equity for the group was \$7.7 billion at the end of the first quarter, up \$216 million from year-end 2014. This is after taking into account capital return through \$75 million of share buybacks and the \$42 million of dividends paid in the first quarter of 2015.

Book value per share increased 4% to \$172.63 from \$166.75 at year-end 2014. Our strong capital position leaves us with capacity to maximize our business opportunities as well as continued share repurchases.

Thank you. And now John Doucette will provide the operations review.

**John P. Doucette**

*CEO & President of the Reinsurance Division*

Thank you, Craig. Good morning. As Dom highlighted, we have continued our trend with another favorable quarterly underwriting result, starting off 2015 on a very strong footing.

Our group gross written premium for Q1 2015 was \$1.4 billion, up 12% from Q1 2014, with growth coming from segments within both our U.S. and international operations and from virtually every insurance profit center. This 12% growth would be 14% on a constant foreign exchange rate basis. Our group net written premium was \$1.3 billion or \$56 million -- up \$56 million or 5% over Q1 2014.

Starting with our Reinsurance segment. I will cover underwriting results during the quarter, then provide color on major renewals, predominantly 4/1, including a discussion of the market and insights on ways we are navigating this challenging time.

For our global Reinsurance segments, including both total Reinsurance and Logan, gross premium was \$1.1 billion, up 4% or up 7% on a constant foreign exchange rate basis. Net reinsurance premium was \$980 million, down 4%, with increased cessions on our catastrophe business, consistent with our retrocessional strategy.

Our reinsurance book, including Mt. Logan, generated \$226 million of underwriting profit in Q1 2015, a slight increase over Q1 2014. These strong underwriting results validate our reinsurance strategy, which we have articulated for the last several quarters, leveraging our core sustainable strength, including global reach and comprehensive product offerings, expanding our opportunity set to capture profitable growth and utilizing additional capital structures to match risk with the most efficient form of capital, while generating fee income.

April 1 renewals represent approximately 10% of our reinsurance Treaty premium. 4/1 is a key renewal date for Japanese and other Asian business, and for some Latin American and U.S. regional property business. The reinsurance market remains challenging, with average market rates off between 5% and 15%, depending on the line of business, product type and territory.

However, globally, large buyers in Japan, Australia and other regions are consolidating their panels of reinsurers, focusing on a few core trading partners, including Everest. These sophisticated buyers are not focused strictly on price, but are also seeking stable, long-term relationships that can provide both meaningful capacity and comprehensive risk solutions.

This benefits Everest as we gain preferential signings, and in some cases, better-than-market pricing or terms, allowing us to sustain attractive risk-adjusted returns. Conversely, regional clients around the globe are increasingly placing business locally, rather than just in global reinsurance subs, especially in the current softening market.

Everest's centralized field risk, with a decentralized distribution, enables us to capture local market business. Individually, these deals are not always that large. But in the aggregate, it's a sizable premium for us and is more insulated from global competition.

Our strong rating, long-standing client and broker relationships, broadly diversified portfolio, efficient expense ratio, underwriting expertise and capital flexibility are critical elements for achieving better-than-market results.

We continually optimize our portfolios, which allows nimble deployment of capital to where risk-adjusted returns are best. At the same time, we are scaling back or declining deals that do not meet our return hurdle. Where accretive, we use alternative capital support. This flexible underwriting strategy has mitigated the impact of rate pressures.

Mt. Logan continues to attract strong investor appetite, with \$60 million of new inflows from external investors at 4/1, bringing third-party capital and Everest funds in Logan to about \$750 million. Logan is one of the fastest-growing convergence vehicles, highlighting Everest's ability to access and deploy third-party capital and improve Everest's internal returns.

Now turning to our Insurance operations. We wrote \$340 million of insurance premium in Q1 2015, up 48% from last Q1, partially due to prior period negative premium adjustments in Heartland last Q1. Removing this, our Insurance operations gross written premium for Q1 is up 32% quarter-over-quarter.

Important to note, this growth is diversified and originating from 10 separate insurance profit centers in a deliberately constructed portfolio of short-tail lines, long-tail lines, regional and state-specific insurance portfolios.

Now some detail on the business composition and what we are seeing in each market. California workers' comp, one of our largest segments of the insurance book, was almost \$100 million in Q1, up over 20% compared to the prior Q1, and had a 94.3% combined ratio. Our renewal retention rate stayed relatively steady, and pricing remains favorable with moderating rate. We continue to selectively add underwriting talent to support growth efforts throughout the state, with recent additions to our Northern California team.

Professional liability premium, largely financial institutions, was \$45 million for Q1 2015, up 43% over last Q1. The FI market is stabilizing after a year of price decline, and we captured several new opportunities while maintaining a high renewal retention rate and grew with selected expansion to other lines for FI. However, we remain cautious for commercial D&O, as rate pressures are evident.

Other casualty business, including our environmental and casualty facilities, was up 25% to approximately \$40 million. Our direct facilities are ramping up with new agency appointments and increased staffing, resulting in increased submission and quote activity, and driving new business growth. Renewal retention rates are about 80%. We are bullish on our opportunities in longer-tail insurance lines.

Turning to short-tail, including property, DIC and contingency business. Written premium was \$65 million, an increase over 60% from last Q1. Focused growth initiatives have been successful. We added offices and underwriters in Atlanta and Chicago to strategically grow and geographically diversify our property insurance book, and we plan to further expand geographically.

Specialty insurance group, our contingency business, has also expanded offices, hired underwriters and forged several new strategic partnerships. Six products are highly complementary to other insurance product offerings, providing synergies across the line.

DIC premium was flat, as competition has lowered rates and relaxed terms. However, we will continue to adhere to our pricing targets and leverage our significant capacity to maintain our position. Nonstandard auto grew over 25% to \$26 million, with rate increases over 5%. Our strategic partner, Arrowhead, is providing select geographic expansion opportunity. We are currently implementing predictive analytics to further enhance this portfolio.

Accident and health premium was up in Q1, with submission and quote activity very high. Our future deal pipeline for A&H is strong, and we anticipate continued growth throughout 2015.

Regarding crop, we compare favorably to last year due to prior period negative premium adjustment in 2014. While it is still too early to predict our final full year crop ratings, we made several strategic hires and are seeing favorable year-over-year volatility factors. We also could benefit from disruption within several transitioning crop companies.

Overall, the Insurance segment ran to a 95.9% combined ratio for Q1, a 2.3% improvement over last year, with meaningful, diverse, top line growth. This demonstrates the success of the strategies to drive profitable growth that we have been communicating over the last several quarters.

We continue to build on our strengthening insurance franchise through selective hires, both in the U.S. and international. We are bringing additional products to market, opening new distribution channels and enhancing existing ones. We are diversifying geographically, as we bolster our relevance to our insurance customers and key distribution partners and provide meaningful solutions for their evolving need.

In summary, we have made significant strides over the last couple of years to reposition our insurance operation, as evidenced by the noted improvement in results. We are poised to take our insurance operations to the next level with our strong and dynamic insurance team. Reinsurance has long been Everest tradition. But over the next several years, we will build an insurance operation that will complement our reinsurance franchise and strengthen and diversify the overall organization.

Thank you. And now back to Beth for Q&A.

**Elizabeth B. Farrell**

*Vice President of Investor Relations*

Thanks, John. Jim, we are open now to take questions.



## Question and Answer

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### Operator

[Operator Instructions] Now we'll take our first question from Kai Pan with Morgan Stanley.

### Kai Pan

*Morgan Stanley, Research Division*

And first question is on the recent catastrophe losses. Do you have any potential exposure in the Nepal earthquake, the terrible earthquake happened? And also, any potential exposure from the riot down in Baltimore?

### Dominic James Addesso

*Chief Executive Officer, President and Non-Independent Director*

In terms of Nepal, no, we have no material exposure of any there. In terms of Baltimore, I don't have an answer for that at this point. Certainly, there might be some risk exposure -- individual risk exposure there, but I would not expect that to be material.

### Kai Pan

*Morgan Stanley, Research Division*

Okay. And then on your insurance side, it looks like you're making a tremendous progress out there. I just wonder, is the 96%-ish combined ratio you have set in the past few years, basically x some items, the underlying is really, x crop, is really around 95%, 96%. Is that kind of like still the target combined ratio for the Insurance segment going forward?

### Dominic James Addesso

*Chief Executive Officer, President and Non-Independent Director*

The target combined ratio for the Insurance segment would be lower than that, and I would anticipate that we could continue to drive that combined ratio lower from here.

### Kai Pan

*Morgan Stanley, Research Division*

Okay. My last question is on your capital management. It looks like you have record -- like earnings for the quarter, the payout ratio is in the 30s. I just wonder -- and also, if you look at first quarter last year, you have much larger buyback. I just wonder, given the market condition, do you think that the payout should be higher than you're currently paying out? Or are you looking for gross opportunities, including both organic in the primary insurance area or potential acquisitions?

### Dominic James Addesso

*Chief Executive Officer, President and Non-Independent Director*

Yes to a couple of those questions. First of all, I think our share repurchase program, we look at our capital position over a very long time horizon. Certainly, we look to grow the business where we can profitably. And I think, just as an example, as we mentioned in the prepared comments, we've returned \$3 billion -- over \$3 billion, almost \$4 billion of capital to shareholders since 2006, almost 40% of that in terms of share repurchases. 40% of our shares have been repurchased since 2006. So that's a very -- but that's over a long time horizon. During that time period, all of us, including yourselves, you might recall that we have had certainly significant pressure to buy in more stock certainly from the Street. But what we have been able to do is balance that out between profitable growth and maintaining sufficient capital to expand the business profitably. And I think we demonstrated that we've been able to produce a quite respectable and superior return on equity by moving in that direction. To your question about going forward, given where the market is today, certainly, if the market continues to slip further from here, we would be less optimistic about premium growth and perhaps push a little bit more on the share repurchase. But that is something that, again, we look at over the very long term. Our purchases of stock



in the first quarter, frankly, had been in the market. And really, the stock just kept moving ahead of our price targets in the first quarter. Otherwise, we likely would have purchased a little bit more. Again, we don't have any specific targets that we've communicated to the Street, nor do we intend to. Again, it's always looking at a balance between profitable growth and maintaining the right level of capital. And those things will always be moving in tandem as we move forward in time. I hope that answers your question, Kai.

## **Operator**

And we'll take our next question from Michael Nannizzi with Goldman Sachs.

### **Michael Steven Nannizzi**

*Goldman Sachs Group Inc., Research Division*

Just maybe to follow up a bit on the insurance book. I'm just trying to -- as far as the growth that came from crop versus the other lines, I think, John, you kind of outlined some of the specific items. But I know the seasonality of crop is a little bit different. Just trying to think about how we should be looking at premiums for the rest of the year on an earned basis. Is there -- any context would be really helpful there.

### **Craig W. Howie**

*Chief Financial Officer and Executive Vice President*

For the overall growth, Michael, the position that has come forth is from a whole bunch of different areas within that area, and it's across the page. I don't have those numbers specifically in front of me.

### **John P. Doucette**

*CEO & President of the Reinsurance Division*

Michael, let's first recognize that the growth year-over-year, we had a premium adjustment last year that's kind of amplifying the percentage growth that we're seeing in that crop number. We won't know the actual premium number, but I wouldn't expect any huge increase year-over-year as we finish the year because there's a couple of things going on. We would certainly -- we do certainly expect to expand. We have expanded our distribution. We are writing more business and geographically spread with more agents and more territories. So that's a positive. Offsetting that, of course, will be the effects of pricing from -- or expect the effects on premiums from commodity price declines, so that's a negative for the premium account. And then a positive will be, as John mentioned in his comments, was the volatility factor, which could help premiums go up. So all that being said, we're not providing a prediction on the premium, but that gives you some flavor of the factors that will affect the premium.

### **Michael Steven Nannizzi**

*Goldman Sachs Group Inc., Research Division*

Got it. And then I guess just trying to understand a little bit more in some of those target areas. Is it because Everest is being able to be more sort of tactical in finding opportunities that you're able to grow and grow at attractive levels of profitability? It's just -- because some of our -- other companies are more focused on optimizing retain books, and we just haven't seen elevated growth. So I'm just trying to understand like -- or maybe you can give me an example of, if possible, opportunities where you're able to kind of pick off new business in this sort of low- to mid-90s range, if weather conditions or were there some displacement in those target areas.

### **John P. Doucette**

*CEO & President of the Reinsurance Division*

Well, are you referring -- was that a question on the insurance operation our reinsurance operation?

### **Michael Steven Nannizzi**

*Goldman Sachs Group Inc., Research Division*

Well, mostly on the insurance, just so we've had the biggest ton of growth and the underlying was a couple of points better than we have, for example.

**Dominic James Addesso***Chief Executive Officer, President and Non-Independent Director*

Okay. Well, first of all, excluding the impact of crop, I think the number would be insurance premium growth probably in the low 30s.

**Craig W. Howie***Chief Financial Officer and Executive Vice President*

Yes, 32%.

**Dominic James Addesso***Chief Executive Officer, President and Non-Independent Director*

So recognize that, first of all. Second, there are markets that others aren't in. So California comp is one example where we continue to grow, and that's not something that the rest of the industry, more broadly speaking, has been a factor in. And we've got a very good position in that marketplace, so we're able to grow that. Same thing would apply with respect to California DIC. Again, given our appetite, predominantly as a reinsurer, that's a risk that we feel nicely fits into our balance sheet, where with many primary companies, it may not. The same thing would apply to our property E&S operation, which is certainly very strong, up and down the Northeast Coast -- or in the East, I should say, up and down the entire Eastern Seaboard. And so a lot of companies and distribution partners look to place their property exposure with A+ carriers. So that's certainly a reason why we're growing. Same thing would apply in the excess casualty area. Remember that these are not today huge businesses. But again, distribution partners looking for A+ large balance sheet partners. That's very helpful. And then finally, in the contingency space, the hiring of a new team in a specialty niche. Again, something that we have built up some unique expertise, and not everybody is in it. Same thing could apply to A&H. I mean, you could go down to each business that we're involved in, as John mentioned, and you could look to a unique offering that we've made to the marketplace, a unique appetite that others may not have and a strong balance sheet. These are all things that are attractive to distribution partners.

**Michael Steven Nannizzi***Goldman Sachs Group Inc., Research Division*

I see. So in some of these insurance lines, so your rating and your sort of unique appetite, those are differentiators that allow you to kind of see business and buying business at maybe better than peer profitability.

**Dominic James Addesso***Chief Executive Officer, President and Non-Independent Director*

That's correct.

**Michael Steven Nannizzi***Goldman Sachs Group Inc., Research Division*

Okay. And then one question, Craig, if I could, one more here, just on the FX impact on the revaluation reserves. I was just trying to understand, should we be thinking about that relative to premiums? Or should we be thinking about that relative to asset marks that run through AOCI? So -- because I was just looking at that, we had a bigger markdown on assets in the fourth quarter, and then we have a smaller revaluation reserve and then no real impact on AOCI this quarter relative to last, but then we have the FX impact on reserves. Just trying to get an idea. Should I be thinking about those 2 next to each other? Or should I be thinking about more of the reserves relative to the impact of FX on premiums?

**Craig W. Howie***Chief Financial Officer and Executive Vice President*

So Michael, it is more relative to the reserves. But overall, I think we've mentioned this before, but we try to maintain an economic-neutral position with respect to foreign exchange. So essentially, matching those assets within the local jurisdiction to the same currency in each jurisdiction. What you have is a mark-

to-market type adjustment here at a point in time on the balance sheet, which is causing what's flowing through the income statement. That's the \$47 million gain that you see in other income, other expense line. Offsetting that, our foreign exchange losses that you just mentioned coming through OCI. So on an overall basis, it's almost completely neutral from a book value standpoint for the quarter.

**Michael Steven Nannizzi**

*Goldman Sachs Group Inc., Research Division*

All right. Okay. So even though -- so the AOCI that we see on the balance sheet, that includes the investment marks and then -- and FX, and then -- but the investment marks were more than the FX headwind, so that sort of obscure that \$46 million that we would've seen on the asset side?

**Craig W. Howie**

*Chief Financial Officer and Executive Vice President*

That's correct, Michael.

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

That means, Michael, in reverse, to the extent that the currency is reversed, of course, then you get kind of the opposite effect, right? So again, as Craig has highlighted, it's economic-neutral to book value-centric.

**Operator**

And we'll take our next question from Josh Shanker with Deutsche Bank.

**Joshua David Shanker**

*Deutsche Bank AG, Research Division*

My first question regards Kilimanjaro and trying to understand the structure. In the event of a loss that triggers Kilimanjaro, does Mt. Logan also receive protection under the Kilimanjaro umbrella or is it just the Everest Re book?

**John P. Doucette**

*CEO & President of the Reinsurance Division*

Josh, it's John. It would just be Everest Re that gets the protection under Kilimanjaro.

**Joshua David Shanker**

*Deutsche Bank AG, Research Division*

So -- and that also does not include your equity participation -- your equity participation in Mt. Logan is under their terms as well?

**John P. Doucette**

*CEO & President of the Reinsurance Division*

If I understand your question correctly, Everest's participation as an investment in Mt. Logan stands pari-passu with the investors in Mt. Logan.

**Joshua David Shanker**

*Deutsche Bank AG, Research Division*

Okay, excellent. And so now we are through 4/1 renewals, heading obviously into the big Atlantic cat win renewal. But the -- I was sort of wondering, if -- when you think about the investor's appetite for third-party capital now that's a big renewal, is there more room for Mt. Logan or a similar vehicle to grow in this environment?

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

Josh, we really can't comment on other vehicles...

**Joshua David Shanker**

*Deutsche Bank AG, Research Division*

No, I'm just saying -- I'm saying, Everest -- does Everest's possible third-party participation stand to grow, I guess? Is the appetite from the market broadly out there for more third-party capital participation at current prices?

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

Well, we can answer the question tied to Mt. Logan and Everest and the answer is, yes. We have investors. We've been building our investor base in terms of number of investors. We have investors that have been looking at it for a long time, and a lot of them, it's a slow process in terms of getting comfortable with the underwriting, the team, the analytics, the portfolio, the construction, the value proposition that we put forth. But ultimately, we feel bullish that, that will continue as we felt -- feel we have built a meaningful and significant and differentiating proposition for third-party capital. So yes, we expect to continue to have increased appetite into Mt. Logan.

**Joshua David Shanker**

*Deutsche Bank AG, Research Division*

And is that equally in the sort of 15% kind of returning characteristic business and the 6% type of returning characteristic? Or is the demand more so in one area of the market than the other?

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

It very much -- that's a good question. It very much depends on the investor and what their risk profile is, what their return mandates or targets are and what their overall investment philosophy is. So it really depends on which investor and which type of investor invests in -- wants to put money to work in Mt. Logan.

**Joshua David Shanker**

*Deutsche Bank AG, Research Division*

Sorry, but I'll have more questions. I'm always learning. Do you need both kinds of investors from Mt. Logan to be really successful? Do you need someone to take the severity risk and someone to take the frequency risk? Or can you grow one pool without growing another?

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

Again, an excellent question. What we've been doing -- Mt. Logan is a core strategic part of Everest capital management and property catastrophe management, and we will have this for many years to come. But it also is not the only thing we do. You mentioned Kilimanjaro cat bonds. So we balance across the cat bonds, traditional reinsurance, protections, traditional retrocessional protections, ILWs and Mt. Logan. And the combination of those suite of hedges and cat management structures gets Everest to the -- what we're comfortable with in terms of a net catastrophe PML position.

**Operator**

We'll take our next question from Meyer Shields with KBW.

**Meyer Shields**

*Keefe, Bruyette, & Woods, Inc., Research Division*

Two quick reserve questions, if I can. First, Gallagher was discussing at CPA business, and I noted they quote the 5% existing clients claim increases year-over-year. Are you seeing that sort of trend in California workers' comp where there's a spike in claim frequency?

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

Was that a frequency trend that they saw or a severity trend?

**Meyer Shields**

*Keefe, Bruyette, & Woods, Inc., Research Division*

That was frequency.

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

I cannot say that we have seen that, no. Not that kind of trend.

**Meyer Shields**

*Keefe, Bruyette, & Woods, Inc., Research Division*

Okay. Is there anything going on with the severity side?

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

Not that's -- it's not been what we've seen over the last couple of years. It's been relatively, I won't say benign, but it's consistently emerging in the manner that we predicted it would in our loss reserving process.

**Meyer Shields**

*Keefe, Bruyette, & Woods, Inc., Research Division*

Okay, perfect. And then broadly speaking, when you look internationally and you're writing business outside the United States, and you got these currencies weakening against the United States, does that translate into a higher required loss trend? In other words, U.S. trend, let's say, higher inflation in those other regions?

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

Not per se. I mean, certainly, a lot of what we do overseas is first-party cover, cat-exposed cover. So it's less casualty-focused and more property-focused. I mean, if you think about global demand, the U.S. obviously being the most casualty-intensive place in the globe and, of course, second behind that would be Europe. But no, we're not particularly noticing any or we're not fearful of any particularly troublesome inflationary trend. No.

**Operator**

And we'll take our next question from Brian Meredith with UBS.

**Brian Robert Meredith**

*UBS Investment Bank, Research Division*

Got some questions here for you, guys. The first one, Craig, was there any FX impact on the investment income or the fixed-income investment income in the quarter? Or is this decline solely related to just lower yields?

**Craig W. Howie**

*Chief Financial Officer and Executive Vice President*

That would -- so in -- the investment piece would actually come through OCI, Brian. And so that's reflected in the number down below the line.

**Brian Robert Meredith**

*UBS Investment Bank, Research Division*

Okay, so nothing would come by, so that's purely just lower investment yields in the quarter, 6% decline in the fixed income. Okay. Second question. On the cat losses, once again, there was a couple of European windstorms kind of at the end of the quarter. They kind of fell into the second quarter. Was there any exposure there? And can you tell us if those were booked if you had any exposure in the first quarter?

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

No, we aren't anticipating anything at this point. It -- we're not anticipating any losses getting into our cat, what we could consider a catastrophe, right? And we classify catastrophe as above \$10 million. It doesn't mean we won't have losses, but at this point, we're -- it's looking as if that would -- any of those events would be below \$10 million.

**Brian Robert Meredith**

*UBS Investment Bank, Research Division*

All right, got you. So they're going to be relatively modest. Got you. And then, Dom, have you seen any impact or seen any business yet from the M&A wave that's going on right now in the reinsurance industry? Or if you're going to see it, when do you expect you might start to see that in this spillover?

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

Well, you see it in a few pockets. I mean, I would not say that it's, at this point, it's a huge impact. You do see it in terms of human capital as well, though. There's certainly more chatter in the marketplace about that. And that -- it would take many months for it to have any material impact for sure.

**Brian Robert Meredith**

*UBS Investment Bank, Research Division*

Got you. So that's what we should be looking for, is like teams of people leaving and that could indicate the movement of business?

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

That would be one factor. It doesn't mean necessarily that we or anyone else, frankly, would be picking up teams because we think we have certainly the resources to underwrite that business. I'm just saying that could be a factor, maybe not for us, but certainly, it could be for others.

**Brian Robert Meredith**

*UBS Investment Bank, Research Division*

Got you. And then just lastly, any kind of early thoughts on what you think the Florida renewals are going to look like?

**Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

Well, certainly, there'll be pressure on the Florida renewals. There was some pressure on what we thought was the appropriate premium base for the cat fund. In fact, we've put out a fairly good line on the cat fund, and we ended up not -- our write was not accepted. And as a consequence, we took a very tiny line. So if that's any indication, it's possible that the market could start to fall below what our pricing metrics would be. And by the way, just to give some context to all that. For us, even though we're obviously listed as one of the largest writers in Florida, a lot of that is pro-rata premium. And our excess of loss premium for the Florida-only companies now, right, which would represent the June and July debt renewals because we do have other Florida exposure coming from nationals and other sources that have different X dates. But that -- our XOL business in Florida is approximately \$150 million. So any rate movement that you think about used to be thought about in the context with the premium base.

**John P. Doucette**



*CEO & President of the Reinsurance Division*

And just to add a little more color. We're not sure what's going to happen as we head into June 1 and July renewals. But we do feel very comfortable that we're positioned well to execute our plan, how it happens, where it happens. And again, moving -- as we've talked about, if you could go back last couple of years, we've moved between pro-rata and cat very easily. Risk, we moved from Florida-specific to nationwide covers and superregional covers. In terms of deploying more or less relative capacity as we look at those, we write property insurance in Florida, we write reinsurance, we write retrocessional protections, we write PURPLE. So we have the ability to access Florida exposure in many different ways, and we take advantage of that. And we also have the ability to hedge and manage the net PML in many different ways, as commented on, on one of the previous questions.

**Dominic James Addesso***Chief Executive Officer, President and Non-Independent Director*

Great point that John made. And the one offsetting factor to what I've described is potential rate pressures, at least, with, obviously, the first client that's come to market, large client, is that there is also some evidence that there will be increased demand coming from the market. So that could beat any of the rate pressures that we're all fearful of. But we will see as the market evolves. But as John described, we have many different levers to pull and many ways to access profitable business.

**Operator**

And we'll take our next question from Amit Kumar with Macquarie.

**Amit Kumar***Macquarie Research*

Just maybe 2 quick follow-up questions. The first question maybe goes back to Meyer's question. Is the California comp book still running at an AOI LR [ph] of mid-90s? Or has there been any shift in that?

**Craig W. Howie***Chief Financial Officer and Executive Vice President*

Yes, that book is still running in the mid-90s, Amit. This is Craig. And the deal was though we're seeing exactly what we expected to come out from a reserving perspective. Those metrics are still running well as well, so that book continues to perform as we would expect.

**Amit Kumar***Macquarie Research*

Got it. And I guess just going back to Brian's question. In your opening remarks, you were talking about, I guess, how insurance will complement reinsurance, and you were talking about the franchise. You talked about the other opportunity, but how does M&A factor in into this picture? Or are you more on the sidelines right now?

**Dominic James Addesso***Chief Executive Officer, President and Non-Independent Director*

When you say, how does this factor, into what picture?

**Amit Kumar***Macquarie Research*

In terms of the strategy. And if you look at the list of companies out there who might be looking for a buyer?

**Dominic James Addesso***Chief Executive Officer, President and Non-Independent Director*

Well, Amit, first of all, we look at many things and we've looked at many things over the last couple of years. So it's not that M&A is not something that we don't consider. But clearly, as we've looked at

many different things over the last couple of years, we've ultimately determined that the path that we're on, relative to what the other opportunities have been, was the best path, meaning, we build our own platform, continue to build out our talent, build with one brick at a time, so you know which you have. It doesn't mean -- it doesn't preclude looking at properties that might be a better fit or might allow you to get to a place faster than you otherwise would. But of course, that's all relative to pricing as well. So none of those things are off the table. But clearly, we have -- as we've gone through the strategy time and time again, we opted to continue to grow by building it one brick at a time. And if something comes along that's a terrific fit, then we will consider that for sure. But right now, we think we've been able to build the right platform on our own.

### **Operator**

And we'll take a follow-up question from Michael Nannizzi with Goldman Sachs.

### **Michael Steven Nannizzi**

*Goldman Sachs Group Inc., Research Division*

Just a couple of quick ones here, if I could. One thing -- a question was the tax rate, Craig. I thought normally, like when the cats were lower, the tax rate would be higher just because you had more profitability maybe in the U.S. Was there something else inside that tax rate? And how should we be thinking about that part?

### **Craig W. Howie**

*Chief Financial Officer and Executive Vice President*

Michael, the way that tax is calculated is on a full year, annualized tax rate. It's an effective tax rate for the year. So in essence, we still have catastrophes planned for the remainder of the year in our plan. So that's what goes into calculating the tax. If, in fact, we didn't have catastrophes like we've had in past years, that tax rate will inch up because you'll have higher taxable income and have to pay higher taxes. But at this point in the year, it's on the lower end of our range because of the fact that we still have 3 quarters of catastrophes planned for the remainder of the year.

### **Michael Steven Nannizzi**

*Goldman Sachs Group Inc., Research Division*

Got it. Okay, great. That makes sense. And then on the international Reinsurance segment. You mentioned some fires, I think, in the prepared comments. How much -- can we quantify how much the sort of one-timer type stuff impacted the underlying there? Or was it significant? Maybe it wasn't, I don't know.

### **Craig W. Howie**

*Chief Financial Officer and Executive Vice President*

For this year, those numbers are not significant from the standpoint of reaching the level of a catastrophe loss. In other words, it was several fires or several losses that fell below that \$10 million threshold that we have for catastrophe losses. But the number -- the amount of those fires added up to about \$40 million so far this year. Last year, that number was substantially higher, which is the reason that we increased our loss estimate selection for the international segment back in the third quarter of 2014. We continue to keep that loss selection a little bit higher as we go through the year just because of these types of losses.

### **Michael Steven Nannizzi**

*Goldman Sachs Group Inc., Research Division*

Got it. Great. And then just last one, if I could. I mean, just thinking about like the cat as being a little bit lower where you get a little benefit, tailwind from taxes, the FX item. How should we think -- or how do you think about the current ROE relative to your own cost of capital, just given your own historical context? And how you're thinking about results at this point?

### **Dominic James Addesso**

*Chief Executive Officer, President and Non-Independent Director*

Well, clearly, at an 18% ROE, we're well above our cost of capital, so I don't know that that's necessarily a pressing issue. Even though -- this may not be answering your question directly, Michael. And if it's not, please follow up. But it's -- we had, as I've said, an 18% ROE, we benefit, of course, from light cat years, but certainly, so does the rest of the market. If you take our expected cat load, which we think about as like 12 points, combined ratio points, that's about 6 points of ROE. But even -- and even at that level, we're well above our cost of capital and clearly, we are outperforming the market. Frankly, even after that cat load, I would almost argue that we're outperforming the market even if you put that number in comparing to the rest of the market with no cats. So we are not bumping into or getting close to even at those levels to our cost of capital. The point I made in my opening comments was that it seems to me that as an industry, we are getting pretty close to that, but we are not there yet, and not even there. But -- and so that should have some -- we think it would have some impact on pricing.

Okay. So I think we're done with the questions. I don't think there's anyone left there with a question. So let me just thank everybody in closing. I'd like to emphasize our underlying core results are strong, both in the Reinsurance and in our Insurance segments. As I've said, clearly, we benefit from light cat years. But again, even with an expected cat load, we are still very much outperforming the market. And this, frankly, is a result of portfolio diversification and an effective use of capital, both internal and external, as we've kind of highlighted on this call and, frankly, in conversations we've had with many of you previously.

So I'd like to thank you, all, for your participation on the call and look forward to speaking with many of you in the weeks ahead. Have a great day. Thank you.

**Operator**

And that does conclude today's conference call. We appreciate your participation.

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