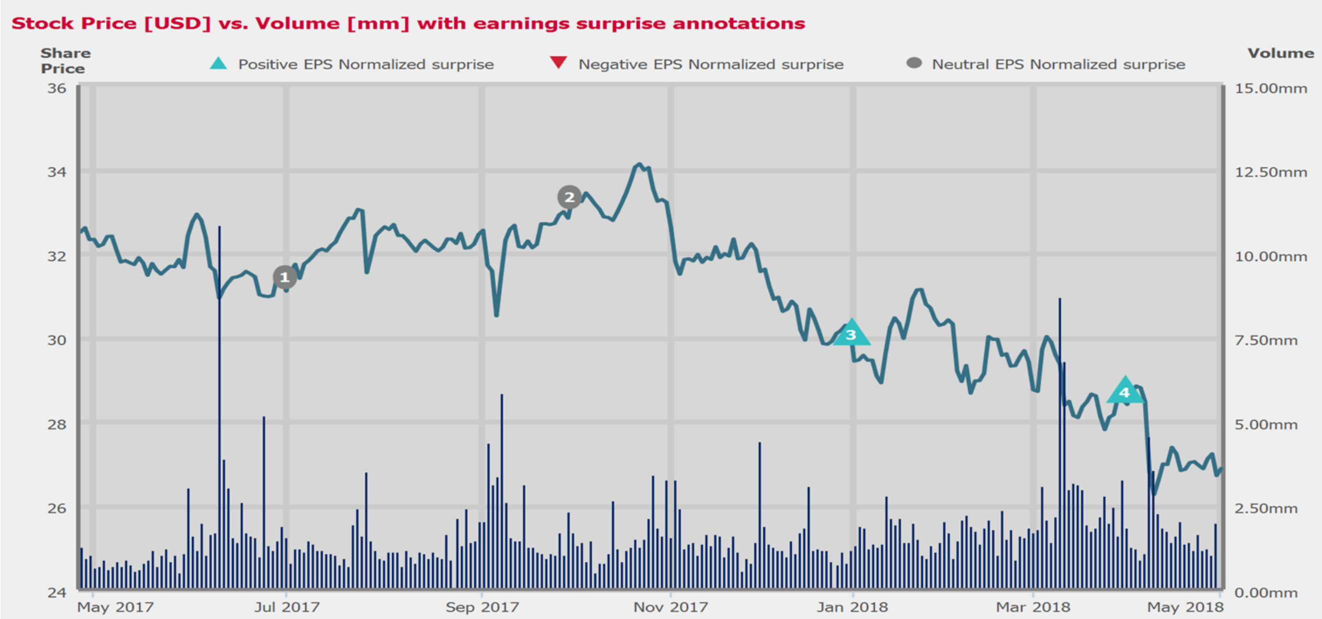
S&P Global
Market Intelligence

Arch Capital Group Ltd. NasdaqGS:ACGL
FQ2 2018 Earnings Call Transcripts
Wednesday, August 01, 2018 3:00 PM GMT
S&P Global Market Intelligence Estimates

	-FQ2 2018-			-FQ3 2018-	-FY 2018-	-FY 2019-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.53	0.59	▲11.32	0.51	2.18	2.32
Revenue (mm)	1128.50	1158.31	▲2.64	1279.70	4822.13	4937.00

Currency: USD
Consensus as of Aug-01-2018 11:29 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2017	0.40	0.40	1 0.00 %
FQ3 2017	(0.21)	(0.26)	NM
FQ4 2017	0.37	0.45	2 21.62 %
FQ1 2018	0.52	0.56	3 7.69 %

Table of Contents

Call Participants

EXECUTIVES

François Morin
Executive VP, CFO & Treasurer

Marc Joseph Roland Grandisson
CEO, President & Director

ANALYSTS

Brian Robert Meredith
UBS Investment Bank, Research Division

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Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

Michael David Zaremski
Crédit Suisse AG, Research Division

Michael Wayne Phillips
Morgan Stanley, Research Division

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Q2 2018 Arch Capital Group Earnings Conference Call. [Operator Instructions] As a reminder, this conference call is being recorded.

Before the company gets started with its update, management wants to first remind everyone that certain statements in today's press release and discussed on this call may constitute forward-looking statements under the federal securities laws. These statements are based upon management's current assessment and assumptions and are subject to a number of risks and uncertainties.

Consequently, actual results may differ materially from those expressed or implied. For more information on the risks and other factors that may affect future performance, investors should review periodic reports that are filed by the company with the SEC from time to time.

Additionally, certain statements contained in the call that are not based on historical facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The company intends the forward-looking statements in the call to be subject to the safe harbor created thereby.

Management also will make reference to some non-GAAP measures of financial performance. The reconciliation to GAAP and definition of operating income can be found in the company's current report on Form 8-K furnished to the SEC yesterday, which contains the company's earnings press release and is available on the company's website.

I would now like to introduce your host for today's conference, Mr. Marc Grandisson and Mr. François Morin. Sirs, you may begin.

Marc Joseph Roland Grandisson
CEO, President & Director

Thank you, Crystal, and good morning to you all. We were pleased with the results across our platform this quarter as our MI segment continued to produce outstanding returns while slightly improving conditions in our P&C operations and higher investment yield helped to produce an annualized operating ROE of 11.6% and an increase in book value per share to $20.68.

As you may know, we believe that an opportunistic approach to underwriting and active capital and risk management will produce higher risk-adjusted returns over time. As a result of this dynamic allocation of capital, we may be underweight or overweight in certain segments or areas of the markets at any point in time. Our MI focus right now is Exhibit A of this strategy, and we believe that the current level of returns available in the MI space justifies the deployment of additional capital there.

In our P&C businesses, market conditions seem to be improving modestly. In most of our insurance lines, rate increases appear to be outpacing claim trends. However, in assessing how this will ultimately impact margins, there are several issues with estimating insurance margins that temper our current market view.

First, the calculation of trend is based on past experience, while actual trend is dependent on future circumstances, which in many lines means looking several years out. Second, at the center of great adequacy projections is an implied perfect knowledge of the current loss estimates. As we all know, loss reserving in our industry is a cumulative result of self-graded exams, and it can take several years for the truth to emerge.

Third, rate changes as reported do not capture new business written or the effects of most changes in terms and conditions. Due to these uncertainties and factoring in the record level of capacity currently in the business, we remain cautious in our underwriting posture.

With that said, let me provide some color on our P&C premium volume for the second quarter. First, bear in mind that the increase in P&C net premium written was magnified by FX movement, which represents about 30% of the increase in net written premium.

In our insurance segment, more than 60% of the growth in net written premium was due to rate increases, and the balance was from exposure growth. On a line of business basis, the increase was the result of our ongoing efforts in travel, programs as well as from recent market opportunities in property. We decreased premium again this quarter in the more commoditized line, such as general liability and D&O due to the highly competitive environment.

In our reinsurance segment, net premium growth was generated primarily from property, other than property cat, growing slightly consistent with our view of conditions in our primary insurance. Of note, net property cat writings were down as most rate levels were below our risk-adjusted return requirements.

With respect to our P&C underwriting results, on which François will provide additional details in a moment, there is one topic, which I think is particularly noteworthy. Large attritional losses affected the results of both insurance and reinsurance but in opposite directions.

The insurance group benefited from a below-average level of such losses, while our reinsurance operations were impacted by a higher-than-normal level, mainly in the facultative area. This demonstrates that the randomness -- that there is randomness and lumpiness of when these type of losses occur. You rarely, if ever, get an even distribution of expected losses in a given quarter or year. But over time, specialty businesses, such as ourselves, can generate good risk-adjusted returns, if managed properly.

Turning now to MI. I'm going to focus on our U.S. primary business, which represents over 80% of that segment. Our U.S. MI production for the second quarter was strong at $19.9 billion, a 15% increase over the same quarter last year. About 80% of our primary MI was still written through our RateStar platform.

As respects growth from a sequential basis, keep in mind that there are substantial seasonal effect between Q1 and Q2 when home purchases typically peak. Our U.S. new insurance written, or NIW, increase was due to a few additional key factor.

First, it's clear to us that MI return fundamentals are excellent. House price appreciation has been broad and stronger than expected, the quality of credit remained high and our ability to price more finely for many parameters is truly an advantage. Given these strong market conditions, returns have been better than anticipated and remain very attractive.

Second, we have been successful in our efforts to expand our distribution and produce relationships with both existing and new customers, and in a few cases, we were able to close some large transactions that, while attractive from a return standpoint, brings some lumpiness to our NIW in the quarter.

Third, the capital and risk management tools that we have put in place, namely the Bellemeade transactions, provide additional downside protection and reduce the volatility of our expected returns in MI.

For the second quarter, RateStar again directed our production away from lower-return projects, such as singles, to borrow [indiscernible] as singles production declined from -- to 6% from 9% in the first quarter.

Higher loan-to-value and debt-to-income products represented a slightly larger share of our NIW in Q2, but we remain underweight in those areas relative to the market. This growth was opportunistic and occurred partly due to the response by our competition to the rapid shift in mix that occurred in the first quarter. Market pricing, at this point, appears to have stabilized after the activity of the last few months.

Before I move on from MI, I want to update you on recent developments. Regarding the pilot programs with the GSEs, IMAGIN and EPMI, they are still in their infancy, and there was no significant NIW in the second quarter. We will keep you posted as to their progress on future calls.

Briefly, with respect to our investment operations, we increased our duration slightly as we moved money out of cash equivalents to predominantly 2- to 5-year treasury instruments. In addition, the current interest rate environment has and will improve net investment income for the next several quarters.

Finally, a few words on capital and risk management. We repurchased a significant number of shares in the second quarter. François will give you the details, but it is worth repeating that share repurchase is yet another way for us to manage and allocate capital. As for risk management, our property cat exposures remain at historically low levels with our 1-in-250 year peak zone at only 5% of tangible common equity at the end of the second quarter.

For our mortgage segment, as of June 30, 2018, exposures under our realistic disaster scenario declined last quarter, as growth in insurance in-force was more than offset primarily by the capital relief from the Bellemeade transaction and a run-off of the pre-2009 business.

Prospectively, we believe that regulatory capital, as defined by the PMIERs, represent a more conservative capital requirement. As of June 30, 2018, Arch MI was up 134% of the current PMIERs. And although we are unable to discuss the proposed changes to PMIER 1 that will create PMIERs 2.0, we do not believe that the proposed changes will have a material impact on our capital position and that our estimated available assets will continue to exceed the required asset as proposed on the PMIERs 2.0.

With that, I will turn it over to François.

François Morin
Executive VP, CFO & Treasurer

Thank you, Marc, and good morning to all. I'm pleased to join the earnings call this morning and to provide more color on our second quarter earnings.

As I stated during our recent Investor Day, one of my objectives in this new role will be to keep providing the same level of clarity and visibility the investment community has come to expect from us when analyzing our financials and public disclosures. This practice will remain a key principle of ours.

On that note, I will make some summary comments for the second quarter all in our "core basis", which corresponds to Arch's financial results excluding the others segments, i.e. the operations of Watford Re, whereas the term consolidated includes Watford Re.

As you know, we effected a three-for-one stock split on June 20, which impacts per share metrics and comparisons to prior periods. My comments will reflect the latest number of shares after the split, which currently stands at approximately 405 million outstanding shares.

After-tax operating earnings for the quarter were $242.6 million, which translates to an annualized 11.6% operating return on average common equity and $0.59 per share.

On a year-to-date basis, our annualized operating ROE increased by 200 basis points since last year to [Audio Gap] highlighting the improved performance of our operations.

Book value per share was $20.68 at June 30, a 1.3% increase from last quarter and a 4.1% increase from 1 year ago despite the impact of higher interest rates on total returns for the quarter and on a year-to-date basis.

Moving on to operations. Losses from 2018 catastrophic events, net of reinsurance recoverables and the reinstatement premiums, were $14.9 million or 1.3 combined ratio points, evenly split between our insurance and the reinsurance segments from a few small events across the globe.

As for prior period, net loss reserve development, we recognized approximately $60 million of favorable development in the second quarter or 5.1 combined ratio points compared to 6.4 combined ratio points in the second quarter of 2017. This was led by the reinsurance segment with approximately $32 million favorable, the mortgage segment at about $23 million also favorable and the insurance segment contributing $5 million.

This level is generally consistent with recent periods on an aggregate basis and across segments. The calendar quarter combined ratio on a core basis was down 200 basis points from the second quarter of 2017, while the core accident quarter combined ratio, excluding cats, improved to 84%, down 230 basis points from last quarter -- last year's second quarter.

The insurance segment's accident quarter combined ratio, excluding cats, was 98.5%, down slightly from the comparable 2017 level, mostly due to an improvement in the current year loss ratio of 150 basis points, slightly offset by higher acquisition expenses, resulting primarily from mix of business changes. We are pleased with these results, but note that a significant portion of the improvement, approximately 90 basis points, is due to a lower frequency of large noncat claims, which, as Marc indicated, are by nature subject to variability from 1 quarter to the other.

The reinsurance segment accident quarter combined ratio, excluding cats, stood at 100% even, slightly better than the 101.1% on a comparable basis 1 year ago. In a similar vein to the corresponding period last year, our results were impacted by noncat large property claims. This result serves as a reminder of the volatility some of our businesses can experience from time-to-time.

The expense ratio benefited from reductions of operating expenses combined with a larger net earned premium base. In addition, a reduction in federal excise taxes of $2.6 million or 0.8 points resulted from the cancellation of certain intercompany property casualty quota share agreements, effective January 1, as discussed last quarter. This item will continue to recur for comparisons of 2018 to 2017 results.

The mortgage segment's accident quarter combined ratio improved by 380 basis points from the second quarter of last year, mostly as a result of improving trends in the underlying performance of the book, particularly within our U.S. primary MI operations.

The accident quarter loss ratio of 15.4% in the second quarter of 2018 compares favorably against the 19.5% in the same quarter of 2017 due to lower delinquency rates. 3.1 basis points of the difference or $9 million is attributable to favorable development on first quarter 2018 delinquencies due to very strong cure activity in 2018.

The expense ratio was at 22.8%, slightly higher than prior periods as a result of higher incentive compensation costs. These figures highlight the contribution to our pretax underwriting income from the mortgage segment, which remains strong this quarter.

However, after allocating corporate items, such as investment income, interest expense and income taxes to each segment, the mortgage segment's contribution to our 2018 year-to-date net income decreases to approximately 65% of the total.

Total investment return for the quarter was a negative 19 basis points on a U.S. dollar basis but was a positive 33 basis points on the local currency basis. These returns were impacted by the effects of higher interest rates on investment-grade fixed income securities, partially offset by positive returns on alternative investments and non-investment-grade fixed income. The investment duration was 2.89 years at June 30, up sequentially from 2.6 years at March 31 as a result of the shift in our portfolio from short-term commercial paper, primarily into 2-year treasuries, where we saw more attractive investment opportunities.

Also during the quarter, we continued to shift our position in -- from municipal bonds into corporates due to improved relative valuations. Corporate expenses were $6.6 million lower than in the prior year as a result of retirements and departures of Senior Executives. The corporate effective tax rate in the quarter on pretax operating income was 9.8% and reflects the benefit of the lower U.S. tax rate, the geographic mix of our pretax income and a 60-basis-point benefit from discrete items in the quarter. As a result, the pure effective tax rate on pretax operating income, excluding discrete items, was 10.4% this quarter, identical to last quarter's rate.

As we look ahead to year-end 2018, we currently believe it's reasonable to expect that the effective tax rate on operating income will be in the range of 9% to 12%. As always, the actual full year effective tax rate could vary, depending on the level and location of income or loss and varying tax rates in each jurisdiction.

With respect to capital management, our debt-to-total capital ratio was 16.9% at June 30 and debt plus preferred to total capital ratio was 23.9%, down 250 basis points from year-end 2017 and a full 480 basis points from year-end 2016 when we closed the UGC acquisition. This leverage reduction is driven mostly by the redemption of $250 million from a revolving credit facility in the quarter.

As for share repurchases, we repurchased 6.4 million shares during the second quarter at an average price of $26.59 per share and an aggregate cost of $170.2 million under both open market purchases and a Rule 10b-5 plan we implemented during our closed-window period.

Since the start of the third quarter, we have purchased an incremental 414,000 shares at a cost of $10.9 million. Our remaining authorization, which expires in December 2019, now stands at $262 million after consideration of the share repurchases made through July 30.

Operating cash flow on a core basis was $34 million in the second quarter of 2018, down on a sequential basis, primarily reflecting the premium seeded for the reinsurance transaction with Catalina General Insurance Ltd., which we discussed during the last quarter's call.
With these introductory comments, we are now prepared to take your questions.

Question and Answer

Operator

[Operator Instructions] And our first question comes from Mike Zaremski from Crédit Suisse.

Michael David Zaremski
Crédit Suisse AG, Research Division

My first question is regarding the mortgage insurance volumes. It looks like you guys took market share, and you mentioned some lumpiness in the prepared remarks. So I was just kind of hoping to maybe understand, do you feel that the market share will be sustained or we should assume that material amount of lumpiness as you said in the comments?

Marc Joseph Roland Grandisson
CEO, President & Director

Thanks for that question, Mike. I think we -- first and foremost, we do not look at market share as an operating principle. We're just looking at the opportunities as we see them in the marketplace. So what I can tell you is what we saw in the second quarter, which generated those -- that production. But I think that the pricing situation in the industry was different as we got into the second quarter, and it's changed since then. And it's a lot more stable. So whatever opportunities we had to do what we did in the second quarter may not keep on being there for the remainder of the year. So it's a really hard question to answer because I don't know the answer to that.

Michael David Zaremski
Crédit Suisse AG, Research Division

It -- does it imply that risk-based pricing is causing more -- is part of the reason you're winning some of these deals? Or it's separate?

Marc Joseph Roland Grandisson
CEO, President & Director

Yes. A large part of our wins was through the RateStar, its ability to more -- again, more finally price for the risk. And the ability that we have to shape the portfolio the way we would want. As I mentioned, we did more monthly. So it's clearly an advantage, and we think the advantage could probably sustain itself going forward, specifically in light of the loan originators and margin being squeezed. So it represents most likely an ongoing advantage. But that advantage that we have from RateStar has been there for a long time. So yes, we do believe it provides us some advantage.

Michael David Zaremski
Crédit Suisse AG, Research Division

Okay. And lastly, sticking with mortgage insurance, thanks for the comments about PMIERs 2.0 not having that material of an impact. I'm curious, is that because you will get a number of quarters to let the impact -- sorry, it's a few quarters before the impact takes place? Or if it happened today, it wouldn't have a material impact?

Marc Joseph Roland Grandisson
CEO, President & Director

Okay. So we are under an NDA. We cannot really talk about the various parameters. But being at 134%, if we tell you that we think we're comfortable, that sort of gives you a rough idea as to where we think it's going to land. Now things could change. They will make the final determination between now and, I believe, the end of the third quarter, which will be implemented in 2019. And those comments, Mike, I would tell you, are -- have been echoed by our competitors as well. And I think it speaks to the health of the results and the returns that -- and the profits that have been generated by the platforms in the MI industry.

Operator

Our next question comes from Elyse Greenspan from Wells Fargo.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

My first question, François, you said the tax rate was going to be 9% to 12% this year. Is that the right level that we should use in 2019 and onwards as well?

François Morin
Executive VP, CFO & Treasurer

That was a good question. Thank you for that. I would say, we don't have the answer right now. Certainly, as you know, we canceled some intercompany quota share agreements at the start of 2018. We're reevaluating those on an ongoing basis. Certainly, as we get into a 2019 planning exercise, which is underway now, we'll have more clarity on that throughout -- internally in the third and fourth quarter. So at this point, it's a bit -- we don't know -- certainly, the B tax, as you know, goes up from 5% to 10% next year. So that will have potentially some impact. But we have certainly a couple of things we can look at -- that we will look, a couple of tools in our toolbox that hopefully will -- we'll try to obviously minimize our tax liability, but we really don't really have a view at this point of what 2019 is going to look like.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Okay. And then on capital return. You guys -- the share repurchase picked up in the quarter. Obviously, at the start of the quarter, your stock was trading at a cheaper evaluation than where it sits today. And I know you guys have your metric, and you look at the payback period as you think about share repurchase. So how does the higher valuation today change your philosophy around share repurchase in conjunction with the fact that we are now also approaching peak 1 season?

Marc Joseph Roland Grandisson
CEO, President & Director

Yes. A couple of points on that. I don't think it really changes how we think about things. Historically, as we said, we said in the past, we typically don't buy back stock in the third quarter. Although we're not really a big cat player anymore, so that's really not something that worries us as much as it might have as a percent of equity going years back. And we've said it many times, we are always looking at opportunities that come to us in terms of potential small transactions, and that's a factor in how we look at share repurchases or buybacks. And there's a couple of things we're working on right now. So we don't really have a definitive view on how the rest of the year is going to look for share repurchases but to answer your main question, I think, is I don't think it really changes our view, even in light of the slightly higher share price that we're currently experiencing.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Okay. And then my last question, going back to mortgage and maybe this ties with some of the questions that Mike was asking as well, but do you think part of the reason that maybe the NIW did grow so much sequentially, were you guys able to lower the pricing variables in your RateStar engine ahead of some of the other changes made by the other primary MIs in their pricing grid? And do you think maybe that led to higher NIW that might not be sustained? Are you able to kind of pinpoint any kind of impact, specifically of your RateStar engine that might have had on the NIW?

Marc Joseph Roland Grandisson
CEO, President & Director

I think your assessment is a very fair assessment.

Operator

And our next question comes from Michael Phillips from Morgan Stanley.

Michael Wayne Phillips
Morgan Stanley, Research Division

I want to drill a little bit more down on the expense ratio for the 2 segments, insurance and reinsurance, kind of going in different directions. Higher acquisition expense in insurance from exchanges and then, if you back out the excise tax thing in reinsurance, you still have pretty good improvement in reinsurance. So kind of -- if you take those 2 separately, kind of just where do you see those leveling off? Continued improvement in reinsurance from here, and 25, 26, is pretty low. I don't know if that's going to continue. And then insurance, kind of where does that peak?

François Morin
Executive VP, CFO & Treasurer

Yes, thanks for the question. Let me start, and I'm sure Marc will chime in. The way -- we certainly look at it in totality. So the geography of loss ratio versus expense ratio, we look at it, but it's not the primary factor we look at. We look at the totality of the combined ratio. If we focus on the insurance segment, certainly, in the quarter, we grew into some areas that have -- are expected, well, will have lower loss ratios at the expense of a higher acquisition expense ratio. So there's a bit of a trade-off here where we're seeing a lower loss ratio against -- and counter that as a higher expense ratio. And it's a similar story in the reinsurance although reinsurance is a bit more opportunistic. We have fluctuations from 1 quarter to the next on what kind of deals we write, what actually ends up coming through our financials. But certainly, in a few instances, we have some agreements and quota share agreements where there's a sliding scale commission where you will see that the loss ratio is a bit lower. Or if it's high -- I mean, vice versa, but if it's lower, right, we'll have a higher, slightly higher expense ratio. So it's a similar story that we look at it in totality, and there's going to be movements between the components.

Marc Joseph Roland Grandisson
CEO, President & Director

Correct.

Michael Wayne Phillips
Morgan Stanley, Research Division

Okay, that was great. I guess if I could drill a little bit further down from your commentary in the press release on the reinsurance development. You talk about short-tail business in the recycling years -- or recent underwriting years and then the longer-tail. The longer-tail piece of that -- the longer-tail business from earlier underwriting years, can you talk about kind of where that is, not just in years, but I mean, the sub-segments, the lines of business that were driving that longer-tail business favorable development?

François Morin
Executive VP, CFO & Treasurer

It's mostly all in the casualties subsegment of the reinsurance -- certain line of business in the reinsurance segment. As you know, we had a fairly sizable part of our business or market share proportion -- a proportion of our production was in casualty businesses, casualty business in the early years of Arch, going back from 2002 all the way to 2008 and '09, let's say, where we reduced our writings in that particular line. So you're still seeing some favorable development coming through from those years in casualty in particular.

Marc Joseph Roland Grandisson
CEO, President & Director

What I would add to what Francois just said is in the earlier years, it was mostly -- we included in the casualty segment general liability and professional lines. In the early years, we wrote a lot more GLs, more -- in proportion than we've written recently. So I would think that the more recent releases will come from professional lines, treaties that we've done, and the early years still giving us some release of -- from the casualty or the traditional GL portfolio that we wrote as far back as 12 to 15 years from now. We are -- obviously, we have deemphasized that line of business very heavily over the last 10 years.

Operator

Our next question comes from Josh Shanker from Deutsche Bank.

Joshua David Shanker
Deutsche Bank AG, Research Division

Can we talk about the production in MI and how much capital that required on the margin from where you were a year ago? And so when we consider the share repurchase and everything and there's maybe a little bit of stagnancy in P&C, how much excess capital are you guys generating per quarter given the consumption elsewhere?

Marc Joseph Roland Grandisson
CEO, President & Director

I think that -- well, you can see our earnings coming through, right? And the one thing I will tell you, I don't want to tell so much because there's a couple of things moving in production, the way it flows through the portfolio, the Bellemeade transaction that we've put together -- that we're putting together on a program-managed basis, the roll-off of the capital from that, that we are experiencing and benefiting from pre-2008, the claims that are actually rolling off even, as François mentioned, on the curing and delinquency. And frankly, Josh, they're all pointing in the right direction, which is we are -- and that partly helped to inform and fill helped -- helps us inform our view about how good and how much the fundamentals -- how good the fundamentals are in the business. And I think that we have -- we made decisions in the past. We certainly have committed to embark on that Bellemeade transaction. They're very, very good for us in protecting the downside. They're allowing us to deploy capital in future periods. And hopefully, we get more excess capital as a result. But we are not running out of ideas in the MI segment. So if anything, we're very happy with our production and happy where we are. And if the efforts just keep on being the same as we've seen now, we're going to keep on deploying capital there.

François Morin
Executive VP, CFO & Treasurer

The one thing I'll add to that, just as a counter to excess capital, is actually persistency is actually trending up. And with higher interest rates, as you know, we would expect they will have a bigger book, the book sticking longer on the balance sheet, which does rewire the capital. So it's hard for us to know when to say exactly how much excess capital we're producing on a quarterly basis. It's certainly something we look at, I want to say, after the fact, not before the quarter starts. But that's certainly an important part that we have to be aware of is, we think the book will stick around for a bit longer. That just triggers capital requirements that we need to be aware of.

Joshua David Shanker
Deutsche Bank AG, Research Division

Well, let me ask the question another way then, and I'm not complaining about $170 million of share repurchase. What tells you, okay, let's stop? Like, how do you know that -- how do you get your fill and decide that you had done enough? Or I mean, was it just like you would -- where you closed out? What was the trigger that you knew how much you wanted to purchase at what time? I guess is what I'm asking.

François Morin
Executive VP, CFO & Treasurer

Well, some of it's the price, some of it is the closed window. So we certainly bought back some stock early in the quarter. Come June 15, we have to implement a 10-b5 plan. We set some guidelines in place. We pass them onto the broker, and we have to just watch from the sidelines and see what they're going to execute on that. So we gave them an authorization, they field it -- I mean, they work with the parameters of the 10-b5 plan, but I don't want say it's a black-and-white line on when we stop and when we keep going. And the other thing you've got to remember is we also wanted to reduce our leverage. So we paid down $250 million of the revolving credit facility, which is one of our objectives as well. We want to bring down the leverage. We want to regain the flexibility we had before the UGC acquisition. And so those are really 2 things that go hand-in-hand that we want to manage through, and we think we're on the right path.

Operator

Our next question comes from Nick Iacoviello from Dowling & Partners.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

It's actually Geoff Dunn. I wanted to revisit the MI capital question. Your cushion is, by far, the biggest in the industry right now. And given your comfort with 2.0, what is the prospect for dividend out of that platform in the back half of the year?

François Morin
Executive VP, CFO & Treasurer

It's something we look at. No question that we did declare ordinary dividends in the first half of the year, which helped us, again, reduce or deleverage, pay down the revolving credit facility. We are also -- there were restrictions, as you know, with the state regulators that there is only so much we can dividend out. So if and when we get to a place where we have to -- we want to extract more capital, we may have to go down the route of extraordinary dividends and/or return of capital, which, as you know, will require regulatory approval. So it's certainly part of the equation, but -- and the other thing I'll add to that, which is a bit of influx is, we're still realigning our legal entities with the merger of UGC and Arch MI. There's a bit of more actions we need to take place, that we need to put through there just to have a bit -- a more optimal capital structure within our U.S. regulated entities in the mortgage space. So it's all being considered. We don't have a hard number at this point. But we're actually -- it's something we look at quarterly with the local board, the local management team, and it's part of the overall capital plan at ACGL.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

Have you submitted a special dividend request to your state regulator?

François Morin
Executive VP, CFO & Treasurer

Earlier this year, we did, and it was approved and it's something -- again, there is a frequency of interactions you want to have with the regulator. We can't go to them. We've got to manage through that, but it's certainly something we want to have a fairly systematic way of going and reaching out to them with definitive, I want to say, views on how the capital requirements -- what they see as capital requirements from their own -- the state regulators versus PMIERs. There's also differences in how much credit we get for the Bellemeade transactions that come into play. So there's a lot of factors that we're working through. But we don't have a definitive plan of action, I'd say, for the remainder of 2018 to go to them at this point.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

Okay. And then 2 questions on the production. First, your 97 mix has been coming up a little bit -- fourth quarter, first quarter and then more materially this quarter. Is there anything that's changing on the underwriting basis in that segment that's making you more comfortable? Or was the -- particularly, this quarter has gained more due to the unusual pricing that you highlighted before.

François Morin
Executive VP, CFO & Treasurer

Right. So from our perspective, our belief is that we didn't change rightfully our view of pricing and risk and our appreciation of those risks. It's probably because the rest of the competition probably put some more extra layers on this, and that probably mean that we won a little bit more in that segment. So we increased our share, but, Geoff, as you know, we are still underweight versus the rest of the marketplace. And as you know as well, I need to tell you, the production of LTV above 95, that's grown in the industry. So we also are on the receiving of this. And it's hitting -- and as the production increase in that segment, there's probably more and more ability to charge or price to take on the risk.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

Okay. And then lastly, you mentioned a couple of large deals in the quarter. Are you referring to kind of these pool deals where you're quoting on a pool of whole loans in the aggregate?

Marc Joseph Roland Grandisson
CEO, President & Director

Yes, and pre-agreeing it's a forward commitment. Yes.

Operator

And our next question comes from Bob Glasspiegel from Janney Montgomery Scott.

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

I just wanted to dig into the insurance segment. You've now had 3 quarters where you've eked out a small underwriting profit. And if you adjust -- even if you adjust for the luck, you are hitting the tougher cat third quarter. But you talked pretty optimistically about the -- sort of the environmental changes. Do you think the work you've done in the environment are sufficient that you can actually get to an underwriting profit looking out forward and start to approach your targeted returns in that segment?

Marc Joseph Roland Grandisson
CEO, President & Director

We're certainly working heavily towards that. Bob, I think you know us. We're trying to work towards that. I think we've always worked towards that level. I think that we're probably not as -- I just want to put a little caveat to what you said. And I think we're cautiously optimistic as to what we see in terms of margins improving. And I think that it will take us sometime. We have some improvement. I think some of it in our loss ratio, but as François mentioned, some of it is due to mix. In terms of returns, we have seen some improvement in returns, but we are not declaring full victory yet. It's going to take us a while to really see the results coming through. But suffice it to say that there's been an active shift between the businesses that has been going on. And this is not of late. So what you see right now on insurance, as you know, Bob, is really the sum total of things you've done over the last 1.5 years to 2 years and we're seeing right now in a reallocation to higher-return lines of business. And we're hopeful that this is the level that will continue and even improve in the future. But the future -- only the future will tell us what happens.

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

François, do you have handy either new money rate for the quarter or current new money rate that you're investing it?

François Morin
Executive VP, CFO & Treasurer

Well, we're actually -- new money rate on the corporates, actually 2% to 3% in the last few weeks. So that's good news. That's -- that will help the investment income going forward. But yes, we're right about like 3.1% in the last 20 days-or-so.

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

That's well above your embedded yield. So investment income, as you said, should continue to accelerate?

François Morin
Executive VP, CFO & Treasurer

Yes. Yes.

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

And last question, was the tax rate guidance full year or second half?

François Morin
Executive VP, CFO & Treasurer

Full year.

Operator

And our next question comes from Meyer Shields from KBW.

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

Marc, when you started your comments, you mentioned that rates are a little bit above loss trends. I was hoping to see whether that's the loss trends that you're currently observing or the longer-term loss trends that you've been baking into pricing and reserving?

Marc Joseph Roland Grandisson
CEO, President & Director

Yes, okay. So it's a bit of both. The -- whatever we use in our loss trend is informed by the data, obviously, and our future expectations. The delta is not significant. It's 150 or 125. But Meyer, it's been only -- that margin has only been -- it's a quarter or 2 effect. It hasn't been a consistent pickup in trend or in rate over loss trend that we would expect to really start growing the book of business. And so it's a very -- it's an art more than science at this point in time, specifically for the more recent accent year. It takes a really long time to have a clear view of what's happening. And frankly, we won't know until 5 or 10 years from now. What we're looking for more is margin of safety between the loss trend and the rate change. And this clearly is not -- we don't believe it's sufficient enough at this point in time in most lines of business. In some lines like property, we are clearly getting way above trend, and that helps inform our position in allocating capital and getting a more and better assurances that our ROE expectation is going to be there and we're going to be able to meet it.

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Related question on the casualty lines, are these -- I guess, different views from different executives right now about whether there is an uptick in claim frequency in a lot of casualty lines. And I was hoping you'd tell us what you're seeing.

Marc Joseph Roland Grandisson
CEO, President & Director

What we're seeing, frequency is not increasing dramatically, but we're not seeing it decreasingly. And the problem with frequency, Meyer, that -- you're an actuator, you know that as well as I do, is that the frequency is a look back estimate. It takes a long time for the true losses to emerge. So we have seen some rate frequency decreases. I would be of the mind and most of us at Arch would be of the mind that some of it is due to looking back to a lower economic environment, lower activity over the last 10 years and carrying on during that projection in the future. I'm reminded of the workers comp years of '93, '94, '95 when things were being extracted, frequency being done very heavily, and it's just a matter of time before it starts picking up again. And in other line of business, our more recent experience is auto liability. It was looking pretty good on frequency, and the frequency shot up over an 18-month to 24-month period. So I'm worried about the false sense of security of ongoing frequency decreases, especially in the light of an economy that has a lot of fiction, a lot of pickup in it, a lot of steam in it.

Operator

And our next question comes from Brian Meredith from UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

A couple of questions. First one, just curious, the pickup in property business you're seeing on your insurance side. I know you talked about some of that's rate but then also adding some new business there. What do you see is the attraction right now in the property business? Is that the area you think that rates well in excess of trend? What's going on there?

Marc Joseph Roland Grandisson
CEO, President & Director

So rate, yes. We believe rate is an excess of trend. There's also -- so the rate on our E&S portfolio, which is -- it's mostly in the E&S portfolio play, right, Brian? It's not the global property side or the small commercial that -- we've seen some of it in certain areas. But by and large, the ones that have, well, E&S in nature, including the [loan loss] business. We're seeing rate increases because of dislocations in the marketplace. Some players have been hurt a little bit. There's been some question as to whether that's a viable book of business. So there are opportunities to slide in and are able to seek opportunity. On the reinsurance side, because I want to mention that as well, Brian, it does matter, there are also opportunities that arise because of some placements not being finalized, and we're able to pick and choose some cycle dated placement around -- just to complete the quilt of coverage that larger risks would have to do to place. So there's a little bit of a shrinking of capacity in this space, specifically on the E&S property. It's an 8% trend, 8% to 9% rate increase, but this is one lone area where we have -- we're seeing some terms and conditions getting better. Actually, working towards as an insurance carrier, so -- and as I say in my notes, we like to see rate increase going up one way and terms and conditions following. So meaning, giving us an extra kick up, and we believe this is what's going on in the property although it's not widespread. We have to pick in -- our spot, but it's certainly what we're seeing in the business that we write.

Brian Robert Meredith
UBS Investment Bank, Research Division

Great. And then my next question, Marc, at Investor Day, Nicolas talked a little bit about maybe some initiatives to try to get the combined ratio down in insurance segment, be it expenses, be it risk selection and stuff. Can you just maybe elaborate a little bit on what you're doing to try to consistently maybe improve that? Because I can't think the returns in your business or that crate when you're sitting here kind of 100 combined ratio, 99, 100.

Marc Joseph Roland Grandisson
CEO, President & Director

Correct. So it's -- we really identify this as an area of opportunity, but that will take years to develop. And the initial things that we've done and we're doing currently right now is there's a little bit more integration going on for some things such as IT, for instance, that we think we need to do and can be done even though we have multiple platforms. So it's a couple of things, integrating services, leveraging some of the overseas employees that we have that are in a lower-cost jurisdiction. And there's some initiatives that we're talking that will be -- we'll be working on going forward to try and decrease it. But I will tell you what happens when they happen, and we're going to give it to -- give us -- give ourselves some time to get there.

Operator

And our next question comes from Ian Gutterman from Balyasny.

Ian Gutterman
Balyasny Asset Management L.P.

So first, François, thank you for doing the script in a slower cadence than we're used to, that was helpful. So my first question is just a follow up on the tax. Can you talk specifically about why it's coming in lower than you expected for the year?

Marc Joseph Roland Grandisson
CEO, President & Director

Well, 6 months have gone by. I mean, no question that when we started the year, it was -- there was a lot of uncertainty after the tax reform, trying to figure out -- it was all based on plan. So when we gave you the estimates back in February, it was all related to where we saw the profitability of the units and what local jurisdiction they'd come from. 6 months have gone by, and now we have a bit more clarity on the actuals, and that's what we were just updating. So I hate -- I can't pinpoint any one particular thing on why it's come down a couple of points, let's say. It's really more just the fact that we've replaced forecast or plan with actuals.

Ian Gutterman
Balyasny Asset Management L.P.

Okay. I guess I would have thought -- I guess I can turn to my model, not your internal model, obviously. But I would have thought that the upside in earnings has come more from MI, which obviously, would be more in the U.S. So I would have thought, if anything, like the geographic mix would have biased you higher, if anything. So I don't know if there were other actions you were taking to try to offset that or...

Marc Joseph Roland Grandisson
CEO, President & Director

It's not a big difference. The 21% of tax rate, we get a 50% quota share on the mortgage book. So that brings it down to 10.5% right there. It's -- there's -- and we can do it offline. There's a couple of other things that are, I think, one-offs that kind of move it in different directions. So it's really hard to kind of give you a lot more clarity over this range at this point.

François Morin
Executive VP, CFO & Treasurer

And this is a primary U.S. business. And just for your benefit, some of it in the U.S. segment is also written out of Bermuda, which would have a different tax code.

Ian Gutterman
Balyasny Asset Management L.P.

For sure.

Marc Joseph Roland Grandisson
CEO, President & Director

Yes.

Ian Gutterman
Balyasny Asset Management L.P.

Okay. And then can you give us some color on the cat losses? I mean, the dollar amount was about similar to last year, but I assume that's a coincidence. Is it coming from the same parts of the book though? Or is it different parts of the book or different geographies? Any color you can you give us on what happened there?

François Morin
Executive VP, CFO & Treasurer

It's different. It's a one-off. It's a one class of business that we had unfortunate -- what I mean, one major event that came in through the quarter. We don't see any trend in it. It's really -- I mean, yes, it's a coincidence that it's happening in the exact same quarter 12 months later. But other than that, again, as Marc said, we've been very happy with the performance of that book over the years. No question that we're going to look into it some more as we move forward. And does that force us to reevaluate some underwriting decisions? But at this point, we don't see anything that's really problematic.

Marc Joseph Roland Grandisson
CEO, President & Director

No. And that loss versus last year, they are different in nature. I mean -- exactly. It's very different in nature. I mean, it's a fire loss, but it's different types of risk, different types of characteristics, different coverages of sort, again, very different -- like different occupancy and that -- yes, we -- it's a very lumpy book of business, as you know, Ian. We are sitting here having q-on-q loss, we could have 5 quarters with no losses.

Ian Gutterman
Balyasny Asset Management L.P.

Okay. Was this the fire that I would have maybe read about in the press somewhere that happened, call it, on the island near Europe?

Marc Joseph Roland Grandisson
CEO, President & Director

No, that was not that one.

Ian Gutterman
Balyasny Asset Management L.P.

Okay, okay. And then maybe just for -- if I think about, say, the full year '17, in fact -- I mean, obviously, there was the bad Q2. But I'm just trying to sort of think about like what's normal over the course of the year. But last year, all-in have been a normal year? A worse than average year? Just how should I think about that?

Marc Joseph Roland Grandisson
CEO, President & Director

Last year has been a worse than average year. I'm not -- I don't -- I'm not comfortable giving you what we think the long-term pricing and returns are. We want to keep it proprietary, but it's showing a very healthy, very profitable book of business. But last year, yes, for -- in the 11 years that they have been writing business for us, well together, it's the 1 year that's fixed out. Everything has been actually below the long-term expected among all years, except for that one last year.

Ian Gutterman
Balyasny Asset Management L.P.

Okay. I was just trying to think about volatility like given there's 2 years in a row with aid back quarter, would it be normal to have a quarter like this once every -- probably not once every 4 quarters, once every 8 quarters? Is it once every 5 years? I'm just trying to get a sense of sort of how unusual the last 2 Q2s are?

Marc Joseph Roland Grandisson
CEO, President & Director

It's a very good question, Ian. I don't know the answer to that.

Ian Gutterman

Balyasny Asset Management L.P.

Okay. Fair enough. And then just quickly on mortgage. You talked about the environment being healthy, and obviously, that seems fairly obvious. But I guess sort of the incremental news maybe over the last months it feels like there's a little bit of softness emerging. I don't know if that's maybe more at the high end, which wouldn't have MI, than the broader market. But are you seeing any signs of that? Or -- it feels like that maybe prices have just gone up a little too fast in certain geographies where affordability has become an issue.

Marc Joseph Roland Grandisson
CEO, President & Director

I wouldn't describe the market as being softer. I would tell you though that the types of risks that find their way to the MI purchase market have a little bit of -- the credit is a little bit wider than it was possibly 3 or 4 years ago. And it's just the nature of the business and the business that we're in. The rates are increasing. There's less refinancing. There's more first term -- first time home buyers, and there's house price appreciation. So there tends to be higher LTVs, and more first-time homebuyers. And that's -- but it's just the nature of what they are. But I would believe that -- and I think the market can certainly, from our perspective with RateStar, we believe that we're pricing appropriately for those risks.

Ian Gutterman
Balyasny Asset Management L.P.

Yes. For sure, yes. I was just wondering about -- yes, if on the margin, the affordability was impacting credit at all. So it doesn't sound like...

Marc Joseph Roland Grandisson
CEO, President & Director

Affordability is actually 15% above the long-term trends. So affordability is still decent. It's not all created equally in all cities, like San Francisco, and in the country. But certainly, affordability, it's still there. The DTI equivalent is about 26. So it's not that bad. It's probably good still.

Operator

And our next question comes from Yaron Kinar from Goldman Sachs.

And I am showing no further questions from our phone line. I would now like to turn the conference back over to Mr. Grandisson for any closing remarks.

Marc Joseph Roland Grandisson
CEO, President & Director

Thank you, guys. Welcome, François, to the call. And we look forward to talk to you after the winter season. Thank you.

Operator
Ladies and gentlemen, thank you for participating on today's conference. This does conclude the program. You may all disconnect. Everyone, have a wonderful day.