S&P Global
Market Intelligence

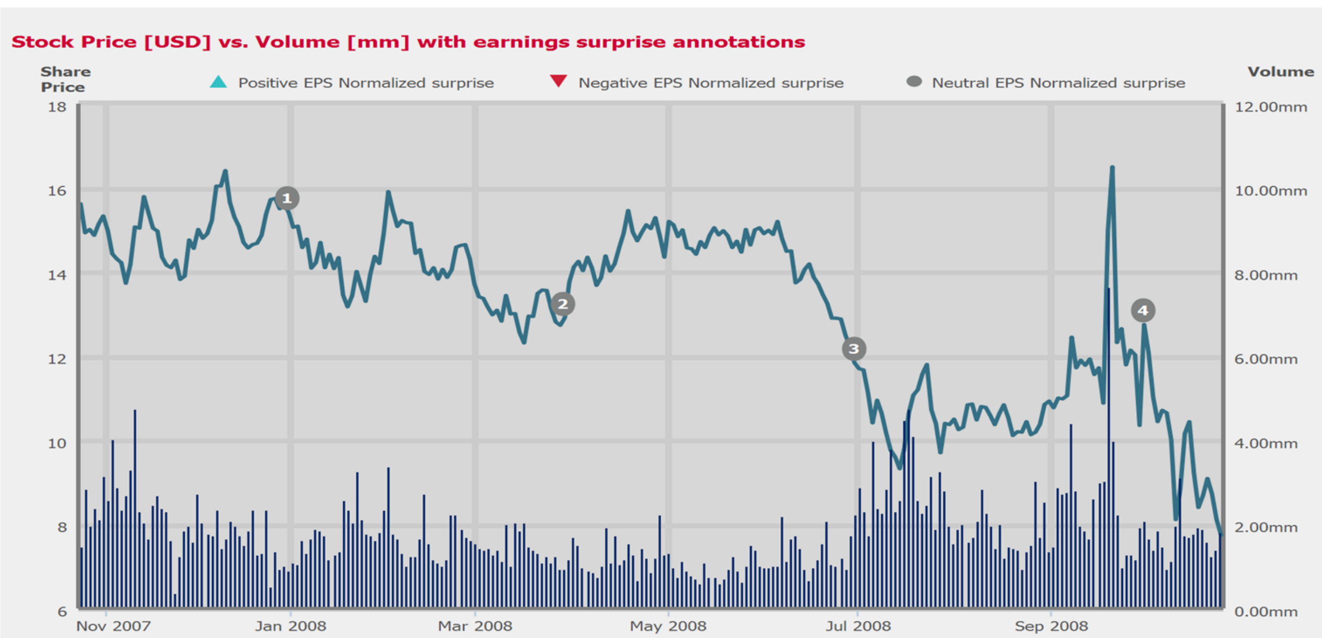
Old Republic International Corporation
NYSE:ORI
FQ4 2008 Earnings Call Transcripts

Thursday, January 22, 2009 8:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2008-			-FQ1 2009-	-FY 2008-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	(0.25)	(0.31)	NM	(0.28)	(0.75)	(0.81)
Revenue	-	-	(4.22 %)	-	-	-
Revenue (mm)	939.30	899.70	-	937.00	3764.00	3721.20

Currency: USD
Consensus as of Nov-21-2008 9:25 PM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ4 2007	0.09	0.09	1 0.00 %
FQ1 2008	(0.02)	(0.08)	NM
FQ2 2008	(0.16)	(0.22)	NM
FQ3 2008	(0.16)	(0.20)	NM

Table of Contents

Call Participants

EXECUTIVES

Aldo C. Zucaro

Christopher S. Nard

Leslie Loyet

ANALYSTS

Daniel Johnson
Citadel Investment Group

David Lewis
Raymond James & Associates

Kevin Preloger
Perkins Investment

Matthew Goetzinger
Fiduciary Management

Mike Grundall
Key Colony

Stephen Mead
Anchor Capital Advisors

Presentation

Operator

Welcome to the Old Republic International fourth quarter 2008 earnings conference call. (Operator Instructions) Now I'd like to turn the conference over to Ms. Leslie Loyet of the Financial Relations Board. Please go ahead.

Leslie Loyet

Thank you all for joining us today for Old Republic's conference call to discuss fourth quarter and year end 2008 results. This morning we distributed a copy of the press release and hopefully you've all had a chance to review. If there is anyone online who did not receive a copy, you may access it at Old Republic's website at www.oldrepublic.com or you may call Han Huie at 312-640-6688 and she will send you a copy immediately.

Please be advised that this call may involve forward-looking statements as discussed in the press release dated January 22, 2009. Risks associated with these statements can be found in the company's latest SEC filings. With us today from management we have Al Zucaro, Chairman and Chief Executive officer and Chris Nard, President Old Republic Mortgage Guarantee Companies. At this time I'd like to turn the call over to Al for his opening remarks. Please go ahead.

Aldo C. Zucaro

Thank you, Leslie and we'll proceed real quickly with some commentary on this morning's release and then, as Leslie just said, we'll open it up to your questions. Again as she said Chris is on the line with me out of his Winston Salem office and he will come on and participate in the question and answer portion of this call.

The news in the morning's release was not much different in terms of operating trends and bottom line results than what we've posted for the most recent quarters. With the end of last year's fourth quarter, unfortunately we've now reported six consecutive quarters of negative bottom line performance at Old Republic and as we indicated at the top of this morning's release, it is I would say more likely than not that we'll be experiencing a repeat of this less than stellar performance for another four to six quarters before more positive consolidated earnings trends can emerge.

All of this, of course, will be due to the continued difficulties we foresee for our mortgage-related businesses of mortgage guarantee and title insurance. In the fourth quarter of last year as well as the full year 2008, as you see in the release consolidated operating results continue to benefit from reasonably good underwriting and investment income contributions by our general insurance business.

But as you can also see the performance in the mortgage guarantee line worsened to some degree, and the same thing happened to a much smaller degree in our title insurance segment where the last quarter's earnings downturn was magnified to some degree by the usual slow production that befalls that business in the fall and winter of each year.

As well as the higher provision we've mentioned of about $6 million as I recall for various class action type of litigation exposures we have in that segment and that we reevaluated as of year end. Focusing on general insurance, we experienced some slippage in underwriting profitability in both the final quarter as well as the full year when we compare those periods to 2007.

At the beginning of 2008, some of you who follow us may recall we suggested that our general insurance segment would likely produce underwriting results within a composite underwriting ratio range of about 95 to 98%, and as you can see the actual composite was a shade above 97% for the entire year.

I would say that the increase in last year's underwriting ratio was driven mostly by our consumer credit indemnity coverage with general aviation providing a much smaller uplift to the ratio, if you will. As we've noted before in past conference calls, the Consumer Credit Indemnity or CCI product line, as we refer to it internally which currently represents about 10% of our general insurance earned premium base, is producing by far the worst underwriting results we've experienced in the 50 plus years that we've offered this product.

Last year the line added, by way of reference, it added nearly 400 basis points or 4 percentage points to the general insurance segment underwriting ratio whereas its affect on the same ratio for all of 2007 was negligible. The line, as the name implies, is tied to consumer borrowings for purchases, such as home improvements and expenditures that are financed typically with second liens on home ownership.

And therefore, as you might expect, the CCI underwriting experience is being impacted by the over abundance, one might say, of the very stressed credit conditions that are currently effecting the American economy.

We currently expect that the underwriting trend line for this product will probably mimic that of the mortgage guarantee line because, again, of its relationship to the credit finance business of this country. Its dollar impact, however, on our results should be and have been a lot less due to the much smaller size of this line and the different pricing and underwriting considerations that apply to it and have so applied for many years.

All in all, the majority of general insurance coverage has delivered flattish to moderately better underwriting results, and in total those results overcame most of the damage from the CCI claim costs in particular.

The investment income in general insurance slipped a bit in 2008 and that was due to the lower dividend income on our relatively small amount of equity holdings, and a somewhat reduced or flattish yield on the aggregate of our long and short-term fixed income securities.

As we point on in this morning's release, this group of companies delivered still very positive cash flows for the year, though the cash flow was at a lower level than had been the case in 2007, which I think I recall was probably the highest cash flow year we've ever had at Old Republic.

While we have not buttoned down our budget for 2009, we do have some reasonable clarity about the likely course that our general insurance business will follow, such that absent any acquisition of a book of general insurance business, which is always a possibility though I've got to say we don't have anything on the burner as we speak, we're basically looking at a more or less level earned premium line for 2009 in this segment.

We may deliver a little bit more than that by virtue of some tinkering we continue to do by reducing purchases of reinsurance coverage, but the fact is that we have enough capital in our general insurance business to increase the amount of risk we carry, and thus the tinkering of referring to relative to our retention levels, which as you know have the impact however small it might be of increasing the earned premium line.

Underwriting wise in general insurance, we feel reasonably confident about delivering an underwriting ratio within the bounds of let's say a 96 to 98% level in 2009. Our comfort in this respect is based, I would say on the overall feel that we have, that the pricing that's baked for all intents and purposes into the business currently in force should not show significant deterioration as that business earns out throughout the year.

And also we feel that renewals will likewise occur with very little, if any, material price or terms of trade concessions. And finally we continue to believe, as exemplified by our continuing posting of reserve adequacy, that our claim reserve structure is sufficiently strong as to preclude any meaningful adverse development and, therefore, no incursion into the current year's profitability.

Turning to our mortgage guarantee business, it obviously continues to run a pretty high fever on the claim side of the ledger. The more accentuated than earlier expected trends in loss emergence as well as severity patterns in this business unfortunately are leading us to eat some humble pie.

And by that I mean that for several quarters since mid-year 2007 we had convinced ourselves that this business would produce a cumulative loss ratio of about 150% on total mortgage guarantee premiums for the 30-month period stretching between mid-year 2007 when, as you recall, housing and finance began to fall out of bed and year end 2009 or a 30-year period as I say.

As matters currently stand for just the 18 months that have already transpired through year end 2008, the cumulative loss ratio in mortgage guarantee has already reached approximately 190%. So as we look at the world through this latest set of numbers, it is not inconceivable that performance of the book can still show improvements during the second half of 2009.

But this can happen only with a very gradual unclogging of the country's lending pipeline and with the ultimate beneficial affect of all the foreclosure stemming and loan modification initiatives that have been factored into various incendiary U.S. government as well as private sector activities in all these regards.

But our current view, nonetheless, is that all of these positives will require a longer period of gestation before a more benign state of claims activity occurs, and for the beneficial affects of the better underwritten and better priced product of 2008 and 2009 for sure for that better priced product to kick in and begin to offset the damage of the business underwritten principally in the years 2006 and 2007.

So the short of it is that the cumulative MI loss costs for that 30-month period are more likely than not to gravitate toward the 200% mark rather than the 150% level that we had contemplated starting as I say around fall of 2007. At least that's our best guess at the moment as to how loss costs will shake out in mortgage guarantee before there is any kind of resumption of a more stable situation.

The type of outcome that I'm just describing in mortgage guarantee has obvious repercussions on the capital levels we have been committing to this business. Everyone that's familiar to any degree with the mortgage guarantee industry knows that there are certain regulatory guidelines that all MI companies need to observe when it comes to minimum capital requirements for a mortgage guarantee insurer with an active book of business.

And while there isn't total uniformity among the various states that regulate mortgage guarantee companies, the generally observed guidepost is for insurers to run the business at a 25 to 1 risk to capital ratio. That's the maximum ratio. For our part, we've previously said that our game plan was to run the segment with a statutory ratio ranging between 17.5 and 20 to 1.

As you can see in the statistical exhibits and the footnotes that are appended to this morning's release, you can see that that ratio stood at 17.6 to 1 or 16.4 to 1 at year end 2008 depending on the alternative calculation methodology followed in determining what true risk in force is, or was I should say, as of that date. Incidentally, those year end 2008 figures that I just mentioned do reflect a capital addition of about $150 million to our mortgage guarantee group of companies as of December 31, 2008.

So, based on our current expectations relative to the loss ratio trends we've just mentioned and given the assumptions we are currently making visa vise 2009 new business production as well as persistency rates, which we estimate, will likely be in the mid 80's. We think it is more likely than not that our mortgage guarantee risk to capital ratio will cross over the 20 to 1 mark and nudge itself more closely to a 25 to 1 level as year end 2009 approaches.

And to stay within that 25 to 1 level and absent the utilization of several controllable variables we have at our disposal, such as reducing our intake of new business in order to mitigate the impact of a growing book of risk in force, we currently believe that we need to add between $50 go $100 million to the MI segments capitalization by year end 2009, again, as I say based on our assumptions as to the likely course of events as it applies in particular to loss ratios, premiums levels, persistency of the business, etc., etc.

I would say that at $50 to $100 million that's something that we should be able to do with relative ease and without undermining in any fashion the capital structure of our general and title insurance businesses. Suffice it to say that for the foreseeable future and until the dust settles, our clear intent is on managing our mortgage guarantee risk and capital structure with a sole and primary focus on meeting our just obligations to policyholders rather than being proactive in securing market share growth.

On that score incidentally when you look at our numbers quarter-to-quarter you will see, as is the case I suspect with our mortgage guarantee competitors, that the amount of business that we've put on the books, new business I should say, has been somewhat declining particularly since the second quarter of 2008.

And as we indicated in the press release that to a large degree is a reflection of two key factors affecting the business and that is one, the much more stringent underwriting standards that are being applied by both the GSEs as well as the mortgage guarantee insurers as well as the fact that the FHA is making a dent in the insurable loan volume that there is out there.

So managing the business in that fashion, as I say of managing good capital in the business, with a clear focus on our primary policyholder obligations, we think that that's the responsible thing to do for the best interests of existing policyholders first and Old Republic's shareholders secondly.

Turning to our title business, not much needs to be said in addition to what we've already indicated about the impact of housing and mortgage lending issues on any business that's related to those industries. From an earnings standpoint, the title segment is likely to idle within range of the bottom line results we've posted for 2008.

It's not out of the question, however, that our title insurance group could pullout of the doldrums somewhat earlier than mortgage guarantee since, as you know, title premiums and fee revenues respond very quickly to any uptick in housing sales and mortgage lending activity.

There is also, of late, in the last couple of months or so a silver lining emerging in the form or greater refinance activity and as you might well suspect that's due to the recent evolving downturns in mortgage rates, which for qualified borrowers allows a refinancing of loans at better terms.

We do not, however, expect this refinance activity by any means to reach the fever pitch refinancing levels that we experienced several years ago, but nonetheless it should be of some beneficial effect on our title business.

Consolidated wise, we've included the usual shareholders equity per share reconciliation at the tail end of the release, and the reconciliation of course brings together all the elements of our business activity into very clear focus. And as you can see just about half of the equity loss last year came from bookkeeping entries to record mark-to-market impairment adjustments as well as market value allowances related to our bond and principally equity investment portfolios.

Again as we indicated in the release, the lion's share of the bookkeeping adjustments stemmed from the significant holdings we have in the two largest mortgage guarantee insurers in the nation, and while this was a painful accounting exercise it is redemptive, I think, to consider that those investments have been written down to a level not very much north of zero so that any further market valuation decline would not result in as bitter a medicine as we've already gulped.

These elements aside, however, Old Republic's balance sheet retains a great deal of staying power and is very sturdy and is going to see us through this downturn in the housing related area. The quarterly cash dividend payout has been kept at the higher rate we announced back in February of 2008. As we have said often, we look at this rate every quarter in conjunction with our board meetings and the next time we visit this matter we will be in late February of this year.
That's the extent of the additional overview commentary we were prepared to make this afternoon. So now, as we indicated beforehand, Chris and I will take your questions as they come.

Question and Answer

Operator

(Operator Instructions) We'll take our first question from David Lewis - Raymond James.

David Lewis
Raymond James & Associates

Thank you for your comments and thoughts on the outlook. It was very helpful. I want to make sure I'm clear. If you're going to pull back in the MI new business does that mean that we may actually see the premiums start to shrink on a year-over-year basis? Would that be your expectation or more of a flattening out?

Aldo C. Zucaro

No. I think the implication of what I said, or tried to say, was that one, the business inherently has slowed down for all of the mortgage guarantee companies, including ourselves. I mean you have differences among the companies but still the production of new business has been on a downtrend for the last nine months I would say as I recall of 2008.

And perhaps the other thing you're referring to, David is the fact that I indicated that one of the instruments we have at our disposal is to not accentuate as much on production in order to better control risk enforce and, therefore, the capital allocations we have to the business.

David Lewis
Raymond James & Associates

I guess I'm surprised given your low debt to capital ratio that you wouldn't look to maybe take down some debt to continue to produce the more favorably underwritten mortgage guarantee business.

Aldo C. Zucaro

We still have that in mind. I'm just suggesting that's just one of the alternatives we have and certainly not the only alternative.

David Lewis
Raymond James & Associates

Couple of questions from a clarification standpoint there's been a lot of talk within the bankruptcy judges on the cram-downs and I guess I am curious if a cram-down occurs does that come back to you in the form of a claim or do you share some of that with the financial institution or how does that impact you?

Aldo C. Zucaro

Yes. I'm going to ask Chris to answer that question.

Christopher S. Nard

Sure. Hey, David. The way that works is if in fact you had a change in the system whereby bankruptcy judges could cram-down a loan amount that does not generate a claimable event for us. So if the judge were to write a loan down from 250 to 225 you can't file a claim for the $25,000.

What we will do though is the policy stays in force at the higher amount, so in my example while you'd now have a new loan at $225, 000 the coverage would remain in force for the $250,000. We'd collect slightly less premium on the new loan amount so you could think about that as a contribution in essence to the cram-down.

David Lewis
Raymond James & Associates

So do you anticipate that some of the new cram-down rules for the bankruptcy judges will have much favorable impact? It can't hurt obviously, but I guess what I've heard is some of these restructure loans may prolong the alternate situation.

Christopher S. Nard

Well, I think where we are and I saw some things yesterday and I don't know if you're seeing something new today, but I think as of yesterday that the cram-down provision was not going to be in an Obama stimulus package right out of the gates. I don't if that's in fact still true today but that aside, will it prolong?

I don't know, but generally if you have a borrower who has shown some willingness and an ability to stay in the house and the bankruptcy court judge rewrites the loan amount, and generally that should be positive for us in so much as now the borrower has a fighting chance and an incentive to stay into that house because the loan's been written down to current market values.

David Lewis
Raymond James & Associates

Al, back to you kind of the outlook in the mortgage guarantee loss ratio, would you expect that it probably climbs through maybe mid-year and then we kind of reverse a little bit but still at high levels for the full year, would that be a good guess at this juncture?

Aldo C. Zucaro

Yes. I would say so. I think Chris and I are in agreement that that could be a likely scenario, but then again as I tried to indicate in the overview comments that I just made, it just takes time for all these positive inputs from the fed, the treasury etc., etc. to take hold and, therefore, I would have to hedge the comment by saying yes by mid-year you should start seeing the light at the end of the tunnel but it could be the fall or what have you, but I think 2009 overall from a loss ratio standpoint is a cooked goose.

Operator

Your next question will come from Dan Johnson.

Daniel Johnson
Citadel Investment Group

Al, can you speak a little bit about the captive relationships with the banks, what's going on there, how many have continued to fund as normal if they've gotten to that point versus how many have been, I don't know what the technical term is, but sort of wound down, if you would please.

Aldo C. Zucaro

Chris, why don't you speak to that?

Christopher S. Nard

Sure. Well, we got out of the captive reinsurance business for new writing several quarters ago so all we are currently ceding to captives are premiums on the in force books. We just simply made the decision to no longer continue with excess of loss captives. Obviously several of them are currently into their loss layers.

We don't have any except maybe one very small one as of this point that have totally pierced their layers, but certainly this continued stress in the market is beginning to push these guys up through their layers at this point in time. But again, we're not ceding any new business they are all effectively in runoff and, again, we haven't blown through any significantly sized capitals.

Daniel Johnson
Citadel Investment Group

And all of them, Chris, right are owning up to their obligations, right?

Christopher S. Nard

Yes. To the extent that there are funds in the trust accounts they are all continuing to operate as we expect.

Daniel Johnson
Citadel Investment Group

What do you think happens, or what have you heard from others in the industry that's already seemingly happening, with trust accounts that may need more funding from the banks? Should we count on them bringing their checkbook or are they going to walk away?

Christopher S. Nard

Well, I certainly can't speak for any of the financial institutions. While we might hope that they would honor their obligations, I think at this point it would be too early to tell.

Daniel Johnson
Citadel Investment Group

Is there any way you can give us a sense of, somehow to give a magnitude sense here as if we do end up in the 200 loss ratio scenario, which I believe is probably a net number. Would that put these banks in a position where we would have to count on them putting more money into the trusts?

Christopher S. Nard

Well, I don't know. When you sit here today and project these trust accounts out it's a difficult exercise because each one of them is full of different productions with different geographic concentrations, and each player had a different risk appetite so they're full of different kinds of risk. So it would be really difficult for me to give you a feel for what the ultimate exposure is because again each one of these some odd 40 or 50 trust accounts is going to be very different.

Obviously, if you had one that was heavily concentrated in California or Florida you're going to run a much higher percentage chance that you completely blow through them, but most of the big ones were reasonably nationally diverse in their mix.

Daniel Johnson
Citadel Investment Group

Finally, one last question, the claims ratio of roughly 220 on a net basis, if we were looking that on a gross basis…

Christopher S. Nard

We said 200 by the way, Dan.

Daniel Johnson
Citadel Investment Group

I'm sorry. In the quarter is now where I'm at, so I'm changing gears onto the quarter of about 220, where would that be on a gross basis?

Aldo C. Zucaro

I don't have, unless you have it, Chris, but I for one can say to you, Dan that the amount that we have recovered from the captives has been on incline fairly steadily throughout the year. As to how many points of loss ratio we've saved by virtue of those recoveries, I don't know, and as I say maybe you do, Chris?

Christopher S. Nard

No. I don't have it in front of me. My guess is it's in that 50 to 75 million range for the quarter.

Daniel Johnson

Citadel Investment Group

That's dollars, right?

Aldo C. Zucaro

Right. So you can divide that 75 let's say by the earned premiums for the quarter in mortgage guarantee and that gives you obviously the loss ratio effect.

Operator

(Operator instructions) Now we'll hear from Kevin Preloger - Perkins Investment.

Kevin Preloger
Perkins Investment

On the Land America that you owned, how much was that and did you sell after Fidelity announced the deal or where in the timeline?

Aldo C. Zucaro

That was about a $39 million investment on our part. It accounted for about 10% of the Land America shares outstanding. We wrote down the security as of December 31st and, as you may know or recall, Kevin that is pretty close to the date, I think Land America declared bankruptcy shortly before Thanksgiving last year.

Kevin Preloger
Perkins Investment

Were you guys still in when they declared, or were you out?

Aldo C. Zucaro

No. We owned and still own the stock. The stock has been written down in value as, other than temporary, diminution in its value. As you well know, there are a number of tax planning and other considerations that enter into an insurance company's, or financial institution's, determination as to whether it's going to take an actual hit, which is deductible in the tax return or just in bookkeeping entry, which is what we have done with that particular transaction.

Kevin Preloger
Perkins Investment

On a happier topic, looking out to the future, right now I know PMI and Radian are our competitors and if you throw in MGIC and Genworth into the mix your market cap is a billion more than the combined market capitals of those other four.

Discuss with me the opportunity for market share shift and if you're seeing any of that now, and especially over the next six to 12 months, particularly if you raise this extra capital and have that once we get to the end of the tunnel and the light at the end of the tunnel?

Aldo C. Zucaro

Well, the capital raising of course is going to be for us and I imagine it's going to be similar to other companies. The cap [inaudible] is going to be predicated on whether we can derive an appropriate return for the shareholders, and perhaps more importantly, whether we need the capital to support our existing obligations to assurance.

As to the lay of the land, based on the latest information we have we don't sense that there has been a significant shift in market share. I think MGIC day before yesterday indicated that theirs was at around 24, 25, which is about in line with what they were. We sense that Radian, another competitor, may be somewhat ahead and may have gained some market share however it's done it. With respect to the others, we don't know of any significant shift. Chris, you're better equipped to address that issue.

Christopher S. Nard

Here's what I would say. We think about this from a number of different aspects, one and probably most importantly, the period immediately after a terrible market is never the best period because if you had decided that, let's say hypothetically we had decided we were in a good position in the fourth quarter of 2007 and made a big run for share in 2008, we would have been building share in what is a market that continues to see declines in home price depreciation.

So we were very focused through the period on essentially keeping the share flat to slightly down, we obviously need to serve our customers, but we wouldn't want to aggressively build share during a period of decline in home prices, irrespective of how much the guidelines and the pricing had improved simply because the decline in home prices are going to be a continuing drag on performance.

And I think really we find ourselves in the same spot here early in 2009 that, as Al mentioned earlier, you're not looking to really dramatically grow risk in force at a period that's still under pressure. The only other thing that I'd add to that is we spend a lot of time thinking about lessons learned from this last risk cycle that we're going through.

And I think that one of the things is always to make sure that our MIC size is balanced against the rest of the Old Republic family to make sure that as a diversified financial institution all the pieces fit together and one does not overly large visa vie the rest of the institution, so all those go into planning for essentially market growth in the coming years.

Kevin Preloger
Perkins Investment

But it would seem that given your position and you have the ability, and I have no doubt you would be able to raise that capital. If your culvert right now you're going to have a hell of a time raising your capital and the same goes true with the rest of the industry.

Aldo C. Zucaro

Yes. But the point is, Kevin, what you're saying is all true, but I think what Chris just said at the tail end of his answer is also very true. What we have to keep in mind is that we are running a single business of insurance. Now true enough we have different pockets.

We've got a mortgage guarantee pocket by way of several insurance companies there, a title company in the pocket and so on and so forth, but the critical element that has gone into building Old Republic over its 85 year history has been just what Chris said, to make sure that you employ the diversification of risk by type, by amount, by geography, etc. in the organization so that no single risk or accumulation of risk defeats a very important principal of managing an insurance institution, which is diversification of risk, among two or three other key principals.

So that's what you have to keep in mind. If your focus is solely on the mortgage guarantee business well we're not game for that. We don't want to be just a mortgage guarantee company because, again as Chris just said, if there is any lesson to be learned from this debacle it is that diversification is critical. Whether you're a bank or an insurance company it's important and that's what our focus is on.

Kevin Preloger
Perkins Investment

But even that being said and I think in a normalized environment you guys were what 60, 30, 10 GIMI title?

Aldo C. Zucaro

In terms of our capital allocation, you're correct, but while I think of it before I forget it let me just throw in one other element into the equation, and we've said this before. The rhyme and reason for our investments in PMI and MGIC was an ability to in fact to not override the necessary diversification we had in the business, but to get a passive interest in the marketplace through pretty significant ownership percentages in those two companies, and we feel comfortable with that approach of a mix.

And so far as our mortgagee guarantee orientation is concerned, we feel comfortable with this mix of a 10, 11% market share direct controlled market share, and a 5 or 6% passive market share through those two company holdings. That's our game plan, Kevin, because otherwise what you say is true.

We have the wherewithal to build our mortgage guarantee business to fare the well, within limits of course, but that's not part of our business insurance management of the business consideration right now. It's never been, really.

Kevin Preloger
Perkins Investment

Sure, but given the landscape that you face and the position that you're in right now and the mortgages that are going to be written from here on out are going to be of much higher quality than what burned your competition.

Aldo C. Zucaro

Well, Kevin that's true but, again, listen to what Chris just said. This housing and mortgage lending situation in this country is still very much in disarray and I think Chris is entirely right when he says when it's in disarray you better lay in the weeds and when until things have got better prospects of making a buck.

Kevin Preloger
Perkins Investment

I agree with all that, but I guess my point is that now is the time when you lay in the weeds but you raise your capital and you're ready to pounce at the opportunities that you're going to have 12 to 18 months from now when things are better.

Aldo C. Zucaro

Yes. But I don't need to tell you, Kevin not to belabor the point that that's easier said than done as well, right? Because while we do have a very good ability to raise more capital, whether it be in the form of debt or preferred in particular, since as you know if we can at all help it, we're not about to abuse the common shareholder by issuing stock while our stock is in the pits the way it is.

Kevin Preloger
Perkins Investment

No understood.

Aldo C. Zucaro

That would be counterproductive in terms of the long-term interests of our shareholders so then that leaves some sort of security, whether it be debt or a common equivalent type of security. But in this market, as you know, access to the capital markets is still very limited. We're just beginning, and you must see this yourself in your management of investments the business you're in, that there's just a slight indication now that there is a thawing in the market, right?

If you eliminate the fact that you had a U.S. government guarantee of debt instruments issued by Goldman Sachs and so forth in this country, they would not have been able to access the markets I don't think. I mean the markets are still frozen. That's reality. So, therefore, when we say and we talked earlier about managing our business as if we are going to be left to our own devices in terms of meeting our mortgage guarantee obligations to the assureds that we have. Okay.

When we say yes we're going to need 50 to 100 to stay within the confines of what's required by the regulators, we're talking in terms of not being able to access the markets in a very cost efficient basis from both shareholder standpoints as well as policyholder standpoints.

As you know, in the insurance business in particular, we always run a very delicate balancing act, right? We have to please policyholders, we have to please insurance regulators, we have to please Uncle Sam, and we have to please the shareholders, right?

And all of those four people have got different agendas and different requirements, so what we're saying is at this stage of the game we have to assume that the capital markets are going to stay relatively frozen for another six months, nine months or so. That's the way we have to manage our business in a responsible fashion, we think.

Operator

Your next question comes from Stephen Mead - Anchor Capital Advisors.

Stephen Mead
Anchor Capital Advisors

Just going back to the general insurance business and I thought it was interesting when you were talking about 2009 in terms of the range of the combined ratio plus your expectations for premium, and I was trying to contrast that with what happened in the CCI business and your comment that in terms of the effect on the combined ration from CCI that it was a 400 basis point?

Aldo C. Zucaro

Yes. Four percentage points, so if our combined composite ratio for the general insurance business for the year was 97% as we published, right? If we did not have the CCI business it would have been 93%.

Stephen Mead
Anchor Capital Advisors

So that brings to question as you go forward into 2009 in terms of your outlook for CCI and some of the say strengthening factors in the general insurance business or say pressures that you're going to face in the general insurance business.

Aldo C. Zucaro

Hello?

Stephen Mead
Anchor Capital Advisors

Well, I was just wondering in terms of our outlook to the CCI business and also from a business model standpoint and in an insurance underwriting standpoint, where is CCI now from your perspective as far as a business where you can generate descent returns in or not?

Aldo C. Zucaro

Well, right now CCI is truly in the doldrums in terms of new production because again lending forget about first mortgage lending, but second lien and similar type of lending is really under pressure nationally, as you know. So there's very little new merchandise available to provide our insurance for.

And secondly, I will hardback to what Chris said in the last question about what you do in a bad market or in a market that still does not show an indication of resurrecting itself, and that's the way we see CCI right now. We're in a holding pattern mode until we get a better feel for the quality as well as the availability of loans to be insured in that business.

Therefore, just as I said that the last year the CCI product represented 10% of our net earned premiums, I would not be surprised if in 2009 it comes down to 8% or 8.5% of our volume because of the reluctance on our part to assume underwriting risk at what we consider is a period with many question marks attached to it.

Stephen Mead
Anchor Capital Advisors

Now going back to the question of sort of the either positive or negative forces that you face in the other areas of general insurance. I was just wondering in terms of on a going forward basis whether '09 is still going to have a similar kind of 400 basis impact on that.

Aldo C. Zucaro

Well, that's the assumption we're making, Steve, and I think our gut right now for what it's worth our best guess is that it doesn't get worse. There's a chance it gets better but we'd rather lean towards assuming that it stays in its current state, which is not an acceptable state.

Stephen Mead
Anchor Capital Advisors

If you could, going back to the mortgage business, I'm just curious on the FHA kind of competition or the different factors that you referred to in terms of your premium growth in the mortgage insurance business, I was trying to get a sense of kind of which factors were having more or a greater impact.

The other question is sort of going forward in terms of whether what the government does as it relates to backing mortgages whether the business model holds up over time. In other words, whether the government will still in a sense allow a market to function for you.

Christopher S. Nard

Let me tackle the first part. When you look at the mix and how the new writings have declined, as you can see in the press release from the fourth quarter of '07 to the fourth quarter of '08, it's a combination of things, but first and foremost we made dramatic changes in the underwriting guidelines.

We made then significant increase in prices, then that was followed on by obviously the reduction in business affected by those changes. Then the market began to come down dramatically and then the FHA stepped in to begin to stabilize the market by writing a lot of the business that we in fact stepped out of.

And that pattern very much follows the last stress period in this industry, which was in the late '80's obviously from the oil patch. We're really the first credit enhancer to take our lumps. We gear back out the FHFA steps in to help stabilize the market. The market stabilizes. They take some lumps and then we come back in. That's sort of the flow between credit enhancers public and private when you look at these catastrophic periods.

Secondly you asked about the government view of the business model. I think one thing that this disaster has shown, and I wish there was an easier way to show it than having incurred these losses, but there are very few other ways to credit enhance high LTV residential mortgages loans than with mortgage guarantee insurance.

If you think about the people in the mortgage business as a whole that have left or gone out of business, those people have diverse mix of businesses amongst high and low LTV products. The six of the seven mortgage insurers, the smallest one obviously is not writing new business, are all still in business writing loans and paying losses and the sum total of what we did was very high LTV mortgages across the country.

So I think what we're seeing today very much bears out the model. The other obvious credit enhancer that was in the business on the private side was the piggyback structure, and I think that has shown not only to be absolutely unreliable but to in essence of exacerbated the problem not made it better.

So obviously there's a lot going on as the governments think about how Fannie and Freddie rollback out, but I think the industry's performance to date bears out that there isn't a better way really to credit enhance high LTV loans than with properly capitalized and regulated mortgage insurers.

Stephen Mead
Anchor Capital Advisors

Then, Al, just on a more general basis and maybe you won't talk about this, but how are you dealing with a low interest rate environment in terms of generating return on the investment portfolio?

Aldo C. Zucaro

Well, of course given our operating philosophy we're stuck with having to invest in the highest quality paper that we can find and of course the reason for that, as we've said repeatedly over the years, is that in the insurance business all of our risk that we get paid for is on the right side of the balance sheet. We don't get any money for taking risk on the left side and, therefore that forces us to not play games with the asset side and that's why you find us in the very high quality area.

Therefore, to answer your question, Steve, we are stuck with having to invest in a lower yielding paper today. As a matter of fact, we are accumulating a greater amount of liquidity for both business reasons, i.e. to match our asset end liability payout structure on the one hand, but also with an eye toward the fact that it is more likely than not that we are bound to get a spurt in inflation in this country, given the fact that the money press is going full tilt.

Operator

Your next question will come from Mike Grundall - Key Colony.

Mike Grundall
Key Colony

Could you give us kind of a highlight on the fraud claim rescissions and what the trend has kind of been there in your mortgage insurance business? Then, Al, could you talk a little bit about the outlook or the potential for any capital via the TARP?

Christopher S. Nard

This is Chris. I'll tackle the first one. It's obvious that you cannot get these kinds of defaults in a marketplace and the kind of collapse that you've seen in the residential real estate business without there having been a tremendous amount of fraud enter into the business and as we look at our book, really you see it most aggressively in the 2006 and 2007 origination years.

The mortgage insurance policy doesn't cover losses for fraud and that's because of the structure of the business. We are not on the front end of the food chain where one could patrol for fraud, so it's not logical that a backend credit enhancer would cover an exposure that you really have to be on the front end to control.

So we have always very thoroughly reviewed the delinquent population and it particularly shows up when you have loans that miss payments in the first 12 months to make sure that those loans are in fact do not have misrepresentation in the files, and we will obviously investigate and review and rescind on those with obvious representation. There's always some misrepresentation in high LTV lending. You simply had a significant increase through the period of '06 and '07 for the reasons that we're all familiar with.

Mike Grundall
Key Colony

Could you give us a sense of the units that you've been rescinding the last couple of quarters and what the trend has been?

Christopher S. Nard

Well the trend is absolutely up, and I would tell you that when you get into certain pockets, Southern California, certain higher risk loan products reduce stock those sorts of things, you again have very, very high rates of misrepresentation in those files.

Aldo C. Zucaro

As to your question on TARP as I'm sure you've got your ears to the ground like everybody else and there's all sorts of buzz out there that some TARP money might be made available to financial guarantors of one stripe or another.

We are obviously looking with interest at that both as a company and as an industry, though we have to say that the benefit of TARP would be as we see it primarily as providing an ability to keep companies that do not have access to the capital markets to keep them in business in order to satisfy the validity of the mortgage guarantee instrument as Chris just described a few minutes ago.

It is the best that there is out there to provide a third party guarantee, but other than that we don't know of anything that's in the pipeline that assures that TARP money would be made available to financial guarantors at this point in time.

Mike Grundall
Key Colony

Then just two quick follow ups, could you tell us your ownership position today at MTG and PMI? What exactly is it?

Aldo C. Zucaro

It's shy. It's just shy of 15 in MGIC, I think it's 14.9. As a matter of fact, we're in process like all other owners of stock to file regular what is it, 13G or 13D or whatever it is filings with the SEC that are due as you know within 45 days of the end of a quarter, and it's a little more than 10% on PMI.

Mike Grundall
Key Colony

One last thing, Al, did you say in your prepared remarks that you did put $150 million of additional capital into the mortgage insurance subsidiary?

Aldo C. Zucaro

Yes. I said that we added $150 million of capital to our mortgage guarantee group.

Operator

Your next call comes from Matthew Goetzinger - Fiduciary Management.

Matthew Goetzinger
Fiduciary Management

Could you remind us of the remaining size of the '07 and '08 vintage mortgage books?

Aldo C. Zucaro

In terms of what, Matt?

Matthew Goetzinger
Fiduciary Management

In terms of the remaining, I guess, risk in force.

Aldo C. Zucaro

Risk in force? Can you put your hands on that, Chris?

Christopher S. Nard

Yes. I think it's in the 30% range. As we're talking I'll dig through for that.

Matthew Goetzinger
Fiduciary Management

Yes. If that could be split between the two years that would be great, and then also could you talk about the relative performance of those two books?

Christopher S. Nard

I think about 30% of the traditional primary book is in that '07 vintage and probably something close to 20 is in the '08, so about half of it's probably '07, '08 traditional primary. Sorry I had to look through real quick for that. Your follow-up question was the performance of '06 and '07?

Matthew Goetzinger
Fiduciary Management

The performance of more so '07 and '08?

Christopher S. Nard

Two thousand eight is kind of the tale of two cities in a book. That first quarter of '08 looks a little bit like the end of '07. It took a while for all the guidelines to get worked through the system. The second, third, and fourth quarter of '08 looked much, much better. They look much more like previous book years. The thing that you'll see though in the early '08 and '07 books are those books have a lot of misrepresentation in them.

The worst of the behavior along the lines of misrepresentation always seemed to work its way in right before the markets collapse or go away. So what we're finding in particularly late '07 is very, very high rates of rescissions. So while those books don't look great right out of the shoot, again a lot of that book ultimately likely to be rescinded because of high levels of misrep in the files.

Matthew Goetzinger
Fiduciary Management

What would you guess your true delinquency is on the primary side of the business excluding kind of fraud and rescissions?

Christopher S. Nard

I'm not sure how to get at that. I don't mean to dodge that's a tough question. I'd have to give some thought to.

Matthew Goetzinger
Fiduciary Management

In terms of the capital that was put into the MI business during the quarter it looks like the outstanding debt went up roughly $100 million and I'd assume that that speaks to part of that $150 million, and my question I guess secondarily is where is the other $50 million from?

Aldo C. Zucaro

Well, we always have some money and we do as we speak have money at the holding companies system. Money from tax recoveries, money from dividends received from subsidiaries in excess of our needs at the holding company level. So, the sum total of those funds together with the additional debt that you detected on the balance sheet, were the source of most of the money that we put in the mortgage guarantee business.

Matthew Goetzinger
Fiduciary Management

How much excess capital, Al, would you say is in that general insurance business at this point?

Aldo C. Zucaro

Well, historically we've had any where between $500 and $750 million of true excess capital. I would say today it's probably $250. Needless to say, our investments in MGIC and PMI in particular were made primarily as part of the investment portfolio of those companies and, therefore, the reduction in the market valuation impaired and otherwise of those securities took a chunk out of that perceived excess capital.

Matthew Goetzinger

Fiduciary Management

Was the majority of the $50 million it was distributed down to MI, was that from general insurance?

Aldo C. Zucaro

I'm not following the question.

Matthew Goetzinger
Fiduciary Management

Was the amount that was…

Aldo C. Zucaro

We put in $150 million in the mortgage guarantee group, and as I said that came from assets that we had at the holding company level. Those assets included I guess accumulations. Cash is very fungible as you know. Those assets came from an accumulation over time of dividends received from subsidiaries in excess of what we needed at the parent holding company level. I mean that money goes up and down during the year.

Matthew Goetzinger
Fiduciary Management

Lastly, Al, what are the other options that you're contemplating with regards to the additional capital you feel you need at this point?

Aldo C. Zucaro

I'm sorry, say that again?

Matthew Goetzinger
Fiduciary Management

What are the array of options that you're considering to fill that capital need?

Aldo C. Zucaro

Well, some of it would be obviously either access to bank debt or otherwise as well as I indicated before we do have still some significant amount of money at the holding company level and the combination of those, $50 million here and $25 million there and $75 million there gets us to the $50 to $100 million that we need.

Operator

Your next question comes from David Lewis - Raymond James has a follow up question.

David Lewis
Raymond James & Associates

First of all, Al, was there any favorable development in the quarter?

Aldo C. Zucaro

Are you talking about our general insurance business?

David Lewis
Raymond James & Associates

Yes.

Aldo C. Zucaro

Although, I have to say that whether it's general insurance or mortgage guarantee or title insurance our reserves last year all played out favorably. With specific reference to the general insurance business, what you see in the 2010K, the triangles that we have in there, which indicate on an average maybe the last five or six years a couple of 3 percentage points of redundancies in our general insurance company loss developments is just about what we had last year. So there was no significant difference between the years affecting the loss ratio by virtue of loss development.

David Lewis
Raymond James & Associates

So it's been pretty consistently in that two to three percentage [inaudible] annually for several years I think?

Aldo C. Zucaro

Correct.

David Lewis
Raymond James & Associates

The refi market, I know it's not getting back to levels we saw a couple of years ago but I know that it picked up in December just when rates were coming down. Any sense of what kind of the refis are in a year-over-year if you look to December just from a high level point of view? And someone had mentioned to me that even though the refi activities picked up it's not necessarily meaning that a lot of those are getting refied because they may not be qualified borrowers.

Aldo C. Zucaro

Correct on all accounts and don't know with respect to your question as to comparing November, December, let's say of last year with November, December of 2007. We don't have a feel for that. Although, my guess would be that there was very little, relatively speaking, very little refinance activity in 2007 the same period.

David Lewis
Raymond James & Associates

And just kind of to look at the dividend. I just ran a calculation if it was correct. Your dividend generally comes out of the general insurance operations and if we look at where the dividends today it's about 58% of your 2008 general insurance net profits. It seems like that would be very manageable if in fact you decided that you wanted to maintain that dividend. Is that kind of the right way to look at it?

Aldo C. Zucaro

We look at it the way you just described, which is we look at the sources of our dividends to the holding company the stability of that. We also look obviously at home much risk we expect to add to individual insurance companies, and as I indicated before in the comments, we basically set even though we look at it on a quarterly basis we basically set the dividend rate for the year in February at the February meeting of our board of directors.

Operator

At this time there are no further questions. I will turn the comments over to Mr. Al Zucaro for any additional closing remarks.

Aldo C. Zucaro
Well, we don't have any other comments. I mean this, as David just said, this turned out to be a pretty long call and for good reason. I think a lot of the questions that were raised pertain to significant parts of our business and address issues that are on everybody's minds at this time. So as always we're very appreciative of the interest that you all have in our company and we look forward to our next visit following the release of our first quarter 2009 results. Having said that, we'll bid you a good afternoon.