AXIS Capital Holdings Limited NYSE:AXS

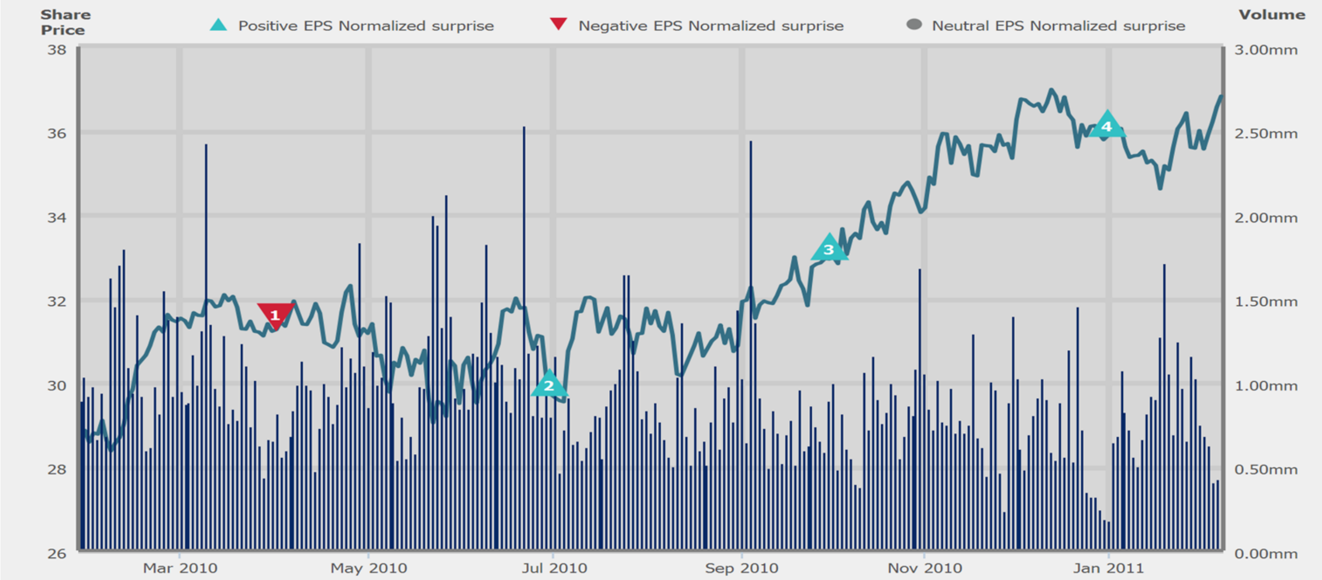
FQ1 2011 Earnings Call Transcripts

Friday, April 29, 2011 12:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2011-			-FQ2 2011-	-FY 2011-	-FY 2012-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	(3.19)	(3.65)	NM	1.14	0.19	4.06
Revenue (mm)	1087.01	1400.78	28.87	840.25	3426.23	3476.89

Currency: USD
Consensus as of Apr-29-2011 12:29 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2010	0.68	0.67	1 (1.47 %)
FQ2 2010	1.19	1.33	2 11.76 %
FQ3 2010	1.10	1.22	3 10.91 %
FQ4 2010	1.20	1.41	4 17.50 %

Call Participants

EXECUTIVES

Albert A. Benchimol
President, Chief Executive Officer & Director

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

Linda Ventresca

ANALYSTS

Elizabeth C. Malone
Wunderlich Securities Inc., Research Division

Ian Gutterman
Adage Capital

John Arthur Hall
Wells Fargo Securities, LLC, Research Division

Matthew G. Heimermann
JP Morgan Chase & Co, Research Division

Presentation

Operator

Good morning, and welcome to the Q1 2011 AXIS Capital Earnings Conference Call and Webcast. [Operator Instructions] Please note, this event is being recorded. I would now like to turn the conference over to Linda Ventresca, Executive Vice President. Please go ahead.

Linda Ventresca

Thank you, Rocco, and good morning, ladies and gentlemen. I'm happy to welcome you to our conference call to discuss the financial results for AXIS Capital for the quarter ended March 31, 2011. Our earnings press release and financial supplement were issued yesterday evening after the market closed. If you would like copies, please visit the Investor Information section of our website, www.axiscapital.com. We set aside an hour for today's call, which is also available as an audio webcast through the Investor Information section of our website. A replay of the teleconference will be available by dialing (877) 344-7529 in the U.S, and the international number is (412) 317-0088. The conference code for both replay dial-in numbers is 449839. With me on today's call are John Charman, our CEO and President; and Albert Benchimol, our CFO.

Before I turn the call over to John, I will remind everyone that statements made during this call, including the question-and-answer session, which are not historical facts may be forward-looking statements within the meaning of the U.S. federal securities laws. Forward-looking statements contained in this presentation include but are not necessarily limited to: information regarding our estimate of losses related to catastrophes, policies and other loss events; general economic capital and credit market conditions; future growth prospects, financial results and capital management initiatives; devaluation of losses and loss reserves; investment strategies, investment portfolio and market performance; impact to the marketplace with respect to changes in pricing models; and our expectations regarding pricing and other market conditions.

These statements involve risks, uncertainties and assumptions, which could cause actual results to differ materially from our expectations. For a discussion of these matters, please refer to the risk factors section in our most recent Form 10-K on file with the Securities and Exchange Commission. We undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

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

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

Thank you, Linda, and good morning, ladies and gentlemen. I will start by providing a brief overview of our results for the quarter and then leave it to Albert to provide more detail. Following that, I will discuss our underwriting operations and market outlook and then open the lines for questions. As you know from the headlines in our earnings release, the first quarter of 2011 has been an extraordinarily challenging quarter not only for AXIS but also for the industry as a whole, marked by an unprecedented series of natural catastrophes, including one of the largest earthquakes ever recorded. The scale of these losses is indicative of the terrible human tragedies we have witnessed during the period and our deepest sympathies are with those who have suffered from these events.

Currently, there is great uncertainty within the industry over the scale and distribution of total insured losses, which we believe are likely to be in excess of $50 billion. Against the backdrop of this uncertainty, we believe that we have been prudent in estimating our catastrophe losses. Our results, therefore, this quarter are heavily influenced by an accumulation of expensive major natural catastrophes, slow pickup in global demand for our products and continuing low investment yields.

We produced a net loss of $384 million this quarter, or a net loss of $3.39 per diluted share. On a positive note, these industry-wide pressures, coming on the back of 4 to 5 years of aggressive price competition, are now driving an earlier exit from the absolute bottom of the property and casualty pricing cycle in a number of lines. We believe our major global businesses stand to gain meaningfully in the coming year. Of course, our business is one that can only be appropriately judged over periods of much longer than one quarter or one year. And generally, these cat events present great option value in the ensuing months.

Even with the major loss events, we have accreted diluted book value per share over the last 12 months by 3.3%. Over the 5 years ended 31st of March, 2011, we have accreted diluted book value per share of a compound annual rate of 13.4%. And with that, I would like to turn the call over to Albert.

Albert A. Benchimol
President, Chief Executive Officer & Director

Thank you, John, and good morning to everyone. As John noted, this has been an extraordinary quarter for the industry, with an unusual frequency of record-breaking catastrophe losses in 3 different markets. As a global insurer and reinsurer with meaningful exposure to short-tail catastrophe-exposed property lines, AXIS was naturally impacted by these events. The March 11 Japanese earthquake and tsunami had the most significant impact on our first quarter results. We currently estimate total insured losses from this event, excluding those assumed by the Japanese government, will be in the range of $30 billion to $35 billion. We understand that our industry estimate is on the high end of what's been reported by others, and that naturally colors our estimate of our own claims. It is just that we believe that it is way too early to be overly optimistic about the economic costs of this tragedy.

We recognized associated pretax net losses, net of related reinstatement premiums of $287 million for this event, with $260 million of this amount emanating from our Reinsurance segment. Within this estimate, we assume the largest mutual reinsurance program was a total loss. Losses in our Insurance segment are not expected to exceed $25 million due to reinsurance protection limiting these retentions. We believe the Christchurch, New Zealand earthquake will generate industry losses in the range of $8 billion to $12 billion. We recorded pretax net losses, again net of related reinstatement premiums, of $203 million for this event. Here again, the majority of the losses emanated from our Reinsurance segment, which accounted for $183 million of that amount. In arriving at these estimates, we assume the total loss of the vast majority of reinsurance treaties exposed to the quake, including a significant treaty exposed to a government-owned provider of residential earthquake coverages.

As for the last of the significant first quarter 2011 cat events, we estimate that January Australian floods and Cyclone Yasi will cost the industry in excess of $6 billion. We booked pretax net losses, net of related reinstatement premiums, of $87 million for Australia, of which $84 million relates to our Reinsurance segment. It goes without saying these are early estimates, subject to change. In particular, earthquake losses are notoriously difficult to quantify and have historically deteriorated from the industry's initial estimates. With this in mind, we aim to set prudent estimates based on all information available to us, but also recognizing that quality and quantity of information will develop over time.

We did not solely rely on models in developing our loss estimates. Models are only one element of our approach to setting catastrophe loss estimates. More importantly, we incorporated our underwriting and claims expertise in a largely ground-up approach developing our loss estimates. Nevertheless, given the timing of the events, very little information is available from clients and brokers at this point. The Japanese earthquake losses are also subject to additional uncertainties, including those related to business interruption and contingent business interruption coverages and the ultimate size of losses to be assumed by the Japan cooperative mutuals. It was our intention in setting our catastrophe loss estimates that the first quarter events be addressed in full now with no adverse impact to future periods. Of course, we will update you throughout the year as we receive relevant information.

So the total net financial impact of these events in our net income for the quarter was $574 million net of tax, reinsurance recoveries and reinstatement premiums. As a result, we reported an operating loss of

$414 million or $3.65 per share. In contrast, we reported operating income of $96 million or $0.67 per diluted share in the first quarter of 2010, which itself was affected by $147 million in catastrophe losses from the Chilean earthquake, the Australian storms, Windstorm Xynthia and U.S. winter storms.

To put things in perspective, in its history, AXIS has reported 3 operating loss quarters: the third quarter of 2005, impacted by Hurricanes Katrina and Rita; the third quarter of 2008, affected by Hurricanes Ike and Gustav; and this year's first quarter. In terms of dollars and combined ratio, this quarter's loss comes in between 2005 and 2008. However, on a per share basis, this quarter's operating loss is the larger one. This is because we had 141 million common shares outstanding during the third quarter of 2005. Since then, we've been active in repurchasing common shares. So this quarter's loss is allocated to only 113 million common shares. Both of these, of course, are basic counts as the diluted share counts will be anti-dilutive to earnings.

Importantly, in those prior years, the quarterly loss was offset by profits in the rest of the year, such that AXIS has never reported a loss year. It would be foolhardy to project annual results, but I will say that at this point, we believe a profit for the year is possible even with additional catastrophe activity during the year. The ultimate outcome for the year will, of course, primarily depend on the frequency and severity of cat activity for the remainder of the year.

The catastrophe events are the big story for the quarter. But our results x cat, while good, were nonetheless lower than the prior year due to an increasingly competitive market, increased large losses in Offshore Energy and lower net favorable prior year development. Excluding the impacts of the named catastrophe events in both quarters, we generated operating income of $160 million or $1.25 per diluted common share in 2011, compared to $243 million or $1.71 per diluted common share in 2010.

There's no question that this was a tough quarter. But this is our business. And we are proud to stand by our clients when they experience times of stress. But also because this is our business, we are well structured to absorb these major claims. Not only do we have a strong balance sheet, but we've built a well diversified portfolio of business that generated meaningful underwriting profit to at least partially offset the large catastrophe claims. We stand as ready today to support our clients as we did prior to these events. However, in return, we do require adequate compensation for the protection we are providing and for the capital we are allocating to those risks.

Let's move to the income statement. First quarter gross written premiums were up 9% to $1.5 billion. Premiums in our Insurance segment were up $52 million or 14%, substantially driven by our new global A&H operations, which reported gross premiums written of $44 million in the quarter versus essentially nothing last year. Our reinsurance premiums were also up with the important January 1 renewal season, given strong growth in European motor business and the renewal of a handful of multiyear contracts that were initially written in 2009. On a constant currency basis, reinsurance gross premiums written were up 10%. However, given a slightly stronger U.S. dollar this year, reported gross reinsurance premiums written increased 7%. Consolidated net premiums written are up 13%, a bit more than the gross premium written due to the previously discussed change in our reinsurance ceded program, wherein we are keeping more of our Property and Professional Lines insurance premiums. Consolidated net premiums earned grew at a similar 13% rate.

Losses essentially doubled on the back of the catastrophe events, leading to an underwriting loss of $461 million this quarter with an accident year loss ratio of 135.7%. In comparison, we generated underwriting profits of $28 million in the first quarter of 2010, with an accident year loss ratio of 79%. Excluding the impact of the named catastrophes, our accident year loss ratio increased by 4.9 points from 57.4% in the first quarter of 2010 to 62.3% this quarter, with the increase relating to increased large loss activity in our Offshore Energy and Property insurance lines and the general softening of insurance rates.

Within our segments, the insurance accident year loss ratio increased 25 points this quarter to 85.9%. Excluding the impact of named catastrophes in both periods, the segment's accident year loss ratio increased by 11.9 points, reflecting the previously mentioned energy losses and softening rates. The accident year loss ratio for the Reinsurance segment was 81.6 points higher than the prior year at 171.1%. Excluding the impacts of the named catastrophes in both quarters, the Reinsurance segment's accident year loss ratio was basically flat year-over-year. The impact of rate softening was largely offset by an anticipated improvement in our trade credit and bond reinsurance loss ratios in light of the continuing recovery of the global economy.

Separately, our estimate of net reserves from prior accident years continues to develop favorably, albeit at a lower level than the prior year quarter. In this quarter, we booked $50 million of net favorable development, delivering a positive impact of 6.3 points on our consolidated loss ratio as compared to a beneficial impact of 11.7 points in the first quarter of 2010. For our Insurance segment, the impact was a 4.5 point loss ratio reduction, while the Reinsurance segment recognized 7.6 point reduction. Approximately 75% of the group's consolidated net favorable reserve development this quarter was generated from short-tail lines and reflected better-than-expected loss emergence. The remainder related primarily to our Professional Lines insurance and reinsurance business, as we continue to incorporate our own experience into our ultimate expected loss ratios. We have yet to do this in any meaningful way for our liability lines with longer development tails. There was no material impact one way or the other from the 2010 cat events.

Net investment income was $111 million for the quarter, modestly above last year's $105 million. We are still suffering from a low interest rate environment and the investment income from our fixed maturities and cash at $91 million was modestly below the prior year level as a larger asset base offset most of the lower coupon yields. The improvement came from our other investments portfolio, which generated $25 million this quarter. In particular, our portfolio of CLO equity has performed very strongly and generated $12 million this quarter as compared to $2 million in the prior year.

In aggregate, the total return on our cash and investment portfolio for the quarter was 0.9%. This reflects tightening credit spreads, offsetting the negative impact of the rising risk for yield curves, and the positive return on our equity and other investment portfolios. While the recent modest uptick in rates gives us hope that trends may improve over time, in the immediate future, we expect net investment income will continue to face headwinds.

To illustrate the point, our current book yield is 3.3%, but the yield at market on our fixed-income portfolio is currently at approximately 2.9%. So we are still generally replacing securities with lower-yielding assets. The other income statement items are relatively straightforward. Total general and administrative expenses this quarter were largely consistent with the fourth quarter of 2010, excluding the impacts of the additional bonus accrual reflected in that quarter, and they're higher than the prior year quarter, largely due to higher headcount.

Interest expense is up year-over-year due to the $500 million debt issue in March 2010. Foreign exchange movements reversed quarter-over-quarter with losses this quarter being driven by the appreciation of the euro. However, as I've mentioned previously, much of this income statement impact is offset by opposing balances and comprehensive income. Therefore, the impacts of these losses on our book value is generally minimal. And in fact, it was a modest positive this quarter overall.

We did have a small tax expense, not withstanding the pretax loss. Our cat losses were predominantly in Bermuda, which does not have a tax benefit and we had profits in certain taxable jurisdictions. The net of all these items in preferred items and preferred dividends was a net loss available to common shareholders of $384 million. Excluding the after-tax impacts of the named catastrophe events, we would have resulted in a net income available to common shareholders of $190 million.

Moving on to the balance sheet. Our assets grew 7% in the quarter to $17.7 billion, with changes very consistent with our activities in this quarter. Given the importance of the January 1 renewals, our balance sheet reflects larger balances for premiums receivable, under premiums and deferred acquisition costs, while the large cat losses affected gross reserves and reinsurance recoverables.

Cash and invested assets totaled $12.9 billion at quarter end, over $800 million higher than the year ago. Cash, U.S. government and agency securities and AAA-rated securities make up over 1/2 of all invested assets and cash. We realized $30 million of net gains during the quarter, and have approximately $170 million of net unrealized gains at quarter end.

There was not much change to the overall composition of our portfolio. During the quarter, we continued diversification of our portfolio and increased equity holdings by about 1% to 4% of total assets. At quarter end, equities and alternatives make up a bit more than 8% of total cash and invested assets. 9% is in cash and short-term investments. 83% of our portfolio is made up of our fixed maturity portfolio. Changes to this portfolio during the quarter included small increases in short-duration, high-yield assets and reduced exposure to investment grade corporate holdings. We do have a 6% allocation to municipal bonds, but these securities have an average rating of AA, and an average maturity of 6 years.

We continue to monitor opportunities to manage our portfolio's sensitivity to interest rate risk through allocation to equities and hedge funds and maintaining a prudent portfolio duration approximating 3 years. Gross reserves aggregate to $8 billion, while net unpaid loss reserves are $6.3 billion, an increase of $856 million from year end, as we booked approximately $581 million in catastrophe-related net losses during the quarter. Our reinsurance balances recoverable of $1.7 billion are equal to approximately 21% of gross reserves. And 71% of our reinsurance recoverable balance is IBNR. This is an item we watch closely and we remain comfortable both with the quality and collectibility of these balances.

Our total capital at March 31 was $6.2 billion, down from $6.6 billion at year end, including $1 billion of long-term debt and $500 million of preferred equity. Book value per diluted share was $35.69 at March 31, a 9.3% reduction over the year-end figure but a 3.3% increase over the book value per share as of March 31 of last year.

While we're disappointed at the recent reduction in our common equity, we are confident that ours remains one of the strongest balance sheets in the industry, and we are committed to resuming our impressive record of book value growth in the quarters and years to come.

Before we turn the call to John, I'd like to give you an update on our warrants. As I mentioned in our last call and as we noted in our press release, we had $19.8 million warrants outstanding that were set to expire in November of this year. Subsequent to March 31, certain holders exercised their warrants on a cashless basis. Accordingly, we issued 11.9 million shares upon the exercise of 18.1 million warrants. At this time, 1.7 million warrants remain outstanding and they will expire November 20. There was virtually no impact on the number of diluted shares outstanding, nor our diluted book value per share, although our calculation of these figures already took into consideration the eventual exercise of these warrants. And with that, I'll turn the call back to John.

John R. Charman

Former Director, Chairman of Axis Re and Chairman of Axis Specialty Europe

Thank you, Albert. What a first quarter to be inducted into the AXIS family! In 2010, we estimate our industry absorbed well over $30 billion in catastrophes and other large losses. Despite these aggregating with the continued soft market conditions, the underwriting side of our business performed reasonably well. Investments, which are also critical to so many companies in our industry, continued to come under enormous pressure because of low interest rates and generally lower investment returns.

We entered 2011 knowing that underwriting conditions were likely to be both aggressive and extreme in price competition. We viewed 2011 as being our most difficult year yet to navigate. However, we also strongly believed that 2012 would herald the beginning of cyclical change and a hardening market across the board would emerge. Then during the first quarter of 2011, in addition to challenging market conditions, Murphy's Law happened. The industry was overwhelmed by a very high number of large market losses, marked by significant severity of loss. For 2011 to date, in addition to normal expected losses, we estimate that there have been in excess of $50 billion in insured large losses. There is huge uncertainty over the scale and distribution of these losses to the industry. However, mindful of our historic conservative reserving philosophy, we believe we are prudently reserved.

Much of the projected profitability for this year for the P&C industry has been lost, yet we still have the U.S. and Asian wind seasons to endure. With the burden of these losses, the incorporation of material cat modeling changes associated with RMS version 11, the continued low interest rate environment and negative industry underwriting cash flows, we strongly believe that cycle change is both imminent and overwhelmingly necessary. Markets are reluctant to give reductions for property catastrophe business in virtually all regions in light of the major cats experienced so far this year. And as expected, property catastrophe pricing is increasing materially in affected areas.

The Japanese renewal season was interrupted by the Tohoku earthquake and tsunami. Many markets had already quoted cat and non-cat renewals before the event. And these quotes were for the most part honored. Those contracts which were able to be renegotiated saw initial increases in Japanese wind pricing up 5% to 10% and Japan earthquake pricing up around 50%. U.S. pricing is moving already, with U.S. property cat reinsurance programs seeing price rises of at least 10%, depending upon entry levels.

With time, the model changes associated with RMS version 11, which we have already adopted in principle, are gaining broader acceptance. The question will be the degree and time to which some of the very material changes can rationally and reasonably be implemented. We are always at the forefront of pricing discussions. If we cannot achieve the appropriate increases on our portfolio based on exposure, experience and model change, we will limit our commitments, if not exit altogether.

We have some evidence that U.S. casualty reinsurance pricing is also starting to see some positive momentum. While not a credible trend yet, this is still yet another positive sign. This momentum away from price reductions to price increases which we are seeing in the reinsurance market is also evident in many areas of the primary insurance market on a global basis, particularly property and energy lines. The areas of the property casualty insurance market in which we participate appear to be in the last phase of a long, soft market cycle. On the other hand, commercial liability remains the most competitive sector due to overcrowding and overly optimistic loss trend assumptions.

As background, for many years, the competitive behavior of many primary markets has been fueled to an extent by a competitively priced facultative reinsurance market. The catastrophe and large losses of 2010 and 2011 have forced the substantial reevaluation of pricing by the facultative markets, which is having a knock-on effect to the primary markets. In our opinion, this impact to primary insurers will be compounded by any hardening in the reinsurance treaty marketplace.

Before I conclude my commentary, I want to emphasize our belief that the transitional nature of this year demands that we act prudently, not hastily, to ensure allocation of capital to the very best opportunities. We've modified our assumptions regarding potential for loss and commensurate capital allocation. We're executing on our plans and working immediately to increase our underwriting margins with these assumptions incorporated. We believe that if we execute on this well, increased future profits will result.

Going forward, we expect that the cycle change will strengthen throughout 2011 and impact the insurance and reinsurance markets more broadly due to the following: the incorporation of material catastrophe modeling changes more broadly in the global industry, and by peril; the impact of greater reinsurance costs mitigating the competitive behavior of insurance companies; and a contraction of capacity for catastrophe-exposed business. We are already contributing to this by reducing our exposure-adjusted aggregates going forward.

In the face of all this, our balance sheet and capital position remain strong. We are operating from a position of strength and we believe that every one of our major businesses stands to gain in the ensuing 12 to 24 months. Our underwriters have a proven track record of capitalizing on opportunities quickly and decisively. This globally coordinated activity takes place within an intelligent peer review environment, strongly supported by a deeply embedded and experienced management team. Our absolute focus remains on building book value meaningfully over the long term. And with that, I'd like to open the lines for questions. Thank you.

Question and Answer

Operator

[Operator Instructions] Our first question comes from Matthew Heimermann from JPMorgan.

Matthew G. Heimermann
JP Morgan Chase & Co, Research Division

A couple of things. First, could you just -- I'd like you to reconcile maybe the comments you made about decreasing your exposure-adjusted aggregate, just with where your 1-in-250 PML [probable maximum loss] is sitting relative to your risk tolerance level. And then the second question I had was with respect to your comment in the press release and prepared remarks on the demand side, was that meant to be an exposure comment? And then just for Albert, maybe, on the A&H product, when we think about premiums there, is that a lumpy revenue recognition product? Or is the production we're actually seeing right now more indicative of the run rate?

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

I'm going ask my new colleague, Murphy, to answer that, if I may.

Albert A. Benchimol
President, Chief Executive Officer & Director

I guess I'm not really part of the family till I have a nickname. Let's deal with all 3 questions. I'm going to deal with the simpler fact answer and then I'll come back in reverse order. The A&H strategy, as John has discussed and management has discussed with you in the past, is really both an insurance and reinsurance strategy that is to be executed both in the U.S. and internationally. As you know, it's been easier to enter the international markets because some of the licensing and jurisdictional issues in the U.S. seem to take a lot longer and are more arduous. And so this book is growing mostly on the international reinsurance side in the early years. But as we get our licenses in the U.S., we expect that we will be able to balance that book out between both primary and reinsurance in U.S. and internationally. And so what you've got this year is essentially a large reinsurance book. And in the first quarter, we've produced close to $75 million of business, of which approximately $42 million was recognized in the quarter. So there's going to be a fair amount of lumpiness to that. There will be some more premium that we expect during the year, but the bulk of the premium has, in fact, been produced in the first quarter. With regard to the second question, the growth here really refers to the fact that with the economy growing slowly, there is less demand for insurance overall. Generally, you expand that with economic activity growing. Demand for insurance grows accordingly, but the economic activity has grown only slowly and that's what we meant by driving the growth. With regards to the limits, I think there's been a little bit of confusion with regards to the table that we have on Page 21 of our financial supplement, specifically as it relates to our stated appetite of having a PML of no more than 25% of our common equity per zone. What you have on Page 21 is a combination of both zonal and total country exposures. Specifically, the United States hurricane is the aggregate of exposures to more than one zone. With regard to the other 4 areas, those are actually zones. So although it appears that the $1.425 billion is in excess of 25% of our common equity, within that number, there are zonal limits and those zonal limits are all within our risk appetite. This is information that, as I understand, was developed over time to provide information that analysts and investors could compare with other disclosures, and it was really not meant to be indicative of a single zone. That addresses the issue of the conference call. The second issue is really probably the broader issue with John, discussed in his comments, and that is as we look at the impact of RMS 11, there is no question that our current exposures are going to give us PMLs that are larger than what we currently have. And what we are currently going through is validating the RMS model and applying it to our own portfolio. And just to give you, as a background, we used more than just RMS. We used a combination of models, we add nonmodeled losses to our analyses, we add some judgment and experience to it. But all of those inputs are considered in calculating PMLs in our risk appetite. We expect that as a result of all of that, our PMLs, as they will be calculated, will increase. And to ensure that we bring our PMLs down to our appetite, we will have to think about how we allocate our catastrophe exposure. It is a rationed capacity, and it will need to go to our best clients and to the best opportunities.

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

And it's going to be better priced.

Matthew G. Heimermann
JP Morgan Chase & Co, Research Division

So is it -- that's very helpful and thorough. Just a follow-up on that. So it's probably fair that -- so U.S. total is multiple zones. California is, I'm assuming, one single zone. Would that be a better barometer for us to back-test against?

Albert A. Benchimol
President, Chief Executive Officer & Director

That is correct. And again, I will say that all of our zones are within the appetite. The multiple zones, of course, are in excess. And I'm sure that Linda has already discussed this with you and others, but there are a number of different limits that the company uses to manage its risk appetite. There's a whole matrix of limits, PMLs, modeled ROEs, losses and so on and so forth. And of course, the company's portfolio is modeled to maintain consistent and within the limits imposed by those matrixes.

Matthew G. Heimermann
JP Morgan Chase & Co, Research Division

And just to clarify it to you right, these are all internal tolerances. I mean, there's not an external -- none of these trigger strong responses, in other words, from a rating perspective, et cetera.

Albert A. Benchimol
President, Chief Executive Officer & Director

No, this is our company's risk appetite as proposed by management and approved by our board.

Operator

Our next question comes from Beth Malone from Wunderlich.

Elizabeth C. Malone
Wunderlich Securities Inc., Research Division

A few questions. On the share repurchase, you didn't repurchase any shares in the quarter. And it sounds like you're going to -- that you may want to keep some of that capital to write this proposed new better-priced business. What's the expectation on share repurchase?

Albert A. Benchimol
President, Chief Executive Officer & Director

I think you just stated it.

Elizabeth C. Malone
Wunderlich Securities Inc., Research Division

Okay. So we shouldn't anticipate that going forward, for the near future anyway?

Albert A. Benchimol
President, Chief Executive Officer & Director

I think there's a lot of fact points that needs to come through. Obviously, we need to take a look at what the cat activity looks like for the rest of the year. We need to take a look at whether or not the market responds the way we think it's going to respond. We've got to take a look at the opportunities that may come up as a result of these events. I think it's too early to basically spend our capital not knowing what those other opportunities may be.

Elizabeth C. Malone
Wunderlich Securities Inc., Research Division

Okay. And then on the Professional Liability line in the insurance, that's been declining, obviously. And I understand pricing, you've spoken that pricing is pretty competitive there. Do you see that changing in the near -- within the next year as this pricing trend? Is that the last place where we should expect it to see price improvement?

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

I think you're right, regrettably. We have -- just to remind everybody, we have an extraordinarily diverse Professional Lines portfolio. By product line, I think I've said before, we have over 20 product lines within the product. And by geography, we write this businesses on a global basis. So there is a lot of competition because it's very good business for us, and historically has always been very profitable. But I don't expect that to move through the rest of this year, barring a major event.

Elizabeth C. Malone
Wunderlich Securities Inc., Research Division

Okay. And then a last question. Just in general, historically, when we've seen a pricing cycle harden, like you're anticipating this one, what accompanies that or another trigger of that is a number of companies get in financial difficulty and trouble on, and that capacity leaves the marketplace. Should -- can you give me a sense of -- do you see the makings of that in among the marketplace at this point?

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

I don't really see balance sheet disruption unless there's another major event. What we have seen is the fact that some of the newer entrants that were overly optimistic about their ability to participate in some very difficult markets, some very difficult products, are actually withdrawing or cutting back substantially their line structures because they've seen the inevitable results on their financial returns. I'm celebrating my 40th year in the industry on the 1st of November, if celebrating is that, but in the previous cycle changes that I've worked through, which are not driven by a major event, it has really got to the stage where the industry has given away all its margin, and more, and is beginning to see strain in the individual product lines. And then that coincides with the reinsurance marketplace saying, "Enough's enough," and beginning to push back, which it has been on the longer-tail line since the beginning of this year, and undoubtedly, since the major cats, has pushed back on all of the shorter, the medium-tail lines. And so, there's a perfect squeeze that is going to take place for the primary insurance market for the rest of this year, and will strengthen going into next year. As well as that, I think the primary insurance market, I was convinced, going into January had, had enough of the price competition and was in a situation of moving, wanting to move in a different direction. The catalyst for that has been the number of cat losses that we've had during the first quarter.

Elizabeth C. Malone
Wunderlich Securities Inc., Research Division

Okay. And then one last question, on the recovery of, the hardening of the market. That, I understood from a number of people that in a weak economy or in a recession, it's very difficult to get price increases. Do you see that some of the modest recovery we've seen in the economy positions the market to be a little bit easier to get those price increases?

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

I think it's a load of baloney, quite frankly, what you just said. Not because of what you just -- that you said it, but I hear the same old stuff time and time again. It doesn't come from those people who actually push prices down by an aggregate of 50% over a 4- to 5-year period. And then when you're trying to get double-digit price increases off of a base of 40% to 50% of what we were earning 5 years ago, everybody squeals, naturally, especially in a difficult economy. But at the end of the day, the insurance industry absolutely oil the wheels of industry and the global industry, and are absolutely critical to the well-being of that industry. Ships don't float, carry cargoes, airplanes don't fly, refineries don't refine, all of this stuff. Yes, there will be, I'm sure, criticism. But it wasn't criticism when they were achieving substantial price reductions during that period. I have no doubt that the industry will be able to achieve the price increases it will need over the next 3 years.

Operator

Our next question comes from John Hall from Wells Fargo.

John Arthur Hall
Wells Fargo Securities, LLC, Research Division

John, in your commentary, you mentioned something about U.S. casualty momentum. I was hoping you could just offer a little bit more granularity or perhaps an example of where that momentum is developing.

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

As you know, we're not big casualty underwriters. But what we do have on the umbrella and excess business -- and we started to feel this very strongly at the end of last year. We saw signs of, again, the market beginning to say that enough was enough. And there were pockets of resistance beginning to occur. And I think that we are becoming more comfortable as each month goes by about the outlook for those businesses. Primary casualty is still tough, on the Insurance side. But at the end of the day, I believe that, that's more subjected to the big national players. And it takes them probably 6 months longer than the rest of the market to react to circumstance. But definitely on the Reinsurance side, the casualty market has changed. It changed, it's become more difficult for the ceding businesses to get better terms. There's been push-back. I've been seeing it in the stuff that we're looking at, with ceding commissions being reduced as opposed to expanded, and terms being looked at much more closely.

John Arthur Hall
Wells Fargo Securities, LLC, Research Division

I had two other questions. One has to do with demand, but a slightly different take on it. Have the catastrophes and the like in the quarter, do you see any capacity for change in terms of the demand for property cat coverage, I guess, maybe in Japan? Elsewhere?

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

I think the model change is going to have a substantial impact on demand. But that would take time to come through, over the next probably 12 to 18 months. Undoubtedly, that's going to be a factor. As the economy continues to strengthen, albeit at a slow pace, that will, as well, continue to provide extra stimulus. We also know that the European wind bubble is going to be strengthening in the same way that RMS 11 has. So Europe is going to have to, I think, reconsider a lot of its exposures and a lot of its buying, both on the primary side and on the reinsurance side, as we move towards the middle of the year. So from model change alone, I expect there to be a material increase in demand for coverage.

Albert A. Benchimol
President, Chief Executive Officer & Director

I was only saying, and that should only be further highlighted with the upcoming Solvency II, which will, of course, put more pressure on that.

John Arthur Hall
Wells Fargo Securities, LLC, Research Division

Understood. And also, John, in your comments, you mentioned a contraction of capacity. I was wondering if you'd be willing to throw a number around that.

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

I'm not going to give you a number. But what I do know is the fact that anybody who thinks that the model changes are not going to be taken seriously by the industry, I think, is cuckoo. The reality of the significance and the materiality of model changes, even if you take out storm surge, is so material, that the industry has to adjust and has to change its practice. So it's a very positive change for the industry in terms of forcing better recognition of exposures and actually moving towards strengthening pricing.

Operator

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

Ian Gutterman
Adage Capital

First, you mentioned some of the energy loss, I assume that was either Griffin or the Canadian loss. Can you give some numbers on that? So I'm guessing that's what drove up the accident year in the Insurance segment?

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

We don't give individual loss numbers. But I do -- I think the Griffin loss is a very interesting loss for you guys to understand, because there you had -- and it shows you the severity of loss that can occur out of really not a major catastrophe. When you think Piper Alpha, going back to the late '80s, was a $1.2 billion loss, this Griffin loss was what is a floating storage and production platform, which is dynamically anchored by 8 or 10 huge anchors. And it's kept in position by computer-controlled systems, so that should then ease and strain the anchors. It's a fantastic technology. But this thing was hit by a storm in the North Sea, and it dragged its anchors by 200 yards. But the issue is it produced $800 million of loss to the marketplace. And so it's this concentration of value and exposures that we're seeing, not just out of cat losses. And this is where I think some of the more -- I'm getting around to my point, Ian, so forgive me. Some of the more excessive competition that we've seen throughout the specialty lines is really through inexperienced underwriters, who have no real understanding of the potential for loss coming out of these highly specialized and highly valued pieces of equipment. And I hope that it sends a very strong message through to the industry about really being more cautious about the terms and conditions they're offering. And the owner of that particular piece of equipment is a first-class owner that the marketplace would want to be involved with. So I'm not questioning that. But it certainly raised some flags with me as to the concentration of assets and values, and what I consider to be an operational loss occurring.

Albert A. Benchimol
President, Chief Executive Officer & Director

If I could add to that, Ian, basically of the 11.9 increase in the accident year ratio -- and we're not talking about any individual, we'd say about 1/2 of that is due to higher activity on the large losses, which are not catastrophic in nature. And 1/2 of that is about rate and market conditions. So yes, we have seen some...

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

And also business makes change as well, Ian, so I'm not too fussed about -- I think our underwriting x cat numbers are performing very well. And because of the robustness of our process in terms of price monitoring, Ian, I'm really as comfortable as I can be in the market conditions about how we're faring.

Ian Gutterman
Adage Capital

That's right. I just want to make sure that I didn't attribute it to something else, that it was mostly equated to the energy losses. The other one just on the large Japanese mutual you mentioned putting up a full loss. Should I assume -- because, I guess, I just saw that they've sort of put out their first notification that didn't touch the uppermost layers. Does that going to imply that you're not on those layers?

Albert A. Benchimol
President, Chief Executive Officer & Director

No, not at all. I think -- in fact, we have a reasonably large exposure to the top layers of a number of programs. And certainly these early indications are, I would say, hopeful. But as you know, these are still very, very early. They're based on some models and so on and so forth. There is nothing that we would like more than to have these early numbers proved to be correct. Because if they are, we will take our loss estimate down. We just don't think it's appropriate to be optimistic when one puts up these claims in the first place.

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

And Ian, if I might just add to what Albert has said. I've been surprised that the lack of attention that's been paid to the releases from carriers about the cat losses in both New Zealand and Japan. And we tried in the language around our loss estimates to be as clear as we could be about the conservatism and the prudence that we put in when we were coming up with our loss advices. Now there are some very big lumpy contracts, both in New Zealand as well as Japan, that will materially impact the ultimate loss position for companies. And I've been privately a little bit disappointed that there isn't greater attention being -- there seems to be a blind acceptance that the numbers are the numbers, and everybody's batting off of the same level playing field. And I would urge you to look at the numbers very closely to see whether the companies have really differentiated, whether they are totaling some of these mutuals or whether they're not accepting any losses at all, or whether they're halfway. Because in one of those situations, that's a reinsured difference of $4 billion, which is distributed through the marketplace. So because of the scale of these losses, the distribution is a real issue. But as Albert said, here at AXIS, because we have historically reserved on a conservative basis, we're very comfortable with the reserves that we've put up.

Ian Gutterman
Adage Capital

That's great. To be honest, I had the same concern for some of your peers, too. Just my last one, really quick. Going back to the PML question from earlier, it looks like you changed the definition, where if I look in prior supplements, it was 25% of capital. And now we're at 25% of equity. Can you talk about that change? Was it always equity and you just printed wrong? Or was that an actual change in how you're managing it?

Albert A. Benchimol
President, Chief Executive Officer & Director

No, it's actually changed. But as you might imagine, the company's risk management evolves over time. And one of the things that's come across is that the company has moved from a small number of hard-line limits to a broader matrix that looks at things like equity, ROE, how much of our operating earnings we're prepared to expose and so on and so forth. So what you're seeing here is a refinement of the overall approach to risk management at AXIS.

Ian Gutterman
Adage Capital

Got it. And I guess, the last thing I'll lob in is, given the things you mentioned on the U.S. wind with the multiple zones, just maybe in the future, if there's a way to break it up by zones so it's a little bit more useful to us, that would be appreciated.

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

Ian, sorry, forgive me. I just want to come back, again on the -- because you did mention the breaking news about some of the, couple of the mutuals giving out some early loss information. I just want to stress again that their loss information was really modeled loss information. There is very little actual. So in terms of uncertainty, there is still considerable uncertainty out there regarding the scale and the distribution of the Japanese loss.

Ian Gutterman
Adage Capital

That makes perfect sense. Thank you guys for the time.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to John Charman for any closing remarks.

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

Well, thank you once again, ladies and gentlemen, for joining us today for our earnings call. I hope that the next earning call will be much more positive in the information we're going to provide you. But thank you again, and enjoy the royal wedding.

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