S&P Global
Market Intelligence

Chubb Limited NYSE:CB

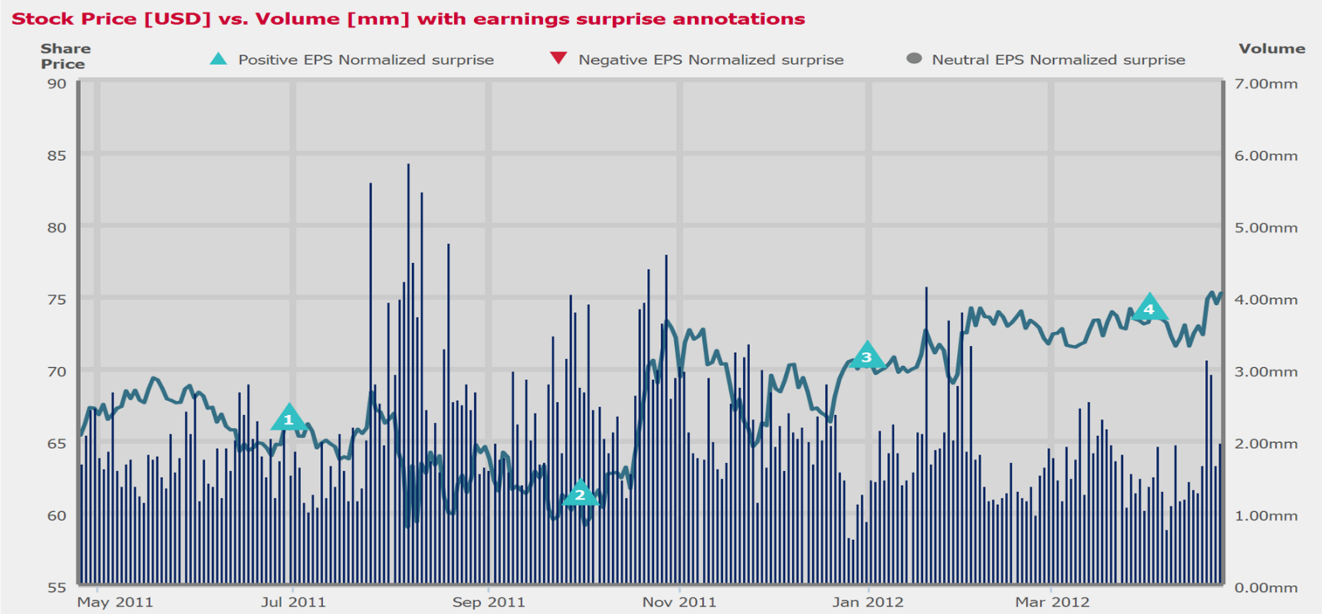
FQ2 2012 Earnings Call Transcripts

Wednesday, July 25, 2012 12:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ2 2012-			-FQ3 2012-	-FY 2012-	-FY 2013-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.90	2.17	14.21	1.76	7.78	7.76
Revenue (mm)	3884.09	4130.00	6.33	4247.20	15183.26	15954.85

Currency: USD
Consensus as of Jul-25-2012 1:29 PM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ2 2011	1.63	2.01	23.31 %
FQ3 2011	1.77	2.22	25.42 %
FQ4 2011	1.79	1.94	8.38 %
FQ1 2012	1.87	2.05	9.63 %

Table of Contents

Call Participants

EXECUTIVES

Brian Edward Dowd
Executive of Office of The Chairman

Evan G. Greenberg
Chairman, President & CEO

Helen Wilson

John W. Keogh
Chairman

Philip V. Bancroft
Executive VP & CFO

Sean Ringsted
Executive VP, Chief Risk Officer & Chief Digital Officer of Chubb Group

ANALYSTS

Amit Kumar
Macquarie Research

Brian Robert Meredith
UBS Investment Bank, Research Division

Gregory Locraft
Morgan Stanley, Research Division

Ian Gutterman
Adage Capital Management, L.P.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

Joshua David Shanker
Deutsche Bank AG, Research Division

Lawrence David Greenberg
Langen McAlenney

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

Meyer Shields
Stifel, Nicolaus & Company, Incorporated, Research Division

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Michael Zaremski
Crédit Suisse AG, Research Division

Thomas Spikes Mitchell
Miller Tabak + Co., LLC, Research Division

Unknown Analyst

Vinay Gerard Misquith
Evercore ISI Institutional Equities, Research Division

Presentation

Operator

Good day, and welcome to the ACE Limited Second Quarter 2012 Earnings Conference Call. [Operator Instructions] For opening remarks and introductions, I would like to turn the call over to Helen Wilson, Investor Relations. Please go ahead.

Helen Wilson

Thank you, and welcome to the ACE Limited June 30, 2012, second quarter earnings conference call. Our report today will contain forward-looking statements. These include statements relating to Company performance, guidance, premium growth, ACE's business mix and acquisition, impact of catastrophes and droughts and pricing and insurance market conditions, all of which are subject to risks and uncertainties. Actual results may differ materially.

Please refer to our most recent SEC filings as well as our earnings press release and financial supplement, which are available on our website, for more information on factors that could affect these matters. This call is being webcast live and the webcast replay will be available for one month. All remarks made during the call are current at the time of the call and will not be updated to reflect subsequent material developments.

Now I'd like to introduce our speakers. First, we have Evan Greenberg, Chairman and Chief Executive Officer, followed by Phil Bancroft, our Chief Financial Officer. Then, we'll take your questions. Also, with us to assist with your questions are several members of our management team.

Now it's my pleasure to turn the call over to Evan.

Evan G. Greenberg
Chairman, President & CEO

Good morning. ACE had a very good second quarter marked by excellent operating earnings, strong broad-based premium revenue growth and an improving P&C pricing environment in a number of areas of the world. Book value growth was up modestly in the quarter, as we were impacted by the euro debt crisis and the consequence like to safety which affected foreign exchange and interest rates and equity markets. After-tax operating income for the quarter was 743 million were 2.17 per share, our operating ROE was over 12.5%. For the first 6 months, we have produced almost $1.5 billion in operating income and an ROE again of 12.5%.

All the visions of the company made a positive contribution to the quarter's results, our underwriting results this quarter were again outstanding as illustrated by a P&C combined ratio of 88.7. The strong calendar year results benefited from both favorable current accident year experienced and positive prior period reserve development.

The current accident year results were excellent both with and without the impact of cat losses which were relatively light this quarter at 55 million pretax. ACE's underwriting performance has been consistently strong all year with over 890 million in underwriting income and a combined ratio of about 89% for the first 6 months.

Investment income held up pretty well in the quarter, it was down only modestly despite the historic low interest rate environment. The strong operating fundamentals contributed to book value growth of 1.3% in the quarter that was impacted by mark to market losses and for financial markets and foreign exchange movements.

Book value was up almost 6% year-to-date. Bill will have more to say about the markets impact on our investment portfolio, the VA mark and foreign exchange. We announced a small but important acquisition last month Asuransi Jaya Proteksi, one of Indonesia's top general insurers and a leader in personal lines.

The company which has an extensive branch network and distribution system will complement our existing business and diversify our presence in Indonesia with a well-established personal lines franchise.

The transaction is expected to close later this year, ACE's total company net premiums in the quarter grew 4.5%, or 6.5% adjusting for the impact of foreign exchange. Our growth in the quarter came primarily from 3 regions of the world, North America, Asia, and Latin America.

North America grew over 7% in the quarter or approximately 10% excluding crop insurance. We had excellent growth in commercial P&C both retail and wholesale as well as personal lines. In Asia, and Latin America we were up 16% and 23% respectively, with strong contributions from P&C, A&H and personal lines which all grew at double digit rates in original currency. Growth in Europe in the UK on the other hand was flat due to both market and economic conditions.

In North America some of the product lines where we saw our best growth were in primary risk management business which was up 9%, retail, general and specialty causality lines of business and aggregate which were up 11% and property which was up 27%. Our U.S. E&S wholesale business was up 24% led by property which was up 37%, our high net worth personal lines business in the U.S. was up 15 points.

In our international business, property was up double digit in Latin America and Asia as was marine while energy related classes in aggregate were up double digit globally. A&H growth globally picked up in the quarter as expected and this trend should continue for the balance of the year. A&H premiums excluding combined were up about 9% globally in constant dollars.

Led by Asia with growth of 17 and Latin America with growth of 15%, combined insurances premiums were down about 4.5% which was better than what we planned. Growth combined is beginning to trend upward and should be neutral by year end or by first quarter next year with growth from there.

The underlying fundamentals Europe aside are definitely improving. Our global re-business was up over 9% in the quarter led by Bermuda which was up 18%, we benefited from continued cat price increases on Japanese renewals at 401 and also from price increases on U.S. wind business.

Crop insurance revenue was down 1% in quarter inline with our expectations. Crop premiums as I explained on our last call are impacted by commodity prices, there is much discussion about the drought conditions in the U.S. In some states quite severe and with a serious impact on crops. Based on conditions as they stand now and given our portfolio mix by state and crop we will adjust our crop loss ratio for the year up in the range of 5 points during the third quarter bringing our crop related business combined ratio to between 93% and 94%.

This year-to-date loss ratio changes equal to about 68 million after-tax. This is our best estimate at this time. We continue to closely monitor crop conditions for changes that would lead us to alter our view, if the current drought conditions worsen and continue till harvest, our modeled worst case loss based on what we know would be an additional circa 200 million after-tax.

We are not predicting this outcome. We are simply letting you know the outer bounds of reasonable worst case. To put the 5 point loss ratio adjustment we are now taking in perspective, the 68 million is less than the difference between our actual nat cat losses and our cat load for the first 6 months of this year, a difference that is benefited our earnings by 75 million.

So with this moment we remain within our year-to-date current accident year projection, while crop is not part of our cat load these drought conditions are another form of cat. The one area basis potentially worse, another can be better, showing the benefit of our diversification balance of business and risk management.

Returning to the quarter I want to make a few comments about pricing and the market environment, but to put our revenue growth numbers in perspective. The positive U.S. pricing trend we have been discussing the last 2 or 3 quarters continued to improve again in the second quarter, if rates further increasing that will be gradually.

Prices in the second quarter were better than in the first, the rate increases were again more broad-based than in the first quarter which was better than last year's fourth. This included many casualty lines, the professional lines for example turning positive, while property rates held up quite well and equaled to the level of pricing we saw in the first quarter.

For the first time, pricing in our international operations in aggregate turned positive up 3% led by cat exposed property, UK causality and across the board slowing of rate decreases in another classes. Even professional lines internationally in aggregate turned positive and showed a 1% rate increase. Let me break this down a bit further beginning with North America.

Overall, for the quarter pricing in North America, was up 4.7% and we achieved better pricing on our new business when compared to our renewal book.

The average rate increase for our retail business went from 2.6% in the first quarter to 4.1 in the second quarter. Similarly, in our wholesale business, the average rate increase went from 6.6 in the first quarter to 8.4 in the second and remember, in reporting rate increases in ACE we separate out exposure growth which was up 3.1% in the quarter.

The U.S. retail on wholesale property book led our rate increases with rates up 14% and 10% respectively. Our U.S. retail causality book achieved positive 5% rate and this excludes risk transfer workers comp. Risk management business pricing was up 3%, the management liability D&O pricing was up 4%.

Finally our E&S portfolio pricing was up 8.5 overall. We have positive rate in all E&S classes. We are achieving this pricing in a marginally more disciplined marketplace, our new business writings in North America grew 30% year-on-year while the renewal retention ratio is measured by premium and U.S. retail was 97% and on a policy count basis it was 84%.

John Keogh and John Lupica are with me and can provide further color on market conditions and pricing trends globally. In summary we had a very good second quarter and posted strong first half results and we are optimistic about our growth prospects for the balance of the year.

P&C pricing globally has turned more favorable and we are well positioned to take advantage in many places around the world, although we face the uncertainty from deteriorating, economic and geopolitical conditions impacted by the euro area debt crisis and U.S. fiscal cliff.

Our earnings prospects for the balance of the year look good with a notable exception to crop insurance. With that I will turn the call over to Phil and then will be back to your questions.

Philip V. Bancroft
Executive VP & CFO

Thank you, Evan. We ended the first half with a very strong balance sheet and capital position. For the quarter, cash and invested assets grew by almost 1.4% to 58.3 billion. Operating cash flow was strong at 811 million, tangible book value per share grew 1.7% in the quarter and is up about 6.5% for the year.

Net realized and unrealized losses were a 138 million pretax including a 266 million gain from the investment portfolio and a 397 million loss from our variable annuity reinsurance portfolio. The gain from the investment portfolio resulted primarily from declining yields of investment grade bonds while the VA loss resulted primarily from decreases in worldwide equity values and a decrease in long term interest rates.

Year-to-date the net loss from our VA re-insurance book was about a 120 million. Our investment portfolio is in very good shape, we have no direct exposure to sovereign debt of distressed European countries and our exposure to Euro zone financial institutions totaled 1.1 billion or less than 2% of the portfolio and is concentrated in Northern Europe. The overall credit quality of our Euro zone financial institutions securities is AA with over 550 million rated AAA.

Investment income was 537 million for the quarter and was inline with our expectation. Our current book yield is 3.9%, currently money rates are 2.8% if we invested in the similar distribution to our existing portfolio. We estimate the current quarterly investment income run-rate will be approximately 530 million on average with some marginal variability up or down.

Foreign exchange had a negative impact in the quarter reducing net income by 24 million and book value by about a 100 million. Our net loss reserves were up 66 million in the quarter after adjusting for foreign exchange. During the quarter, we had positive prior period development of about a 100 million after-tax primarily from short tail lines.

Cat losses after-tax were 40 million for the quarter. The current accident [ph] year P&C combined ratio excluding cat losses is 2.7 percentage points lower than last year's quarter. This is due primarily to our successful efforts to shift our book of business through profile management to our higher margin products, our ability to achieve rate and growth in our short tail classes and fewer large losses in the quarter in property and energy this year versus last year.

Our press release issued last night included our updated guidance for 2012, our range is now $7.20 to $7.60 in after-tax operating income per share for the year. First, the update reflects the positive prior period reserve development and lower than planned cat losses in the first half of $0.74.

Second the update includes a reduction of $0.19 to reflect a projected third quarter increase in our year-to-date crop insurance loss ratio. Finally, the guidance includes estimated cat losses of 270 million after-tax for the second half of the year.

As usual, our guidance for the balance of the year is for the current accident year only. With that I will turn the call back over to Helen.

Helen Wilson
Thank you, Phil, good point. We will be happy to take your questions.

Question and Answer

Operator

And we will take our first question from Amit Kumar from Macquarie.

Amit Kumar
Macquarie Research

Macquarie Capital. My first question relates you know what would be helpful if you could get the distribution of crop hail versus NPCI in your crop book and maybe also talk about Group 1 versus Group 2 and 3 states.

Evan G. Greenberg
Chairman, President & CEO

Yes, we are not doing that. We have given you what you need to know as an investor, our projection where we do the projections and if there is any material change to the estimate as we put out there we will notify the street in -- all investors in a timely manner.

Amit Kumar
Macquarie Research

Okay, how about this, can you talk about the impact of the stop-loss program in your crop book. I presume when you mentioned the 93%, 94% numbers those do not factor in the stop-loss, but probably the 200 million which you gave us factors in stop-loss is that a fair assumption?

Philip V. Bancroft
Executive VP & CFO

It factors in any of our estimates, factor in our re-insurance protections. Both the risk sharing we do with the federal government and any private sector re-insurance that we place.

Amit Kumar
Macquarie Research

Okay, how about this, final question, there is this debate that this could be similar to 1988 and maybe just comment on what we are seeing in 2012 versus what we saw in 1988. I guess, the program was a lot different at that time, but maybe just give us some color as to where do you think this might be versus what we have seen in the past.

Evan G. Greenberg
Chairman, President & CEO

You're correct, this is the -- these are the worst drought conditions that we have seen in the -- that has been experienced in the farming community since 1988. It is broad-based though it is very much concentrated in the mid-west states and in 1988 crop insurance was much less factor in the overall financial pluming of the agriculture industry. It's far more wide spread and taken up as a valuable protection and this is center piece for the support of the agriculture industry today than it was in 1988. But these are the worst drought conditions we have seen, have been experienced since '88 that is true.

Amit Kumar
Macquarie Research

I guess just related to that, there is this debate that I guess smaller companies might be up for sale down the road just based on what's happening would ACE be interested in sort of that or you feel that you are that the current position is good enough. You don't need to acquire any more companies going forward especially as it relates to the crop program.

Evan G. Greenberg

Chairman, President & CEO

Thank you for your questions. I think we can't dominate the call there are many others in the queue who want to ask a question and we will move on now. So thank you.

Operator

And we will take our next question from Matt Heimermann from JPMorgan.

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

Couple of questions, first was just with respect to the A&H business and combined in particular, I guess can you just remind us what kind of gives you conviction that we are going to bottom out and spring the neutral next year. I think the international side is a lot easier to get your arms around from an external perspective.

Evan G. Greenberg
Chairman, President & CEO

You are talking about combined specifically, Matt?

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

Yes.

Evan G. Greenberg
Chairman, President & CEO

It's what we see and in the real fundamentals of -- remember that's an agency distribution channel and so what we see in both growth in number of agents, productivity per agent retention of business of renewal retention of business and the trends in that have turned positive or neutral in a number of territories, Canada, Australia, New Zealand, the United States where the core of the business is and it's those fundamentals that really is what I and the management team measure on a monthly basis and a quarterly basis and we see sustained what we can now have confidence is trend in that, I think management is doing a really good job and there is no guarantees around it. It's what gives us the confidence that it's on the out swing that way.

Philip V. Bancroft
Executive VP & CFO

As I remember it takes you have to see at that way first, because it's you know it's 150 to 300 bucks a policy.

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

Okay, that's helpful. I guess another question we just with respect the rate you are pushing at, in the past you have kind of talked about you know a need for a lot more rate and kind of to sustain themselves to kind of make this real material overtime. I guess, how comfortable are you with your ability to kind of keep pushing rate and kind of finding this incremental opportunities as we kind of seem to be hitting a point where rates at least that some companies are staying to plateau out.

Evan G. Greenberg
Chairman, President & CEO

With some, and you will be able to ask my colleagues who would be prepared to give you more color around this, but here is what I would say about what we see at the moment about pricing. Property pricing is reasonably robust, particularly if it has any cat exposure around it and while the rate of increase has obviously flattened out and is decelerating it's still positive rate on what is reasonably robust on pricing, as I say particularly that has cat around it, when you get the casualty lines the price increases are more broad-based and while they're far more muted we are seeing that they are sustained, the rate of increase is not declining if anything it's accelerated to debt and it is more broad-based. Now how long that could, that's obviously ameliorating and it varies by line of business if you were -- if it exceeds trend in any class then you are actually gaining on an accident year. If the rate of increase is equal to trend then you are not deteriorating any further and if it's below trend it's ameliorating the decline. So in any event, any rate is good rate and it is more broad-based than it was and our risk selection capabilities have only improved, and we are getting better risk reflected pricing because we are more insightful on our portfolio than we were even a year ago or 2 years ago.

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

And that last point, is it fair to assume that like separating the good versus the bad maybe this time around that will be the differentiator, it's just how intelligent the underwriting is in terms of risk selection rather than your ability to just kind of pump rate through an entire portfolio.

Evan G. Greenberg
Chairman, President & CEO

I think it's so axiomatic about the insurance business is that your ability to select better, is what differentiates you in the marketplace, period and your results, you know that's it that's the guts of the business, that's underwriting.

Operator

Let's take our next question from Michael Nannizzi from Goldman Sachs.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Just one quick follow-up on, I was trying to put my head around this so, if this is a worst-case year and well effectively a cat year and it sounded like from your mouth it would be about a 10 point like a 110 or maybe 115 point combined ratio. Just trying to understand the risk management part of that and how big of a role reinsurance have to play in that sort of risk return. Just follow-up.

Evan G. Greenberg
Chairman, President & CEO

Risk management is at every level of the business when you think about it, because first incident how good your data and how insightful are you in selecting one farm versus another farm and understanding that, how much concentration you take by county, one versus another. How much concentration you take within a state and how you balance your portfolio. And then understanding and having the data as we have, we have both the computer power, the software programs and years and years of data to be able to do scenario analysis. Now while none of its perfect because the past is hardly the reflection of the future. It makes you more insightful and then your ability to do portfolio management, because this is a government private sector risk sharing and then from there what you do you, how insightful are you to understand your concentrations and then further if you choose to protect your own retentions with stop-loss or any other forms of reinsurance protection which we do.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

And do you expect the reinsurance will get more expensive then, it sounds like the reinsurers will be absorbing some of this loss. Do you expect that cost for protection next year will be more expensive given this year's loss experience?

Evan G. Greenberg
Chairman, President & CEO

You know I can't speculate on that, remember cat is a, crop is like a cat business too and it's long term and the pricing reflects long term experience not just a moment to moment change. So I really can't speculate on that, I don't know.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

If I could one quick one for sale, alternative investment income sorry, I think Huatai Life is a big part of the other investment income but that piece is now about a third of investment income, just trying to get an understanding of what drives that seems like about a 20-plus percent return and is it mostly the private investment there and how should we think about that as it becomes a bigger part of the overall pie and thanks.

Evan G. Greenberg
Chairman, President & CEO

Huatai Life is actually a part of other income that's other investment income right, so other investment income is predominately private equity and hedge funds as they contributed about $10 million of income to the quarter.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Huatai Life did.

Evan G. Greenberg
Chairman, President & CEO

No, Huatai Life is not a part of our investment income it's a part of other income which is down below the line, it's a partially owned subsidiary, so we don't include them in our investment income.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Okay, so can you help me understand the contributions of fixed income was about 2.8% yield from the supplement so it seemed like 350 million, the total investment income was low 5, so just trying to understand what is the rest of the piece and is that a yield, how should we think about as it becomes a bigger part of the pie.

Evan G. Greenberg
Chairman, President & CEO

Okay I will tell you what Michael can we take this offline?

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Sure, sure.

Evan G. Greenberg
Chairman, President & CEO

I will take you through it. I want to give you a one piece of information on crop that I think rather just than the general that I can give you specifically. Our stop-loss protection attaches at about a 104% combined ratio and it runs up to about a 154% combined ratio.

Operator

We will take our next question from Greg Locraft from Morgan Stanley.

Gregory Locraft
Morgan Stanley, Research Division

Just wanted to actually pursue sort of a question I've been getting from investors with investment yields where they are at, with your excess capital being you know where it's at a drag of say a 150 plus on the ROE and then now we are living through the worst crop loss probably in the history of the industry, it's actually, these results are amazing, double digit ROE, the guidance is strong and I guess, what is allowing ACE to outperform the peers given the headwinds especially what is -- usually when a company takes a loss like this the numbers do fall versus peers but you're laying out top quintile results even with this loss.

Evan G. Greenberg
Chairman, President & CEO

I am going to try to answer that, I am going to answer that for you but I am going to say this, I think it's is right in front of you and it's right in front of everyone, it shows itself right in the numbers in a reasonably transparent way and that is why you see our geographic spread and where we are growing and we are growing where we know we can make an underwriting profit and there are areas of the world that are doing better economically than other areas of the world and the need for insurance are growing. Secondly, you'll look at our product spread, commercial P&C is now about 60%, the U.S. has become a growth engine for us in the last 2 quarters along with Asia and Latin America, and you see an improving pricing environment and ACE is taking advantage of that, because we did trade market share for underwriting in the past and we engaged in better portfolio management and shared business where we couldn't make a reasonable return i.e. E&S casualty, i.e. risk transfer workers comp, where we said we can't make the money we will get out of those things and we will focus on other areas. We are a specialty underwriter, where an underwriter makes a difference to our broad spread of casualty products in the U.S. and globally our growth in commercial P&C in Latin America and in Asia and then while our ability to write a profitable book in the U.K., because we focus on casualty and energy and construction and property where we can make an underwriting profit. And then you complement that with our A&H book which has been built brick by brick on in those economies of the world where we see that rising middle class and that [indiscernible] and that balance it brings to our overall business. And crop insurance is a great business over any period of time, it has been very good and because we have a got a great insightful franchise in that business, but it's a cat business and right now at this point while the earnings are under more pressure they are still projected to be reasonable and the risk reward balance within that. We think between public sector sharing and private sector protection we've got the risk reward balance of what we could lose in a bad year versus what we could earn so our management of risk concentration. We focus a lot on it, because this is fundamental in underwriting company that's what we do and I think you know from there we have been saying it, we are planting the seeds today what you see as results or the things we've been working on the last 7 years, and the things we have been planning the seeds for, in the last 2 or 3 years they'll begin to show in years to come, we are long-term builders and that's what you can tell your investors.

Operator

We will take our next question from Mike Zaremski from Credit Suisse.

Michael Zaremski
Crédit Suisse AG, Research Division

Evan in regards to the updated guidance and I know you can't see my model but if I strip out reserve releases.

Evan G. Greenberg
Chairman, President & CEO

I don't want to see your model. I have seen too many models.

Michael Zaremski
Crédit Suisse AG, Research Division

If I strip out reserve releases below plan cat losses and the crop guidance, the guidance I guess appears to imply no margin improvement or maybe even some deterioration, whereas there was clearly considerable margin improvement this quarter and pricing momentum has continued. So does that imply there were some one-time items positively impacted this quarter?

Evan G. Greenberg
Chairman, President & CEO

I don't think so, what I would say is that our guidance is almost the same where we started the year and when we started the year we had an anticipation that we would be earning these results so these really reflect what we have in our base plan. The other thing we did obviously is reduce the guidance for the crop, the $0.19 of crop. Remember something if we have pricing better than we assumed in our plans it's got to earn its way through. These are pretty good current accident year projections for the balance of the year.

Michael Zaremski
Crédit Suisse AG, Research Division

I agree, Phil you said reserve release is primarily stemmed from short tail lines. I think that differs from previous quarter trends, should we read anything into that and can you provide color on the reserve leases this quarter.

Philip V. Bancroft
Executive VP & CFO

No not at all. I mean it's a seasonal thing, because we have reserve studies all throughout the year and in this period the reserve studies were basically on the shorter tail lines.

Michael Zaremski
Crédit Suisse AG, Research Division

Okay and lastly this does relate to crop but, so the crop impact this quarter’s results in terms of…

Philip V. Bancroft
Executive VP & CFO

No it did not; we don’t believe it's a second quarter event. The issues with crop really emerged in July with the weather that we had in July. So it would be something that’s going to effect the third and fourth quarters.

Operator

We will take our next question from Vinay Misquith from Evercore Partners.

Vinay Gerard Misquith
Evercore ISI Institutional Equities, Research Division

The first question as in growth and I think you talked about it a little bit earlier in the call and last quarter too but looking at new business up 30% and I think retentions remain pretty reasonable just wondering how ACE is managing to outperform peers who are having weak retentions and weak new business.

Evan G. Greenberg
Chairman, President & CEO

You know I can’t opine on peers, that’s not my job and so whatever their results are their results, they have different mixes of business, they have different distribution, they have different geographic concentrations or kinds of customer concentration. So I or my colleagues can answer the questions specifically about ACE that we think you know obviously, to us the results we see are logical and make all the sense in the world to us. One thing I told you last quarter that I will keep in mind. Our new business writings are dropped off substantially year-by-year-by-year, as they should, it's rational in a soft-market. So the kind of increase, it's 30% but it's on a relatively small base of new business and I said that last quarter when we had robust growth and I tell you that again.

Vinay Gerard Misquith

Evercore ISI Institutional Equities, Research Division

Sure that’s fair enough. Then as we look at growth in the future, do you think that the slowdown, the economy worldwide will have a negative impact on growth and also your ability to raise pricing.

Evan G. Greenberg
Chairman, President & CEO

ACE doesn’t exist in a bubble, and I think the global uncertainties that really emanate from Europe and from the United States and that are impacting that are political and are impacting the economic fundamentals create both headwind and a great deal of uncertainty and inability to predict. I talk to a lot of CEOs in a lot of different industries and what is very clear, their level of confidence in the future and their ability to predict with any confidence is at a relative low point right now and for the obvious reasons and if we don’t get our leadership and political act together both in the U.S. and in Europe, this has an impact on economic growth and it will and insurance you know we are a reflection of activities to society at large beginning with economic activity.

Vinay Gerard Misquith
Evercore ISI Institutional Equities, Research Division

Fair enough, one last question if I may just on margins, you have had strong price increases in the U.S. maybe flattish outside the U.S. but you have grown more on property line. So do you expect margins maybe to slightly improve next year versus this year?

Evan G. Greenberg
Chairman, President & CEO

No I am not predicting it at this moment. You know I get the mix question I don't -- but I don't want to give you an off-the-cuff the answer and don't have a thoughtful answer for you right off at the top of my head.

Operator

We will take our next question from Larry Greenberg from Langen McAlenney.

Lawrence David Greenberg
Langen McAlenney

Evan I am just wondering if you'd be willing to elaborate on and really what has to happen in crop for conditions to worsen and I guess, I'm just wondering as we sit here today does your current assumption incorporate the highest probability outcome from any visibility that we might have.

Evan G. Greenberg
Chairman, President & CEO

It does yes, it does incorporate the highest probability outcome both our current projection as we have it and what I told you guys as what we can model as a worst-case is on the highest probability outcome to us, yes and look what I gave you and I said it clearly, but I am going to say it again the $0.19 that we just took that we are going to take in the third quarter as a charge is based on the conditions today as we see them.

We don't expect that it's worse than that, if we thought it was worse than that then it would be $0.19, it would be a different number. But what we do know is there still that question out there, could it be worse and no one can predict the weather but what we have said, we said was these drought conditions continue right and you got this and it continues right up to harvest time, what is that likely worst case outcome and that's why we put that number out there. It can be anywhere in between right now, we are at $0.19 and that’s the honest representation of it.

Lawrence David Greenberg
Langen McAlenney

Great that's helpful and you know the volumes in agriculture was flat year-to-date, you had said that you expected it to be down 250 for the year. Is that still the case that you would expect agriculture premiums to be down that much?

Evan G. Greenberg
Chairman, President & CEO

Expected to be down closer to Brian Dowd? A 175 million and so we'll see, it will be less than the 250 and you will see that it will show itself.

Operator

And we will take our next question from Jay Cohen from Bank of America Merrill Lynch.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Topic of the day, crop insurance, just a couple of questions. Phil you had mentioned that the effect of the drought will be in the second half of you said third and fourth quarter. I am assuming the $0.19 kind of incorporates sort of an annual impact, or would you expect an additional loss in the third quarter and excuse me in the fourth quarter.

Philip V. Bancroft
Executive VP & CFO

We were saying that we are going to increase our loss ratio of crop in the second half. In the third quarter, will increase max.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Got it, okay. And the second one it's a small number but the earnings from the ag line were up pretty substantially from a year ago and I am wondering what drove that.

Evan G. Greenberg
Chairman, President & CEO

Brian is giving answer to that question but let's be specific, the crop adjustment year-to-date in the third quarter, the loss ratio is raised 5 points year-to-date in the third quarter. The fourth quarter will carry that same loss ratio that raised loss ratio that's in your $0.19 so it effects both the third and fourth quarters.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Got it.

Evan G. Greenberg
Chairman, President & CEO

Okay, our second question, Brian?

Brian Edward Dowd
Executive of Office of The Chairman

Second question, I guess, I think was the year-over-year ag results and this year, remember last year in the farm on the book we had cat activity both flood and tornado losses that's the real difference this year second quarter, [indiscernible] for us on cat loss. On the farm versus the crop specific question, crop no real change year-over-year.

Operator

And we will take our next question from Joshua Stirling from Sanford Bernstein.

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

So I was hoping to just get a little bit more color on pricing, commentary obviously that's it's broadened some of the causalities line, that professional line seem to be taking up internationally is great, would love to get your color though on if this is leading you to reset your sort of general underwriting posture which has been sort of very property focus versus causality over the past couple of years. I mean obviously and the numbers you reported it looks like you did increase you're casualty writing this year and with pricing up it will be nice to know if you think that's something that we should broadly see sort of a better place for opportunities these days.

Evan G. Greenberg
Chairman, President & CEO

No, I don't agree with how you are viewing it at all. We have many more casualty underwriters in this company than we have property and in fact we have many more casualty units in the company and we have property units, the fact is we play ball the same way in a soft market as we do in a better pricing market. It's just what's the return we get for the effort. So guys are just getting guys and gals are just getting better returns for their effort right now. So we may have quoted a hundred risks a year ago in a certain casualty line of business and our pricing and terms and conditions would have called for ACE and that could have placed us right outside the market and others would it cheaper and so they win and we lose or in our way of thinking about it they lose we win. And now those same risks we are underwriting them the same way and however, the market has raised its standards and so we are more successful in securing those accounts now. We have not switched our focus, the people who do those lines for living, that's all they do for a living so they are focused on them. It's just the yield for the effort.

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

So marginal change of environment.

Evan G. Greenberg
Chairman, President & CEO

We don't take property underwriters; we don't take property underwriters and put them in the casualty department.

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

If I could ask one another headline question, although it's not the headline question we all are talking about. Obviously you guys have been defensively underwriting for couple of years broadly and Europe stresses is sort of not an open area is not new news. I would love to get a sense of some of the policies and sort of just generally, sort of industry areas on the liability side that you have been sort of defensively positioned around and I am thinking at things like industry exposures to surety, trade credit, political risk, other financial lines, areas where perhaps you've been monitoring the environment and perhaps so should we.

Evan G. Greenberg
Chairman, President & CEO

You are thinking in context Josh, of Europe?

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

Yes, I am sorry, in Europe.

Evan G. Greenberg
Chairman, President & CEO

Got it, fine, both in Europe and outside Europe related to Europe.

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

Yes.

Evan G. Greenberg
Chairman, President & CEO

Okay, I am going to ask John Keogh to maybe give you some color around that.

John W. Keogh
Chairman

Josh, I will give you some color around our trade credit business since you asked and sure the question is to have is to impact of Europe potential and the book of business. One I can tell you right now from what we are seeing in terms of claim notices or potential for claim activity in Europe or anything that's coming in other parts of the world as a result of the economic slowdown in Europe. Right now, there is nothing we see that is outside we planned for in our loss claims for clinical risk and trade credit. Having said that we do run models and do run realistic disaster scenarios on those books of business and when we run an RDS that showed what we think would be an extreme event, but nonetheless one that we model which is a breakup of Europe where the [indiscernible] in core France, Germany seg in the Europe and what that would mean in terms of loss due to political risk and trade credit business, that model is out to 150 million poor state scenario for loss for us. As respect to surety, we have not been a market for surety in Europe.

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

Great, and just thinking about those sorts of numbers in the political risk business, is that function of you guys sort of mass exposure there, or do you think that's something we could extrapolate to sort of broader industry, industry exposures.

John W. Keogh
Chairman

Don't extrapolate, that was an RDS scenario specifically around a euro breakup defined as the PIIGS countries leaving the Euro zone and what would be, that's a stone in the global pond and so what would be your global losses in trade credit, political risk as a result of that. Wasn't just the losses in Euro zone region, it was caused by Euro zone breakup, what would be your losses globally in trade credit, political risk.

Operator

Our next question comes from Brian Meredith with UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

So just a point of clarification to 5 points that you said is that for crop or the total ag buck.

Evan G. Greenberg
Chairman, President & CEO

Crop.

Brian Robert Meredith
UBS Investment Bank, Research Division

Just crop, that's what I thought okay. And then just quickly the North American growth, how much of that is coming from recent acquisitions like Penn Miller.

Evan G. Greenberg
Chairman, President & CEO

Very, very modest. Penn Miller was roughly 70 million of annual premium.

Brian Robert Meredith
UBS Investment Bank, Research Division

Got you, so it's organic.

Evan G. Greenberg
Chairman, President & CEO

Yes.

Brian Robert Meredith
UBS Investment Bank, Research Division

Great. And then last question, just curious the growth you are seeing your property business, what impact is that having on your PMLs and do you kind of think about that potentially won't accept some more volatility here going forward just because of the attractiveness of the property versus the casualty business.

Evan G. Greenberg
Chairman, President & CEO

Brian to-date we have really not increased our PMLs, we have kept them they are steady and the growth we have seen in exposure is within the PMLs as we establish them. Would we be willing? Let's see how pricing looks and opportunity as it presents itself but we have not had we have not increased our PML exposure.

Brian Robert Meredith
UBS Investment Bank, Research Division

Just one another quick one just curious, Evan are you seeing any benefit from or any flight to quality going on right now particularly with what's going in Europe and there has been some ratings activity and somebody European insurers, is that been a benefit to you and going forward.

Evan G. Greenberg
Chairman, President & CEO

Not really, John you want to add any color on that?

John W. Keogh
Chairman

Not yet, Brian, I mean that was your question that we are looking at on the ground in Europe but right now I think it's relatively stable, so the culture there especially the people don't move as quickly and reactions to those kinds of situation that they might be on the U.S. so I think if there is an opportunity it's going to be in front of us as opposed to easily [ph].

Operator

Our next question comes from Thomas Mitchell from Miller Tabak.

Thomas Spikes Mitchell
Miller Tabak + Co., LLC, Research Division

This is a sort of a broad conceptual thing but if the Central Banks around the world continue to attempt to keep interest rates as low as possible both short-term and long-term for an extended period of time let's say another 2 years or so, it strikes me that that puts tremendous pressure on underwriters who are less skilled at making underwriting profits than perhaps you are. And I'm wondering if you are observing that you having a relatively an advantage relative to other insurers is actually helping you gain market share in the market you want to be in.

Evan G. Greenberg
Chairman, President & CEO

Well Tom I think what you're saying to me if I didn't speculate and look forward and just took the current environment, the current pricing environment is not driven by balance sheet pressures you know it's really driven by ROE pressure because of low interest rates, they are already low. Investment income is therefore declining for the industry, the yield is declining and so and loss ratios have climbed to point where ROEs are just so under so much pressure that has driven pricing and that is a rational response, as opposed to where it's real balance sheet pressures. And I think that's and so you have already seen that, and as the marketplace becomes more disciplined in underwriting it creates varying degrees of opportunity for us which really varies byline, by territory and based on our view of what is the experience in that line of business today relative to its price need, relative to what the marketplace will allow in terms of price. And so I think what you're speculating out loud, you are actually already seeing it and the question is as to what degree does that continue, accelerate, broaden geographically and that's a question mark, no one knows. The good news here is we don't need to speculate a lot about it because we are ready when it occurs, when pricing improves and it presents opportunity, we are all day long working on our capability to just be there ready to take advantage of it.

Thomas Spikes Mitchell
Miller Tabak + Co., LLC, Research Division

Well that makes a great deal of sense and then my second question is I think I know the answer, I don't think it will surprise if answered, but I was looking for the potential for a silver lining in this drought, is it possible that the silver lining could be that crop prices are higher in the next crop year and that you end up writing a lot more business.

Evan G. Greenberg
Chairman, President & CEO

Commodity prices?

Thomas Spikes Mitchell
Miller Tabak + Co., LLC, Research Division

Yes.

Evan G. Greenberg
Chairman, President & CEO

That's possible. If I was a good or you are a good commodity price pickers we would be the world's great commodity traders and that's not what either of us do, but of course it's going to depend on global crop conditions, as well as projected U.S. weather conditions. And we all know how easy it is to predict the weather.

Operator

And our next question comes from Paul Newsome from Sandler O'Neill.

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

I wanted to I will also ask a several broad question, my supposition is that as prices increase broadly we should see retentions decline and as well as an acceleration of E&S versus primary. I am not sure, we have seen that and I was curious as to particularly given your large E&S business if you thought there was a reason for that this time around.

Evan G. Greenberg
Chairman, President & CEO

Well I don't think you're looking at a raw, hard market. I don’t view this is a hard market, I view it as a that we are in a pricing correction period, hardly in a hard market and I define that broadly were prices are broadly adequate, or beyond what you require to beat your hurdle rates in terms of combined ratio on current accident year business. So I start with that, secondly when I tell about E&S is while and it's true about a lot of classes that while pricing is improving E&S casualty lines pricing is not improving enough to broadly make most E&S casualty lines attractive underwriting perspective. To me it's sort of like you know the akin workers comp where you look at if the industry is running or 117 or a 120 great you are getting 8 or 10 points, it's hardly enough and you add trend, then put it in the black from an underwriting perspective while that’s true about most E&S casualty lines. So you are not seeing that classic pattern that you would imagine. Though you are seeing incrementally greater opportunity than there was in E&S lines.

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

And throughout it's raining in our farm.

Evan G. Greenberg
Chairman, President & CEO

Good, so you won't be making a claim to us.

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

I think it's way too early to tell.

Evan G. Greenberg
Chairman, President & CEO

Spoken like a true insured.

Operator

Our next question comes from the Josh Shanker from Deutsche Bank.

Joshua David Shanker
Deutsche Bank AG, Research Division

I know there has been too many questions on crop but it's really what everyone wants to know, can you talk a little bit about the reinsurance markets and business that you are seeding and given your scenarios how big a loss you are anticipating for the industry both in your modeled $0.19 versus your worst-case scenario?

Evan G. Greenberg
Chairman, President & CEO

No. Sorry Josh, on the reinsurance side I gave a little bit about how our stop-loss works, that’s as far as I am going to go on that and how the industry is going to run overall in crop insurance is way too early to know, we have no idea. You can talk about us and I can only tell you what I already said about us but I think is pretty fulsome.

Joshua David Shanker
Deutsche Bank AG, Research Division

Well then I will try one more wave I am sure I will be denied, can you talk about you never know, maybe I will get lucky. For your reinsurance in terms of the loss that you are seeding sizeable or right now your retention is high given you’re forecast?

Evan G. Greenberg
Chairman, President & CEO

Josh, if you look back on what I said that we were increasing our loss ratio by $0.19 and that was 5 points of loss ratio and a combined ratio that would put us in a combined ratio below a 100%. And I told you we are stop-loss attaches, so actually you did get lucky, I answered your question.

Joshua David Shanker
Deutsche Bank AG, Research Division

And where are loss cost and access casualty right now, are they benign at this point?

Evan G. Greenberg
Chairman, President & CEO

Lost cost, it's never benign, access casualty is never benign but loss cost are, I am sorry Sean brings that our Chief Actuary will finish that.

Sean Ringsted
Executive VP, Chief Risk Officer & Chief Digital Officer of Chubb Group

I think we have commented in prior quarters, we might to frequency and disparity. In the second quarter, we do the same and broadly frequency severity overall are inline with our expectations. There are implications or not, that they are not benign.

Joshua David Shanker
Deutsche Bank AG, Research Division

No real change from the previous quarters?

Sean Ringsted
Executive VP, Chief Risk Officer & Chief Digital Officer of Chubb Group

Correct.

Operator

We will take our next question from Meyer Shields from Stifel, Nicolaus.

Meyer Shields
Stifel, Nicolaus & Company, Incorporated, Research Division

And then in your commentary you noted that your pricing is better on the E&S side than on the retail side, is there a similar differential in loss-cost trend between E&S and retail?

Evan G. Greenberg
Chairman, President & CEO

That it's better on one side than the other side.

Meyer Shields
Stifel, Nicolaus & Company, Incorporated, Research Division

Are lost cost trends higher on the E&S side or is it just the market adjusting more rapidly?

Evan G. Greenberg
Chairman, President & CEO

Not particularly, no not when you measure more of a like for a like basis, but the portfolios are different. But if I, I am not evading your question, but what I am telling you is on level if I could put portfolios like for like they behave the same, but the portfolios by its nature what comes into E&S is tougher more difficult risk.

Operator

And our next question comes from Ian Gutterman from Adage Capital.

Ian Gutterman
Adage Capital Management, L.P.

I think following question, the quarter picked over it's a last year a bigger picture question. If this cycle is going to play a different, like you said it's not a hard market yet and we are going to sort of been I guess, what we call goldilocks [ph] which is you know slow increase in pricing greater than trend but we don’t get a true turn if you will. How does that effect the way you approach the market I mean, and the reason I am asking as I think of ACE is being a company who is sort of takes advantage of when there is chaos right and when there is disruption and there is big opportunities for you to underwrite people. If we have sort of more steady market that we never get that big hard turn, do you have to change the way you approach how you stick to grow the company overtime.

Evan G. Greenberg
Chairman, President & CEO

No. Ian let me ask you a question, if we looked at what do you think of this quarters, growth results?

Ian Gutterman
Adage Capital Management, L.P.

To determine it depends on…

Evan G. Greenberg
Chairman, President & CEO

ACEs, do you think they were pretty good?

Ian Gutterman
Adage Capital Management, L.P.

I want to see where those accident years end up, first one I will tell you. We are getting profitability and it's growing fast.

Evan G. Greenberg
Chairman, President & CEO

I am trying to answer your question, you just now are asking a different question. So I think what I am really trying to say to you is, in this environment I think we have taken pretty good advantage of market opportunity as we see it. We are not simply build for a hard market, we are built as an underwriting company to take advantage where we see an opportunity to make an underwriting profit and that’s different than saying you are a company that is just built to take advantage when you can make excessive underwriting profits to fill the holes of the industries bad behavior from the past which is typically what happens in an over correction in a very hard market. In this case, we are seeing more opportunity to earn an underwriting profit because of market pricing than we had seen, we have a very broad geography and product portfolio as you know and I think our revenue growth in the quarter reflects our capability to do that and I think therefore, that answers how we look going forward and why say do you know. There is not something to rebuild for a different playbook here.

Operator

We will take our final question from [indiscernible].

Unknown Analyst

One touch base on 2 things, first, with the LIBOR scandal for the European banks what’s the potential response or coverage implications for D&O and professional liability writers then I have a follow-up for Phil.

Evan G. Greenberg
Chairman, President & CEO

I am going to ask John Keogh to answer that question and if he is not fulsome enough then John Lupica will fill in. Go ahead.

John W. Keogh
Chairman

Sure, I will answer for ACE, I can't answer for the industry. Generally, we are an underwriter for large financial institutions, we don't take to surprise anybody. So here in the U.S. and internationally. I would say that most of our coverage in this space is in the D&O area, we have pulled away from E&O over the last few years and a very little D&O exposure currently. And then further I suspect D&O business we do a vast majority of our exposure to financial institutions in D&O is Side A only. Now to your question about LIBOR investigation which is underway, I mean I will be just speculating right now, the investigations are underway. The facts are yet to emerge, as those facts emerge they are going to be very specific to you know certain allegations and certain financial institutions, and what that means for that financial institutions in terms of liability what it means in terms of the actual coverage then they have with the insurance carriers, you that's all I get to play out.

Unknown Analyst

Something like Side A, typically it seems like that may not be designed to respond to civil litigation amounts related to something like that correct?

John W. Keogh
Chairman

So Side A is just for situations where the insurer is unable to or unallowed to indemnify the individual direct responses that are covered by policy. So the scenario you worry about their which is the remote one with this big financial institutions is that they are bankrupt and therefore it can't indemnify because they are financially unable. The more likely scenario to coverage will be derivative action against the financial institution which because the specifics of the derivative which is actually you know pursuing on behalf of the company, against these notes, those sorts of cases are not allowed to be indemnified. That would be the scenario that would be covered, more likely covered by D&O and then it's going to be a question of again the facts just cover apply or their exclusions where you sit, are your primary and therefore you are going to worry about defense cost, are you sitting excess, and remote from that. So it's something I would be very careful to generalize about that maybe company or the industry.

Unknown Analyst

Right, and then typically regulatory fines and penalties aren't covered under D&O, right?

John W. Keogh
Chairman

Typically not, but again you know on either of those policies again though that will be very fact specific to the actual policy for me so for particular financial institution.

Evan G. Greenberg
Chairman, President & CEO

John and we spent a lot of time in the U.K.

Unknown Analyst

Okay. and then for Phil, the effective tax rate continues to run sort below that 18% level that has been kind of modeled for a while. What do you think about for the back half, we are working out effective tax rate come in [ph].

Philip V. Bancroft
Executive VP & CFO

We are not giving guidance on that but I can tell you that it's going to be driven by where our PPD falls and what jurisdiction it falls in and cats as well.

Unknown Analyst

Right, so with the crop losses in the second half that have the effect of driving effective tax rate lower.

Philip V. Bancroft
Executive VP & CFO

I would think it would tend to drive it up a bit.

Operator

That concludes today’s question and answer session. Ms. Wilson at this time I will turn the conference back over to you for any additional or closing remarks

Helen Wilson

Thank you, everyone, for joining us this morning. We look forward to speaking with again at the end of next quarter. Thank you, and good day.

Operator
Ladies and gentlemen, that does conclude our conference call for today. We do appreciate your participation.