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Everest Re Group, Ltd. NYSE:RE

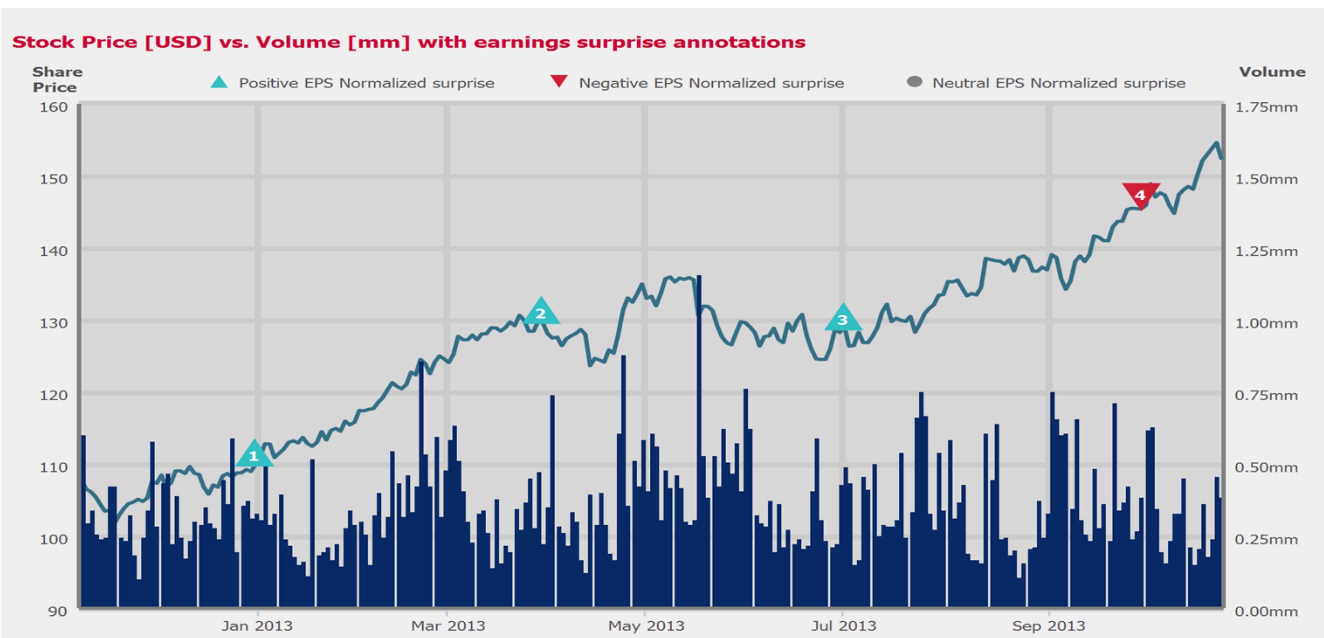
FQ4 2013 Earnings Call Transcripts

Thursday, February 06, 2014 3:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2013-			-FQ1 2014-	-FY 2013-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	4.98	6.28	▲26.10	4.77	20.22	21.47
Revenue (mm)	1234.53	1287.50	▲4.29	1241.50	4985.87	4753.54

Currency: USD
Consensus as of Feb-06-2014 6:00 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2012	0.27	0.80	▲1 196.30 %
FQ1 2013	4.39	5.88	▲2 33.94 %
FQ2 2013	4.21	5.10	▲3 21.14 %
FQ3 2013	4.59	4.20	▼4 (8.50 %)

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Presentation

Operator

Good day, everyone. Welcome to the Fourth Quarter 2013 Earnings Call of Everest Re Group Limited. Today's conference is being recorded. At this time, for opening remarks and introductions, I would like to turn the conference over to Beth Farrell, Vice President of Investor Relations. Please go ahead, ma'am.

Elizabeth B. Farrell
Vice President, Investor Relations

Good morning, and welcome to Everest Re Group's fourth quarter and full year 2013 earnings conference call. On the call with me today are Dom Addesso, the Company's President and Chief Executive Officer; John Doucette, our Chief Underwriting Officer; and Craig Howie, our Chief Financial Officer.

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

Now let me turn the call over to Dom.

Dominic James Addesso
President, CEO & Non-Independent Director

Thanks, Beth. Good morning, everyone, and thank you for joining us this morning. We're very pleased to report record earnings for the fourth quarter and the year. There were many elements of our portfolio that performed very well and others less so. However, with over $1.3 billion in earnings and a 20% ROE, it is a great result overall.

Certainly a factor was the absence of any major catastrophe, but it is worth noting that the year was not without losses. In fact, there were $195 million or $170 million net of CAT losses during the year.

Growth by diversification of 21% or $900 million growth in premium during 2013 enabled the company to absorb a reasonable level of loss events, while still expanding margins. New products and growth in many of our traditional lines have all contributed to margin expansion.

Growth in our core businesses was noted in treaty casualty, treaty property, facultative and specialty insurance line. In particular, our property strategy continues to be fluid, meaning that we allocate our capacity to those products offering the best return profile. This translates into more primary insurance and some additional pro rata in U.S. reinsurance segment.

As CAT XOL rates were trending down, we have been shifting to a different product mix. We're moving capacity to the better price layers. The ability to adapt and react quickly to changing market conditions remain the core competency of the Everest team.

The continued management of our portfolio mix resulted in a 4 point improvement in the combined ratio to 81%. All of this improvement came in the reinsurance portfolio. On the other hand, our insurance business underperformed relative to our expectations.

Crop losses and prior period development overshadowed many underlying improvements in this business. Excluding crop, the underlying accident year combined ratio improved to 94.6% in 2013. John and Craig will go into further details, but in summary, the crop losses were primarily due to a significant decline in the price of corn. Our estimate at the end of the third quarter did not sufficiently take into account yield factors, which were unknown at that time in our larger states.

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The loss development we continue to see was in lines of business that are some of the most difficult to assess, as can be observed generally in the industry. In fact, much of the development you saw emerged from business we had terminated several years ago. The good news was that our overall reserve position was redundant. And therefore, the specific development had no impact on overall earnings. We continue to feel confident about our overall reserve position, but recognize that any one of our numerous reserve buckets could prove inadequate, while at the same time many others will result in savings. That is the nature of the estimation process within our portfolio of reserves, a key to the overall adequacy.

Let me finish up with some commentary on the overall market. As many observers point out, there're many challenges that we face. Nothing new of course to those of us who have been around awhile. Today's headline topics are declining rates and capital markets invasion, but on top of that, a low investment yield environment, you have a recipe for lower overall returns to the industry. The key is of course not to get your company stuck in the averages.

Yes, U.S. CAT at the lower rates were down in 2013; and at 1/1, they were down in the 10% to 15% range. However, this view the market and how it applies to us is too binary or one-dimensional. These factors are just a slice of the market.

In other parts of the world, particularly in the loss affected areas, rates were up. And in many other regions, rates were flat. In addition, primary pricing is still holding and we access this business through our direct insurance platform, facultative operations and through pro rata deals in reinsurance portfolio. Other examples include new products.

As I mentioned previously, we have and will continue to deploy capacity to those areas and others, including new products that provide the best risk-adjusted returns. Yes, the capital market is a factor, but frankly, we see it as a tool, not a threat. John will speak to that when he discusses that facility, which for us is another form of capital that can be used to deliver well underwritten products.

Nevertheless, capital market is not a perfect fit for all risks and this is where company capital can be deployed to new products and risks not well suited to the capital market structure. The world is changing as it always has. It's how one adapts that determines if it can beat the average. Our business plan and strategy anticipate that we can continue to replicate similar returns to what you have seen over the last 2 years.

Thank you. And now Craig will cover the financial results, followed by John Doucette, our Chief Underwriting Officer, for the operations review. Craig?

Craig William Howie
Executive VP, Treasurer & CFO

Thank, Dom, and good morning, everyone. We're pleased to report that Everest had a record quarter of earnings, with net income up $365 million or $7.54 per diluted common share. This compares to net income of $59 million or $1.13 per share for the fourth quarter of 2012. Net income includes realized capital gains and losses. For the year, Everest had record net income of $1.3 billion or $25.44 per share compared to $829 million or $15.79 per share in 2012. The 2013 result represents a return on equity of 19.5%. Operating income for the year was $1.1 billion or $21.47 per share. This represents a 58% increase over operating income of $13.62 per share last year.

These results were driven by $480 million increase in underwriting income, representing a 185% increase year-over-year. As you will hear from John Doucette, there're a number of strategic initiatives that are driving these improved results. This increase in underwriting income was partially offset by higher income taxes and lower net investment income compared to 2012.

The results continue to reflect the improvement in the overall current year attritional combined ratio, which has declined a full 4 points from 85.0% to 81.0% for the year. This measure excludes the impact of catastrophe, reinstatement premiums and prior period loss development. The total reinsurance attritional combined ratio was 75.5% for the year compared to $80.9% in the prior year.

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The insurance segment attritional combined ratio was 101.4% for the year compared to 100.9% in the prior year. However, removing the crop results, which show a 94.6% attritional combined ratio for the insurance segment, compared to 97.2% in 2012, all segments reported increases in premium volume for the year and all reinsurance segments reported underwriting gains for the year.

Total reinsurance reported an underwriting gain of $390 million for the quarter compared to $48 million underwriting loss last year. For the year, total reinsurance reported an underwriting gain of $877 million compared to $327 million gain last year.

The insurance segment reported an underwriting loss of $156 million for the quarter compared to a loss of $46 million last year. For the year, the insurance segment reported an underwriting loss of $147 million compared to a loss of $68 million in 2012. The 2013 results reflected prior period reserve development and the crop loss for the year. John will discuss the crop insurance results in more detail.

Mt. Logan Re's financial position and operating results were consolidated into Everest beginning July 1, 2013. These results were included in a separate segment and reflected a $9 million underwriting gain for 2013. Everest retained $3 million of the income and $6 million was attributable to the non-controlling interest of this entity. The overall underwriting gain for the group was $238 million for the quarter compared to an underwriting loss of $94 million in the same period last year. For 2013, the underwriting gain was $739 million compared to a gain of $259 million in 2012.

These results reflect $30 million of current year catastrophe losses in the fourth quarter of 2013 related to Typhoon Fitow compared with $325 million of CATs in the fourth quarter of 2012 related to Sandy. For the year, catastrophe losses were $195 million in 2013 compared to $410 million in 2012. Our reported combined ratio was 84.5% for the year 2013 compared to 93.8% in 2012.

On reserves, we completed our annual loss reserve studies. The results of the studies indicated that overall reserves remained adequate. In the fourth quarter, we booked the prior year development in the insurance segment, which was more than offset by favorable development in the reinsurance segment. The $125 million of prior year reserve development in the insurance segment is largely related to workers' compensation, construction liability and umbrella business. The construction liability and umbrella were programs the company discontinued several years ago.

The $142 million of favorable prior-year development in the reinsurance segments mostly related to treaty casualty and treaty property business both in the United States and internationally. These redundancies have developed over time, but we don't react until the position becomes more mature. We continue to hold our estimates for the more recent years.

For investments pre-tax investment income was $126 million for the quarter and $549 million for the year on our $16.6 billion investment portfolio. Both the quarter and the year investment income amounts were below last year, as anticipated. This result was primarily driven by the low interest rate environment, the decline in limited partnership income and the amount of cash flow used for share buybacks and the redemption of debt. However, for our investment strategy to diversify into high yield bonds and dividend paying stocks enabled us to exceed our planned investment income for the year.

The increased allocation to equities was also a benefit to net income, as the year reflected $197 million of net after-tax realized capital gains compared to $140 million last year. These gains are mainly attributable to fair value adjustments on the equity portfolio. On income taxes, the effective tax rate is primarily driven by lower than planned catastrophe losses in the year, resulting in higher than expected taxable income for the year. For 2013, operating income effective tax rate was 14.9%. This 14.9% effective tax rate for the year is in line with our expectations and yield with much lower than planned CAT losses, as mentioned last quarter.

Total cash flow continues with operating cash flows of $1.1 billion for the year compared to $695 million in 2012. This is primarily due to our premium growth and lower catastrophe loss payment.

As you previously heard, Mt. Logan Re successfully completed its initial capital raise and now has over $360 million of assets under management. This serves to validate Mt. Logan's business model, as investors recognize the value proposition of partnering up with a leading global reinsurer.

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Shareholders' equity for the group was $7 billion at the end of 2013, up 3.5% compared to $6.7 billion balance at year-end 2012. This is after taking into account capital return for $622 million of share buybacks and $107 million of dividends paid in 2013. The company announced a 56% increase in its regular quarterly dividend and paid $0.75 per share in the fourth quarter.

Additionally, we repurchased another $28 million of stock after the year-end close. These purchases will be reflected in the first quarter 2014 financial statements. Book value per share increased 12% to $146.57 from $130.96 at year-end 2012. Our strong capital position leaves us with capacity to maximize our potential business opportunities as well as continued share repurchases.

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

John Paul Doucette
Executive VP, President of the Reinsurance Division & CEO of the Reinsurance Division

Thank you, Craig, and good morning. As Dom highlighted, we had a solid Q4, finishing a successful year. Our group 2013 gross written premium was $5.2 billion, up $908 million from 2012, with growth coming from all segments of the reinsurance and insurance.

For our reinsurance segments, total reinsurance gross written premium was up 21% in 2013, with new opportunities globally, and all reinsurance segments had increasing gross written premium led by our U.S. reinsurance segment up 38%. We benefited both from a continued fight to quality and Everest being one of the leading U.S. domestic property reinsurers. With over 50% of the global property CAT premium emanating from the U.S., this is an important sustainable competitive advantage for Everest. We write U.S. CAT business from the U.S. with the ability to seamlessly provide capacity in any form, excess or loss, pro rata, pro risk, all underwritten by the same underwriting team.

We grew topline on several attractively priced treaties with clients seeking capacity exclusively from domestic traditional reinsurers. In particular, we wrote several large multi-line treaties with U.S. regional companies, a targeted market for us. Total reinsurance bottom line had a $549 million improvement in underwriting profits for the year to $877 million, benefiting from the successful rollout of new product initiatives such as Purple, Everest's pillared product; increased capacity to property pro rata deals where we saw improvement in original pricing, terms and conditions; and new credit related opportunities in multiple places.

Globally, we saw the benefit of Mt. Logan Re in 2013, as we chose to deploy larger lines on deals we like and increased our CAT capacity for key clients. Logan allowed us to manage our net P&L, while growing our topline and having additional flexible capital management such as Logan gives us more flexibility to manage our P&L before wind season. As Dom said, we view capital markets more as a tool than a true competitor.

In several cases, providing clients with more property capacity resulted in securing better signings on deals we wanted in other classes. As a leading, global multi-class reinsurer, we have the ability and expertise to underwrite all lines of P&C business. This is important to note as less than 25% of our overall business is property catastrophe related.

We wrote several new prop reinsurance and weather deals globally and these performed well in 2013. We continue to develop capabilities here and view weather and agriculture as long-term strategic core competencies.

In 2013, we also wrote some large quoted shares both internationally and in the U.S. across various lines. These were strategic transactions with some large global clients. The premium on these deals has not yet been fully reflected in earnings.

We continue to execute on several large one-off transactions from new and existing clients, which require significant reinsurance structuring capabilities, the ability to combine underwriting skill sets across multiple lines of business, manuscript policy warding expertise, and global capabilities with multiple jurisdictional expertise and paper. We can bring all of this to bear and our ability to execute nimbly and in size with a highly rated balance sheet has been a key differentiator in this competitive market.

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Globally, we deployed more FAC capacity, increasing shares on well rated program and enhancing our product offering to our FAC and treaty clients. To summarize, we are a leading global multi-line reinsurer and we have the culture and organizational structure to react quickly to changing market dynamics and identify strategic opportunities that can enhance the long-term franchise of the group.

Now turning to insurance operation, our premium grew by $195 million in 2013, primarily driven by crop, workers' comp, non-standard auto, property E&S and casualty. However, insurance calendar year results underperformed, as Craig indicated, driven by prior year loss development and a difficult U.S. crop season. The result was an underwriting loss of $147 million. Our crop insurance had an underwriting loss of $57 million in Q4, resulting in an underwriting loss of $68 million in 2013. This was driven by a fall in commodity prices, particularly corn, as well as final crop yields that were lower than we originally expected and even what we expected a quarter ago. We saw crop yields fall below average in some areas, where we have a large footprint such as Southern Minnesota due to excess moisture, and in Texas due to abnormally dry conditions in the areas we write in.

We anticipate improved underwriting results in our crop book in 2014 as we continue to build out a more diversified geographic footprint, increased operating efficiencies and roll out new systems. As I stated earlier, ag and weather are long-term strategic focuses for us and the crop business we write through this platform complements that well.

We have a great team at Heartland. We believe that under more normalized circumstances, our crop insurance book will achieve profitable growth along with our ag and weather reinsurance products.
Our California workers' comp book saw a 13% rate increases in 2013, continuing the double-digit rate increases for the last several years, providing a compound rate change of over 60% since 2009. Workers' comp writings increased $50 million, mostly from rate increases.

Our current accident year workers' comp combined ratio is in the mid-90s. Our non-standard auto book grew nicely, given broader geographic mix and economies of scale. And our property E&S book continued to see rate increases, growing over $30 million in 2013 with additional geographic diversification.

Our financial institution book remains profitable, but growth was flat as we remain cautious in light of increased competition. Our casualty and environmental facilities achieved rate increases throughout 2013 and we grew these books.

Other recent insurance initiatives, including our primary A&H, Canadian insurance and contingency business, all continued to enhance their capabilities with new hires, new products and new distribution channels and are poised for profitable growth in 2014 and beyond.

Finally, some color on January 1st reinsurance renewals, which represents approximately 45% of our annual reinsurance premiums. Some key themes we saw at 1/1. First, it has become a stratified reinsurance market of haves and have-nots. Everest is solidly in haves and we have found new business opportunities, had strong signings on existing treaties and in some cases differential pricing.

Second, there has been a globalization and consolidation of treaties by several global insurers seeking to both narrow their reinsurance panel to improve security, but also diversify their credit exposure with a broader panel of high-quality reinsurers. This has generally been positive for companies such as Everest with strong ratings and high quality balance sheet.

Third, we are successfully competing with and winning against non-traditional capacity everywhere. In many instances, Everest won placements despite offering higher prices due to our ratings and diversified 40-year-plus franchise, the breadth of our trading relationships with clients globally and our ability to tailor solutions to meet clients' needs and to design products that benefit from structural advantages we have over competitors, which have all proven to be significant competitive advantages.

Furthermore, unlike the non-traditional markets, Everest's promise to pay does not expire, nor do we force a collateral release mechanism into products earlier than the natural expiry of the liabilities being reinsured. Specifically, on 1/1 renewals, casualty was challenging, especially pro rata, due to demand for expanded terms and conditions. As a result, we did withdraw from some contracts and deployed

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capacity at higher layers on others. On the other hand, despite headlines on property conditions, we had a successful renewal of our property portfolio globally.

Net written premiums for property grew by $150 million this January 1. Over all territories and all products, our property book combined ratio increased by a couple of points at 1/1, but we still saw margin expansion across the whole book at this renewal, as we continue to grow at what we consider to still be attractive returns. Across all classes, we grew gross reinsurance premium by $300 million or 18% on our 1/1 reinsurance renewal book. And our net reinsurance premium grew by 6%. We accomplished this growth by expanding shares with existing clients on desirable treaty layers, plugging new call to shares at attractive terms and conditions and increasing our marketing of new product and deploying capacity to them.

For example, our Purple premium was up significantly at 1/1/2014, as our long-term clients clearly preferred to buy this product from Everest's highly rated traditional balance sheet. The ability to flexibly move between products has been critical to our 1/1 success. We trade with our clients in many different products in every P&C line of business around the world. We are not beholding to excess of loss or pro rata, nor to reinsurance, retro or insurance. And we will dynamically reallocate capacity to where the best risk-adjusted returns exist. We are not restricted to any product class, premium size or minimum rate on line. And we continue to roll out many new insurance and reinsurance products in 2014.

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

Elizabeth B. Farrell
Vice President, Investor Relations
We are open to questions now.

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Question and Answer

Operator

[Operator Instructions] We will move to our first question from Michael Nannizzi from Goldman Sachs.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

The reserve development in your insurance segment, I was just wondering if we could talk about what book specifically, what year is that related to and could you tell us in the case of the affected books what's the total case in IBNR that you're currently holding?

Dominic James Addesso
President, CEO & Non-Independent Director

Michael, the first part of your question kind of cut out could you just again restate it.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

So I was just saying the reserve development in your insurance segment, I was just wondering, you mentioned work comp construction umbrella, so could you give us some color on what accident year that is related to, and from a magnitude perspective what is the total case in IBNR that you are currently holding after development for those books?

Dominic James Addesso
President, CEO & Non-Independent Director

In the insurance segment, we had about approximately $45 million of developing in work comp, a little over $40 million in construction liability and $17 million in umbrella. The construction liability and the umbrella, those are programs that we discontinued several years ago. So that should not be something that we see in our future results. In the workers' comp, part of the development related back to some earlier years, the early part of 2000 time period when we first got into the program, and it's just a matter of some severity in a handful of claims that we saw from the early part of decade. We also did see some increase of frequency of some smaller claims in the later years, primarily in '09, '10, and '11, I believe. And in that particular case, what we've seen is that increased frequency has been contemplated in the more recent accident years. So our more recent accident years do reflect that increased frequency. And I might point out those most recent accident years are profitable.

John Paul Doucette
Executive VP, President of the Reinsurance Division & CEO of the Reinsurance Division

Mike, I just wanted to add that the majority of the workers' compensation adverse development came from years before our rate increases started to kick in 4 years ago. We've been getting double-digit rate increases since then as well.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Has that been related to case reserves or do you still hold IBNR for those older years?

Dominic James Addesso
President, CEO & Non-Independent Director

We still hold IBNR for those, yes. I don't know that we have our disposal right this minute because its split between case and IBNR.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

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You mentioned, Dom, recent years. I'm just curious, because we've heard some commentary about recent professional liability years. Have you seen any adverse development either in recent comp or recent professional liability years just to be clear?

Dominic James Addesso
President, CEO & Non-Independent Director

No, we have not seen any development in recent years for professional liability in particular. As I mentioned, the comp where we saw the development on the insurance side, was really in the more recent years '09, '10 and '11.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

On the renewal comments from John, you seem pretty optimistic about opportunities property CAT I'm just curious, how are you thinking about opportunities heading into mid-year renewals? I mean do you think that your structure, your market position or some other differentiator is allowing you to achieve terms in pricing that are materially better than the market?

John Paul Doucette
Executive VP, President of the Reinsurance Division & CEO of the Reinsurance Division

Michael, as we talked about, I think each of us talked about it in a different way on our drafted response, we do believe that we have given our balance sheet, given our market position, given how we access U.S. catastrophe business and the ability to dynamically move between different structures around the globe that we do have an opportunity to get better than market results. As you may recall, we increased our quota share writings in June and July and we also increased quota share writings at 1/1 as well as repositioning the book to better lines that we write at more attractive prices.

Dominic James Addesso
President, CEO & Non-Independent Director

Mike, let me add to that. In many cases, we're not necessarily going to get different terms and conditions and market pricing, but there are unique circumstances where certain clients we have longstanding relationships returns that we do get may be different than the market. So I wouldn't say that it's universally in every particular offering that we get terms different than the market. But as John is pointing out, with those terms come to us and it doesn't hit our pricing targets, then we begin to allocate our capacity into other places, whether that be pro rata, facultative or into the primary space. So even if terms and conditions are at the market, we still have the ability to not take those terms and conditions and we can move our capacity into different lines or segments.

Operator

We'll move next to Amit Kumar with Macquarie Capital.

Amit Kumar
Macquarie Research

I guess 2 quick follow-ups to the previous question. You had mentioned that some of that piece was from some of the run-off lines. Can you expand on that piece, or is that also related to the comp piece?

Dominic James Addesso
President, CEO & Non-Independent Director

It is not related to the comp piece. These are separate programs. As I mentioned, part of it was construction liability, in particularly one program where it's a landscaper's program and because of the additionally insured endorsement that we had on many of those policies, what we're seeing is an increase in expense, even though you wouldn't normally expect landscapers to be brought into a construction liability claim. But because of the additionally insured endorsement, they are being drug into those matters and it is mostly an expense or defense issue. The umbrella program again is one that we

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cancelled a while ago. And again, that umbrella, as you probably know, is a very volatile class of business and we've got hit this year with several large claims, which caused us to increase our estimates in some of the older years.

Amit Kumar
Macquarie Research

What should give us comfort that this might be hopefully this is the last time that this noise sort of resurfaces? What will you say to that?

Dominic James Addesso
President, CEO & Non-Independent Director

Well, I guess, Amit, I would say that it's not going to be noise at all. We have $10 billion of reserves. We actually reported an overall reserve redundancy coming through the numbers. And because I've mentioned on previous calls, we manage some 200 different reserve buckets. And there are pluses and minuses in all of those buckets each and every year. These estimates in these particular lines are well within the actuarial ranges. It's not anything unusual to those of us that have been around the reserving process for a long, long time that I've been. But I think we're proud to point out that our overall reserve position as a group is positive and our accident year development, if you go back in time for the entity, has been a pretty stellar record relative to how each accident year has ultimately developed at the group level. But here again, you're managing a portfolio and you have individual buckets or lines of business that sometimes develop poorly. And on the other hand, offsetting that would be lines of business that develop redundantly. That is the nature of the beast.

Amit Kumar
Macquarie Research

The discussion on the increasing CAT premiums growth on 18% and net 6%, do you have corresponding P&L numbers, which might have been updated post-renewals?

Dominic James Addesso
President, CEO & Non-Independent Director

Well, we could get into that detail later. Renewals are up about consistently with those premium increases we cited. It's in different regions. It doesn't mean that will end the year, as John pointed out in his opening comments. We have the ability to go into the market before wind season and change that if we so desire. But right now, given our capital position, we're quite comfortable with where our P&Ls are at. And as you probably have noted, through the years that what we carry is our net P&L for 1 in a 100, 1 in 250 are pretty conservative relative to the industry.

Operator

We'll move next to Josh Shanker with Deutsche Bank.

Joshua David Shanker
Deutsche Bank AG, Research Division

Going back a little bit on the reserving issue, I just wanted to understand the process that you go through. Is there an annual reserve review that comes in the fourth quarter and this is sort of how it came to be? What's the process right now at Everest Re?

Dominic James Addesso
President, CEO & Non-Independent Director

We review reserves throughout the year. Starting at the beginning of the year, though, the reserve buckets that we review tend to be the less material buckets. And then as we get into the fourth quarter, we're evaluating our largest lines of business or largest classes of business beginning for most recent data, meaning as of September timeframe. In other words, all the claims data up through September, is accumulated in order to do our year-end reserve review. And that's the process since I've been here in

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2009. And if there is anything, for example, during the year that comes up with some of those smaller classes of businesses, we would certainly book that into our numbers. But generally, given the size of it, it's generally not an issue. And then of course, the larger, more material lines, as I mentioned, we wait until the fourth quarter to accumulate all those studies. Is that what you're asking about?

Joshua David Shanker
Deutsche Bank AG, Research Division

The charges that you took, are they more prone to changing hues on a frequency or severity?

Dominic James Addesso
President, CEO & Non-Independent Director

As I mentioned, we saw both, but not out of the accident periods. The more recent years, '09 and '10 and '11 was predominantly due to frequency of smaller claims. It's hard to tell maybe due to economic conditions, but nevertheless what we have done is we've factored in that increased frequency into our most recent accident year pick. So that influences the entire booking of all of our results. The severity that we encountered was due to business that has since been discontinued. So there really wasn't any need to make any dramatic adjustment for severity relative to our current book.

Joshua David Shanker
Deutsche Bank AG, Research Division

And finally, in speaking about the price kind of reinsurance, going forward, do you see an opportunity for Everest to buy more XOL coverage in mid-year or even thinking about a long-term reinsurance protection plan for the company?

Dominic James Addesso
President, CEO & Non-Independent Director

There is always that opportunity, as I mentioned in the answer to the previous question, John even made some reference to it, now that 1/1 is over, we have the opportunity between now and wind season to look at various structures. And we did put a structure in place last year. Or actually it was renewal last year.

John Paul Doucette
Executive VP, President of the Reinsurance Division & CEO of the Reinsurance Division

Josh, this is John, we also – part of the reason that we decided to star Mt. Logan Re, and very excited about that it gives us a lot more flexibility in terms of how we position our footprint and how we manage our capital on CAT P&Ls, and with Mt. Logan Re and other capital market initiatives a lot of the traditional reinsurance or otherwise, we think we slow the overall book very profitably and keep the P&Ls to a level that we are comfortable with, and it will be accretive to every shareholder.

Operator

We'll take our next question from Vinay Misquith with Evercore.

Vinay Gerard Misquith
Evercore ISI Institutional Equities, Research Division

The first question is on the adverse development on the construction liability and umbrella. Curious as to what the liabilities are. So [indiscernible] programs discontinued. So when can we see the end of these claims?

Dominic James Addesso
President, CEO & Non-Independent Director

Well, on the construction liability, I believe that the 7-year period after which the policy was issued, I don't recollect the exact date, but it was the 2008 was the last policy that was issued. I think the claims can be made in a period of 7 years after that date. We feel, obviously our reserve addition was sufficient to answer your question about seeing the end of it. But as you know, again, reserves can always move

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around. But again, in the context of our overall reserve posture, we don't believe it's going to be a problem. Umbrella on the other hand, it doesn't have a fixed discovery period, if you will. So umbrella claims can come in for a long time, again a volatile class, but we feel as if what we book is reasonably conservative. And again in the context of our overall reserve position, we don't feel that either one of these classes or lines of business will present a problem for our future financial performance.

Vinay Gerard Misquith
Evercore ISI Institutional Equities, Research Division

And when was the umbrella program discontinued?

Dominic James Addesso
President, CEO & Non-Independent Director

4 years ago.

Vinay Gerard Misquith
Evercore ISI Institutional Equities, Research Division

And then moving on to crop, you said $68 million of losses. I believe crop premiums was about $300 million-ish last year?

Dominic James Addesso
President, CEO & Non-Independent Director

Yes. Gross, yes.

Vinay Gerard Misquith
Evercore ISI Institutional Equities, Research Division

So just looking at the combined ratio, that seems to be about 122% combined ratio. Just curious why it would be that high on the crop?

Dominic James Addesso
President, CEO & Non-Independent Director

Well, our technical ratio was about 112% and then the rest of it's just expenses. And we're a little higher than the industry, at least what's been reported to date, just because of some of the concentration we have in particular as John mentioned in Minnesota and Texas, being some of our largest states, which in fact relative to the industry held us in better stead last year. Minnesota, for example, has a long history of being very, very profitable state.

Vinay Gerard Misquith
Evercore ISI Institutional Equities, Research Division

And for '14, what's the targeted combined ratio for the primary insurance operations, because I believe that on the workers' comp, you said it's mid-90s, on the rest of the book [indiscernible] 94.6. So looking at '14, what's your targeted combined ratio for the primary business?

Dominic James Addesso
President, CEO & Non-Independent Director

We believe that the numbers in the low to mid-90s would still be achievable and perhaps better. But for now, I'll leave it at that.

Vinay Gerard Misquith
Evercore ISI Institutional Equities, Research Division

I think you're changing your business mix, just a tad moving to write more pro rata versus excessive loss business. Should we see an uptick in the accident year a loss ratio x CATs because of that business mix shift?

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Dominic James Addesso
President, CEO & Non-Independent Director

Not necessarily. There might be an uptick in certain lines of business due to rate movements, but also as we move the portfolio into other lines of business, particularly new products, that's actually having the impact of lowering our attritional combined ratio. So I'm not going to give you a number at this point, because we don't give guidance. To be honest with you it depends on what the final nix at the end of the year comes in at, but we're not anticipating an increase in that number. I'll leave it at that.

Operator

We'll move next to Greg Locraft with Morgan Stanley.

Gregory Locraft
Morgan Stanley, Research Division

I'm just looking at the profitability out of the insurance segment, and it hasn't been profitable on an underwriting side for many years. I certainly understand the reasons why this particular year, but how do we think about net investment income allocation of this segment? Is it just kind of pro rata with the premiums or is there more investment income being earned out of this book of business?

Dominic James Addesso
President, CEO & Non-Independent Director

We don't really do a specific allocation if we could talk about it in this call, but I would think about more in the context of a premium allocation.

Gregory Locraft
Morgan Stanley, Research Division

For those of us that are looking, they're not making any money in underwriting, the reality is you're making, call it, $100 million-plus probably in investment income as well, if you would actually break it?

Dominic James Addesso
President, CEO & Non-Independent Director

But our focus, quite, Greg, is on the underwriting account. That's where our attention is. And we don't rely on the investment income, because at today's yield, that's not really giving you the appropriate return. And as I mentioned, our current year attritionals are very good positioned. And given the rate increases, we'll continue to get in California comp, what we're doing in the property in that space, our other strategic initiatives, reinsurance platform, we're quite bullish on it. So the profitability issues that you're seeing are things that relate to frankly a lot of which was discontinued 4, 5 years ago.

Gregory Locraft
Morgan Stanley, Research Division

In crop as well, yes.

Dominic James Addesso
President, CEO & Non-Independent Director

The crop in particular, remember, when you look at that, not unlike we look at our reinsurance catastrophe business, right. And also, even though it's reported within the insurance segment, we have capabilities now globally, as John somewhat mentioned in his comments, we look at weather and crop in other jurisdictions kind of jointly, we have capabilities that we can look across the organization on how we're doing in crop [indiscernible] even though they're reported in 2 different segments.

Gregory Locraft
Morgan Stanley, Research Division

And then turning to capital management, on the one hand, you bought back 9% of the shares outstanding at the beginning of the year, so it was a robust buyback in a strong year. On the other hand, there's only

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68% of capital returns via buybacks in dividends on a year. So in a way, you held back. Looks like you haven't done much in the month of January. You've done a little bit, but I'm sort of wondering, stock is below book value. What's keeping you from doing more on the buyback front?

Dominic James Addesso
President, CEO & Non-Independent Director

We were in January as long as we could be in the month of January. Of course, as you know, at some point, during a month, we begin to know the numbers and we were basically restricted from being in the market. So that's really the only thing that held us back in the month of January. In the fourth quarter, we were buying stock even at above book value. But we couldn't get all of the stock that we wanted at the prices that we wanted it at. So we continue to be bullish on share repurchase, balance that up against what the market opportunities are. As we pointed, we've had a strong 1/1 and we'll consider that and the upcoming 4/1 as we evaluate and the price of the stock as we evaluate what our share repurchases will be in this quarter and the upcoming quarters.

But I think it's fair to say that we're still very interested in share repurchases.

Operator

And we'll take our final question from Meyer Shields with KBW.

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

Is there any way of ballparking, given the growth that we had in 1/1, how much more capital do you think you need this year compared to last year?

Dominic James Addesso
President, CEO & Non-Independent Director

Well, I guess if you wanted a ballpark that you could relate to P&Ls is in the premium growth.

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

Was there any adjustment to the accident year '13 loss cost for workers' compensation in the quarter, given the adverse development on recent years?

Dominic James Addesso
President, CEO & Non-Independent Director

No, there was none.

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

Are you confident with the level of pricing that you've been implementing over the last 6 months?

Dominic James Addesso
President, CEO & Non-Independent Director

Well, our reserve numbers that we picked in most recent accident year is what I call bridged off of the previous accident years. So it's taking into account the experience of those years, plus we layer on top of that rate increases that we've had, and as John pointed out, over 60% cumulative rate increase since 2009, and then subtraction from that would be assumed loss cost trends. So our most recent accident years are a reflection of the development we've seen, plus pricing.

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

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Right. But I guess the question is that you've known the pricing for a while, but the base on which the premise is applied seems like it would be higher.

Dominic James Addesso
President, CEO & Non-Independent Director

I'm not sure I understand that question.

Craig William Howie
Executive VP, Treasurer & CFO

I think what's happened here as well, this is Craig, is that you're essentially picking a conservative number to begin with. And we have not let that number come down just because of the pricing.

Operator

And I'll now turn the call back to presenters for any additional or closing remarks.

Dominic James Addesso
President, CEO & Non-Independent Director

Thank you all for participating on the call. As you've heard, we're quite bullish on our opportunities and trajectory going into 2014. We think we have the capital to take advantage of market conditions, while at the same time continuing our interest in share repurchases.

So again, thank you for your interest.

Operator
That does conclude today's conference. Thank you for your participation.

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