S&P Global
Market Intelligence

AXIS Capital Holdings Limited NYSE:AXS

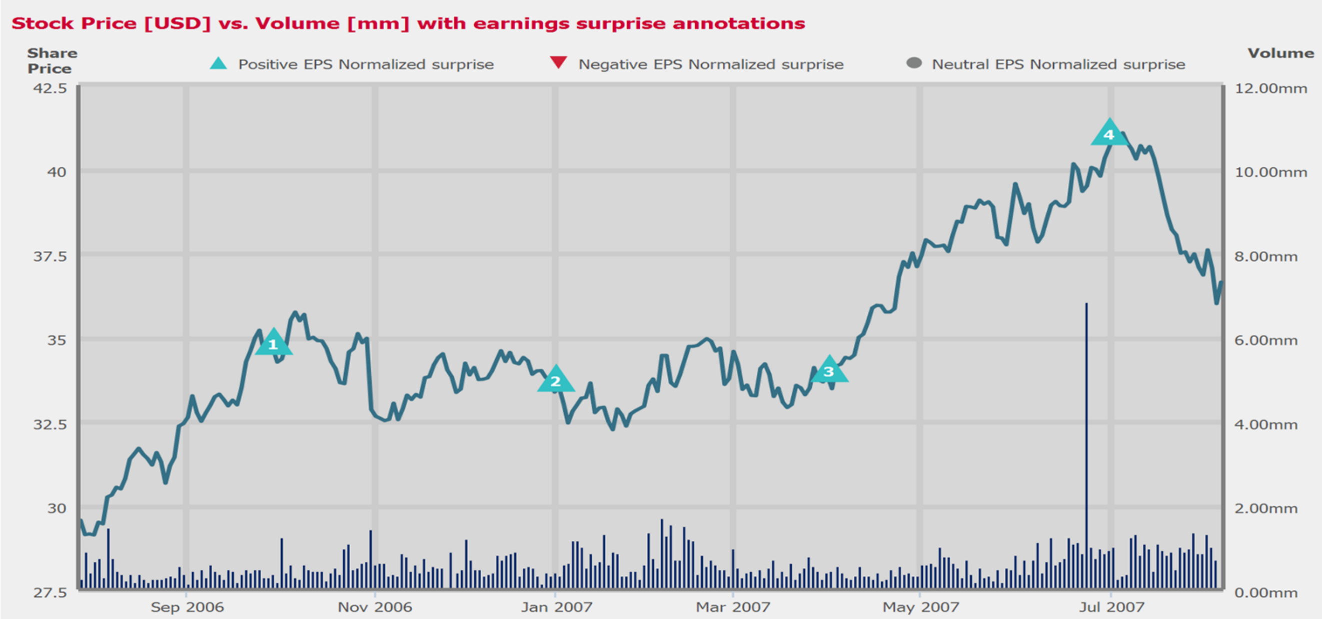
FQ3 2007 Earnings Call Transcripts

Tuesday, October 30, 2007 12:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2007-			-FQ4 2007-	-FY 2007-	-FY 2008-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.38	1.66	▲20.29	1.44	5.80	5.52
Revenue	-	-	▲(2.59 %)	-	-	-
Revenue (mm)	599.43	583.90	-	548.17	3049.54	3086.64

Currency: USD
Consensus as of Oct-30-2007 6:40 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ3 2006	1.31	1.37	▲1 4.58 %
FQ4 2006	1.36	1.67	▲2 21.90 %
FQ1 2007	1.18	1.37	▲3 16.10 %
FQ2 2007	1.46	1.54	▲4 5.48 %

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Call Participants

EXECUTIVES

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

John R. Charman
Chairman & CEO

Linda Ventresca

ANALYSTS

Bill Wilt
Morgan Stanley

Jay Cohen
Merrill Lynch

Matt Heimermann
JP Morgan

Ron Bobman
Capital Returns

Susan Spivak
Wachovia

Vinay Misquith
Credit Suisse

Presentation

Operator

Welcome to the third quarter 2007 AXIS Capital Holdings Limited earnings conference call. (Operator Instructions) I would now like to turn the presentation over to your host for today's call, Ms. Linda Ventresca. You may proceed, ma'am.

Linda Ventresca

Thank you, Jeremy.

Good morning, ladies and gentlemen. I am happy to welcome you to our conference call to discuss the financial results for AXIS Capital for the quarter ended September 30, 2007.

Our third quarter earnings press release and financial supplement were issued yesterday evening after the market closed. If you would like copies, please visit the investor information section of our website, www.axiscapital.com.

We set aside an hour for today's call, which is also available as an audio webcast through the investor information section of our website through Friday November 23, 2007. An audio replay will also be available through Friday November 9, 2007. The toll-free dial-in number for the replay is 888-286-8010 and the international number is 617-801-6888. The pass code for both replay dial-in numbers is 19500687.

With me on today's call are Michael Butt, our Chairman; John Charman, our CEO and President; and David Greenfield, our CFO.

Before I turn the call over to John, I will remind everyone that statements made during this call, including the question-and-answer session, which are not historical facts, may be forward-looking statements within the meaning of the U.S. federal securities laws. Forward-looking statements contained in this presentation include, but are not necessarily limited to, information regarding our estimate of losses related to catastrophes and other loss events; future growth prospects and financial results; evaluation of losses and loss reserves; investment strategies; investment portfolio and market performance; impact to the marketplace with respect to changes in pricing models; and our expectations regarding pricing and other market conditions. These statements involve risks, uncertainties and assumptions which could cause actual results to differ materially from our expectations.

For a discussion of these matters, please refer to the risk factors section in our most recent Form 10-K on file with the Securities and Exchange Commission. We undertake no obligation to update or revise publicly any forward-looking statements whether as a result of new information, future events or otherwise.

In addition, this presentation contains information regarding diluted book value per common share, calculated using the if-converted method and operating income, which are non-GAAP financial measures within the meaning of the U.S. federal securities laws. For a reconciliation of these items to the most directly comparable GAAP financial measures, please refer to our press release and Form 8-K issued last night, which can be found on our website.

With that, I would like to turn the call over to John.

John R. Charman
Chairman & CEO

Thank you, Linda and good morning to you all. We are extremely pleased to report our results for the third quarter of 2007. Our quality underwriting portfolio, good investment earnings and overall favorable loss experience delivered record results for the quarter and for the year-to-date. For the first nine months of this year, we achieved $749 million in net income, yielding an annualized return on average common equity of 23.9%. Our diluted book value per share has increased 15% from the start of this year and 22% for the rolling 12 months.

In the quarter, our overall gross premiums written were stable relative to last year end; and for the year-to-date, gross premiums written was up modestly to $3 billion with many continuing important underwriting portfolio changes underlying these overall top line results. Our underwriting results were strong and healthy with a combined ratio for the quarter of 74.1% and a combined ratio for the year-to-date of 76.7%.

Mindful of the robustness of our pre-binding price monitoring embedded in our underwriting peer review process, I am pleased to report that our current year loss ratios continued to represent our solid underwriting performance. Our underwriting results also contributed meaningfully to earnings with pre-tax net investment income up 20% from the same quarter last year and up 26% for the first nine months.

With that, I will turn the call over to David to discuss our financial results for the quarter in more detail.

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

Thank you, John. Good morning, everyone. As John mentioned, we are extremely pleased with our results for this quarter. Our third quarter results marked another quarter of record earnings against a comparable prior year period, our eighth quarter in a row. This once again demonstrates the powerful earnings potential of the global AXIS franchise.

For the quarter, net income was $270 million, a 19% increase over the $226 million in the third quarter of 2006. Earnings per diluted share for the quarter of $1.65 compared to $1.37 per diluted share in the third quarter of 2006. After-tax operating income, which excludes the impact of realized gains and losses on investments, was $271 million, a 19% increase from the $228 million for the third quarter of 2006. Operating earnings per diluted share of $1.66 in the quarter compared to $1.38 in the same quarter last year.

For the first nine months of 2007, net income reached $749 million, a 16% increase over the $645 million for the first nine months of 2006. Earnings per diluted share of $4.53 for the first nine months of 2007 compared to $3.94 per diluted share in the first nine months of 2006. After-tax operating income was $754 million, a 13% increase from the $666 million for the first nine months of last year; and operating earnings per diluted share of $4.55 for the first nine months compared to $4.07 in the first nine months of last year.

These results translate to an impressive annualized return on average common equity for the quarter of 25% and 23.9% for the first nine months of 2007. Our diluted book value per share increased 22% over the last 12 months and 15% for the year-to-date.

Turning to our top line, our consolidated gross premiums
written was $755 million for the quarter and compares with $735 million in last year's third quarter. For year-to-date, consolidated gross premiums written of $3 billion were up 4%, due primarily to increases in our reinsurance segment, which I will comment on in a moment.

Gross premiums written in our insurance segment were $481
million and compared with $453 million in last year's third quarter. This 6% increase in the segment's gross premiums were largely generated from our political risk line. Transaction timing worked in our favor this quarter and we also benefited from additional resources in this line to address the opportunities as they arose. As I've shared with you before, the unpredictable timing and lengthy analytical lead time associated with the political risk business impacts any comparative analysis amongst periods.

The other notable increase in the quarter was from our
professional lines book, which is benefiting from the diversification strategy we started three years ago. This strategy has shown to be prudent. The increase in the quarter was primarily associated with renewal rights acquired in connection with our Media/Pro acquisition this past May.

Other than U.S.
exposed catastrophe property business, which continued to present good opportunities, market conditions in our other lines of business continued to be less favorable during the third quarter of 2007. This limited our opportunity to expand these lines, although we continued to seek out better price and structured opportunities.

Gross premiums written in the insurance segment for the nine
months of 2007 were comparable with the same period in 2006.

Gross premiums written in our reinsurance segment were $274
million in the quarter, down 3% from $282 million in the third quarter of last year. This decline was driven by a reduction in catastrophe business where we allocated lower amounts of capital in the third quarter of 2007 relative to the same period in 2006. As discussed in prior quarters, we reallocated some catastrophe capacity from January 1
2006 renewals to take advantage of the much stronger mid-year 2006

pricing. The reduction in catastrophe premium in this quarter was partially offset by increased participation on certain professional lines and liability renewals.

For the first nine months of 2007, gross premiums written in the reinsurance segment increased 8% compared to the same period in 2006. This was largely a result of increased participation in the U.S. and European reinsurance markets during the major renewal period of the first quarter. The increase included approximately 3.6 percentage points related to the favorable impact of exchange rate movements.

Our professional lines business was the only reinsurance line for which we experienced a reduction in gross premiums written over the nine months. This was driven by the non-renewal of several large contracts during the second quarter due to cedents increasing their retention of business.

Consolidated net premiums written decreased 4% in the quarter. This was due to the reduction in reinsurance gross premiums written in the quarter, the purchase of additional reinsurance coverage on a number of business lines within our insurance segment and the change in the mix of business toward lines with reinsurance programs associated with them.

Year-to-date, net premiums written were up 3% driven by the increase in reinsurance gross premiums written. In line with our period-to-period changes in net premiums written and mix, consolidated net premiums earned were down approximately 1% in the quarter and up 3% for the first nine months of 2007.

Moving on to our underwriting results, our underwriting income for the quarter of $200 million, which includes $112 million from our insurance segment and $88 million from our reinsurance segment, is up 14% relative to the same quarter last year. Underwriting results this quarter benefited from both strong current-year underwriting results and continued favorable loss development from prior periods. The increase in underwriting income was driven by our insurance segment.

For the quarter, our consolidated combined ratio was 74.1%, an improvement of 3.6 points from the same period last year. This was primarily driven by our insurance segment where the combined ratio of 63.3% represented a 15.7 point improvement relative to the same period last year. The improvement was due to more favorable loss experience than initially expected and a higher level of favorable loss development from prior years.

Our reinsurance segment combined ratio increased 6.3 points over the prior year quarter to 77.1% due to a higher incidence of midsize catastrophe losses in the current year and a lower level of favorable prior period loss development in the quarter.

With respect to our current accident year loss ratio, this can vary from period to period depending on a number of factors that include the level of estimated losses, changes in our mix of business and changes in the benchmark assumptions used to establish our loss ratios. Of note, the current accident year loss ratio was favorably impacted in this quarter as compared to the same period last year by the increased weighting of our own favorable loss experience and development trends for catastrophe-exposed short-tail lines in both our insurance and reinsurance segment.

Our overall accident year loss ratio for the quarter of 59.9% compares with 61% in the same quarter last year and there were a few moving parts. Our insurance segment accident year loss ratio for the quarter was 56.9%, down 7.2 points from the same quarter last year. This brings our accident year loss ratio for the year-to-date in our insurance segment to 62.9%, down 2.6 points from the same period last year.

As I previously mentioned, reported claims on our short-tail lines of business in the insurance segment were favorable relative to our initial expectations and the reduction in the current year loss ratios in the quarter and for the year-to-date compared to the same periods in 2006 reflects this lower loss activity.

Our reinsurance segment accident year loss ratio was 62.1%, up 4 points for the quarter. This brings our year-to-date accident year loss ratio in the reinsurance segment to 65.2% from 62.1% in the same period last year. The increase for the quarter and year-to-date was primarily due to the increased mid-sized catastrophe losses, which impacted a variety of property reinsurance lines. We also experienced changes in business mix with more longer-tail reinsurance lines in the mix, which generally have a higher initial expected loss ratio compared to our other lines.

Turning to prior period reserve development, our net favorable reserve prior period development in the quarter was $82 million, or 12 points. Of this amount, $59 million was from our insurance segment representing a positive impact of 19.4 points on the segment's loss ratio. Our reinsurance segment posted $23 million in favorable loss development representing a positive impact of 6.1 points on the segment's loss ratio. All of the favorable reserve development is related to short-tail lines.

As ever, we caution against comparing the level of reserve development amongst periods. However, I would like to remind you that we do continue to maintain the same discipline and conservative approach to quarterly reserving established at our inception.

Turning now to our investment portfolio, our total cash and investments increased to $10.3 billion at September 30 2007, up 2% for the quarter and 6% from year end.

Net cash generated from operations was exceptionally strong at $563 million for the quarter and $1.3 billion for the first nine months. These represent record levels of cash flow from operations for AXIS.

Our fixed income portfolio is of high quality with a weighted average rating of AA+ and 90% of those securities rated A or better.

The amount for which collateral comprises sub-prime or Alt-A mortgages is a negligible portion of our overall investment portfolio at $197 million or less than 2% of our portfolio. All of this is rated AAA. Our position remains unchanged relative to last quarter.

Our investment portfolio performed well overall in the quarter. Our net investment income for the quarter was $119 million, a 20% increase over the 2006 quarter. Our nine-month net investment income of $358 million was up 26% year-over-year. These increases were due to larger investment balances and higher yields on cash and fixed maturities. We remain optimistic that positive cash flow will continue to drive growth in investment income.

During the quarter, our net investment income from alternatives, or other investments, declined $1.6 million from the same period last year. There were a few underlying changes of note here. First, we had an increase in the fair value of our life settlements contract investment of about $20 million. Absent this increase, our net investment income from our alternative investments was down.

This was due to the broad repricing of risk in the capital markets and the lack of liquidity in the below investment grade credit market, which substantially and negatively impacted the performance in the quarter for our credit funds and to a lesser extent our hedge funds. We do expect that this repricing of risk, which presented some downside for the quarter, will present opportunities for us going forward. It is worth mentioning that since quarter-end, we have already recovered a substantial portion of the decline from credit funds.

With respect to hedge funds, we have now been invested in this asset class for almost three years and returns have been as expected. You will have noticed that we no longer hold the portfolio of life settlements contracts in our other investments. Following the extraordinary disruption in the financial markets in the middle of this year, we found the volatility in our investment earnings introduced by the structure of this investment to be unacceptable to us.

However, the longevity risk component remains attractive. So during the quarter, we saw an opportunity to restructure the transaction to reduce earnings volatility and retain the longevity risk. Specifically, we sold the asset-backed note. In connection with the sale, the $400 million repurchase agreement used to finance the purchase of the note was also terminated. You should note that the interest expense associated with this repo will not be incurred in the future quarters.

Finally, we retained the longevity risk in the form of an insurance contract, which indemnifies the holder of the note in the event of nonpayment on the principal of its investment in the asset-backed note. This contract is recorded as a derivative contract and quarterly movements in its fair value will be recorded in the other insurance income line of our income statement.

Moving on, net realized losses for the quarter were $1 million as compared with net realized losses of $2 million in the third quarter of 2006. Net realized losses for the nine months were $6 million as compared with $22 million in the same period last year.

With respect to foreign exchange, changes in exchange rates primarily between sterling and euro versus the U.S. dollar continued to have a positive impact on our net asset positions. In this quarter, we had $7 million in foreign exchange gains and $16 million in the first nine months of 2007. These gains compared with losses of $3 million in the third quarter and gains of $25 million in the first nine months of last year.

Our interest expense for the quarter was $14 million compared to $8 million in the third quarter of 2006. This increase was due to the interest costs incurred on the $400 million repurchase agreement, which I mentioned has now been terminated.

Returning to the balance sheet, our total net loss reserves stand at $4.2 billion and 71% of these net reserves are IBNR reserves. Total shareholder's equity increased 12% to $4.9 billion since year end.

With respect to capital management, in August, we were able to take advantage of the equity market volatility to repurchase 2.2 million common shares for a total cost of approximately $80 million. This brings our year-to-date share repurchases to $180 million. We have a further $220 million available under our current share repurchase authorization. We will continue to actively manage our capital position and evaluate opportunities as they arise. Total capital to deploy in our globally diversified franchise now stands at $5.4 billion.

Now I would like to turn the call back to John.

John R. Charman
Chairman & CEO

Thank you, David. As a general comment, the market continues to be more competitive as the year progresses. As I said last quarter, the increase in competition is particularly apparent in primary insurance lines of business. As always, the magnitude and rationality of this competition varies considerably by line, by segment of the market and by competitor. Opportunities continue to exist in all lines, although we have to work harder each day to try to find them. We believe that the strong marketing initiatives and brand building that we have undertaken over the last four years are key advantages in navigating through these challenging market conditions.

Rate reductions on U.S.

casualty business that were flat to minus 10% have now moved more towards 10% reductions in price. Our rate monitoring shows that our rate reductions are meaningfully below those published in mainstream market indices. An important point is that we are not competing on deductibles or self-insured retentions.

North American catastrophe exposed risks remain the most

attractively priced, although we are coming off peak levels. Aviation, most segments of the marine market, terrorism and international North American non-cat property continue to be the most competitive and we continue to hold an extremely defensive posture here. Whilst the pace of broker request for more favorable terms and conditions are increasing, we are holding firm and the market generally also seems to be resisting.

As I reported in our last call, overall discipline continues

to be maintained in the established reinsurance marketplace and the competitive behavior for the most part appears rational. At that time, I also expressed my consternation with respect to the increased retentions on the part of primary companies given the price competitive behavior we are witnessing in many areas of the insurance marketplace.

I firmly believe this trend towards higher retention should

cease in the coming months. We are of the view that primary companies simply cannot reach the competitive levels of the late '90s without the aid of cheap reinsurance and so far reinsurers have not been leading the market down.

As 2007 has progressed, underlying exposure growth and

experience continues to be dealt with both appropriately and technically by the reinsurance market with some normal competitive wear on price. Broadly, we have not experienced any significant slide in terms, conditions or overrides.

As you know, during this time of year following the July 1

reinsurance renewals, the reinsurance marketplace is relatively quiet. We are still quite far away from the major January 1 reinsurance renewal date, but we do expect the reinsurance marketplace to remain disciplined.

As we have matured, we have continuously experienced improved signings in our reinsurance business due to our high quality financial security, consistency of approach and overall service. During upcoming reinsurance renewals, we expect that we will continue to strengthen our position in the signings for business that we deliberately target. We maintain one of the strongest capital bases amongst our Bermuda peers and this does not go unnoticed by our cedents.

On the topic of the impact of the recent crisis in the financial markets, we continue to monitor potential exposures across our enterprise, which we believe are limited. As discussed by David ,on the asset side of our balance sheet, our assessment of our investment portfolio indicates that we have minimal exposure to sub-prime and credit issues. We have also examined potential exposure in professional lines, particularly in the financial institutions area and we are comfortable at this time that any exposure will be within our estimates of expected loss for these lines.

It is still too early in the credit market to predict the impact of pricing in the D&O market. What is clear is that some lawsuits have been filed, which likely will trigger coverage under D&O policies and we expect that more suits are likely to follow. As we have seen with other market events, total limits purchased will be a key driver to the marketplace. Sub-prime lenders typically did not purchase large limits. This group is expected to bear the brunt of litigation. But companies that have substantial balance sheet exposure to sub-prime mortgages may also be targeted.

We have seen a number of large financial institutions announce charges to earnings for the third quarter. Many of these types of institutions buy only Side A coverage. These factors, combined with a strong risk selection, high attachment points and average net limits of around $6 million at AXIS, support our view that any losses will be manageable.

In conclusion, I once again stress that our core competencies have become even more important, namely: risk selection, pricing experience, negotiating savvy, market positioning, all of these vital attributes, which we possess are showing their true worth in our current and near future trading activity.

Our focus is on how we redeploy capital to maximum advantage. Our experienced underwriters at AXIS have, in previous ventures, strongly differentiated themselves in softening markets. AXIS previously has demonstrated that if we believe there are unacceptable changes in the market, we will quickly and efficiently walk away from unattractive business.

Since our inception, we have been consistently pricing over our required technical margins and we believe there is still ample room to continue to do so. Our price and exposure monitoring continues to underscore the robustness of our current year loss ratios and I am confident the underwriting at AXIS will continue to drive strong results.

Our expectation is that our activities this year will continue to drive strong book value growth of the highest quality. We will continue to seek out ways to outperform over time.

With that, I would like to open the line for questions.

<TAG>Question-and-Answer Session</TAG>

Question and Answer

Operator

Your first question comes from Ron Bobman - Capital Returns.

Ron Bobman
Capital Returns

I had a question about the life settlement note. Could you give us a little more background when the investment was made? I am not sure if I heard you right. Was it a $400 million note? I may have heard you wrong; that sounded awfully large. What was the effect, the economic loss or gain investment to date? Thanks a lot.

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

Sure, Ron. We made the investment at the end of 2006 in the fourth quarter and we were carrying that as a $400 million investment in our other alternatives portfolio throughout the first three quarters of this year. As I made a comment in my remarks, we sold it at the end of the third quarter, so it is no longer on the balance sheet.

In terms of the economic returns, you can go back and look at our results for the quarter, but essentially we were carrying that on a fair value mark-to-market or mark-to-model basis and the net return on the investment side through the quarters was a net of zero through the nine months.

Ron Bobman
Capital Returns

At year-end '06, you had about a $7.5 billion investment portfolio. It is presumably comprised of hundreds if not thousands of life policies, but I am surprised you'd have $400 million in one particular note. Could you comment on that? Out of a $7.5 billion portfolio.

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

We haven't discussed the underlying details of the license settlement, but it wasn't hundreds of thousands of policies I can assure you of that. It was a particular transaction that we spent a great deal of time looking at and we were quite comfortable with the underlying risk exposure in the investment, particularly the longevity risk and we like the way that risk fit into our risk profile.

Ron Bobman
Capital Returns

What do you mean by longevity risk?

John R. Charman
Chairman & CEO

Essentially it has to do with the underlying lives in the policy and how long those lives will continue.

Operator

Your next question comes from Jay Cohen - Merrill Lynch.

Jay Cohen
Merrill Lynch

What was the interest expense associated with the life settlement contract that now goes away, if you could just quantify that?

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

I think it was about $6 million a quarter.

Jay Cohen
Merrill Lynch

Separately, maybe just go over this again, but you seem to suggest that you were now using your own loss experience more in setting accident year loss ratios. Later on in the call, you said you haven't changed your philosophy and I think I understand that, but if you could talk about that and if in fact your own loss experience does suggest lower loss ratios, which I guess that is the conclusion?

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

I think both of those points are correct, Jay. I think overall in terms of our reserving philosophy, we have not changed our conservative nature, so I think that was the point of those comments that I made. But with respect to the current accident year 2007, we have begun to consider some of the experience within this year in establishing the loss ratios that we reported in the third quarter and through the nine-month period, but essentially all within this quarter.

Effectively, we couldn't ignore the favorable experience we were seeing throughout the early parts of '07 in those analyses and that is why we have incorporated that in the current accident year loss ratios.

Jay Cohen
Merrill Lynch

So it is favorable development from the first half of the year?

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

Through the first nine months essentially.

Operator

Your next question comes from Bill Wilt - Morgan Stanley.

Bill Wilt
Morgan Stanley

You are purchasing more reinsurance on your insurance portfolio. Prices in reinsurance presumably favorable and you are happy to lay out some of the risk. John, you have commented on a couple of quarters now the discipline in the reinsurance marketplace. I assume you are very careful about the credit risk you are taking, so could you help square those two actions and comments?

John R. Charman
Chairman & CEO

I think that I have been extremely consistent about my comments about the stability of the reinsurance marketplace in general. We have very high regard to the security that we use and accept within our reinsurance programs. What we are able to do is the fact that we are a very good underwriting company. People recognize that. They saw that our experience through the hurricanes of '04 and '05 was very much broadly in line with the underwriting information they had been provided and we were one of the very few companies that didn't actually exhaust all its reinsurance protection. I think that has been well-received by reinsurers that have been doing business with us for quite some time.

So we are able to squeeze a bit more margin from them on the back of not only our underwriting results, but also the robustness -- and I want to deal with this -- about the way we go about our underwriting.

I have said we have had a price monitoring system in place for the insurance business that has evolved over about 15 to 18 years and it encompasses both new business and renewal business and there is a very strong consistency of approach in the way that we monitor that. That again is respected by our reinsurers.

So the way I square it up, Bill, is the fact that I think we have had a greater benefit because of our underwriting track record and the way we go about our underwriting in a very disciplined way and the fact we will just not accept business unless it is priced right and has the right conditions and has the right deductibles. Our reinsurers are prepared to respect that and price that in accordingly.

Bill Wilt
Morgan Stanley

Is there a governing philosophy that we can keep in the back of our respective heads as we think about your approach to purchasing reinsurance?

John R. Charman
Chairman & CEO

My approach to purchasing reinsurance has always been to either enhance profitability or to dramatically reduce the potential for loss. It has been consistent over the 35 years that I have been buying it.

Bill Wilt
Morgan Stanley

The weighting of the current AXIS individual loss experience with industry data, I asked you to generalize -- realizing it wouldn't be by line -- but could you describe where you are in that process from a broad perspective? Is it 50/50 at this point? Is it still skewed towards more credibility assigned to the industry experience or vice versa?

John R. Charman
Chairman & CEO

I just want to state again what David stated earlier. We maintain our conservative approach to reserving. That is embedded throughout our insurance business and reinsurance business.

Secondly, our price monitoring activity, which I believe is

one of the strongest in the industry and one of the most tested over a long

period of time, allows us to feed automatically through to our current loss

actual market conditions, not perceived market conditions by a lot of people in

the marketplace, ours feed through automatically. We like to think that we do

demonstrate real time our real experience in the marketplace and are then

reserving on a very conservative basis.

So David, I don't want you to overlay on that.

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

Bill, I would just

add this is really related to our shorter-tail lines and within the current

accident year, the view that the experience was more favorable than we thought

we would see at the outset of the year, so we effectively took that into

consideration beginning in this quarter.

John R. Charman
Chairman & CEO

We have not released this. We keep on banging on about many

of our what we consider to be long-tail reserves. We have made that point

quarter after quarter and then if you look at the long-tail element of our

reinsurance business, which is the majority that has an impact on the way that

we are conservative loss picking that business.

Operator

Your next question comes from Matt Heimermann - JP Morgan.

Matt Heimermann
JP Morgan

Could you just clarify on the current year re-estimate, how

many points that was for the full year, the benefit?

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

We don't look at it that way, Matt, so I would just focus on

the end of quarter accident year ratio.

Matt Heimermann
JP Morgan

Could you just repeat

that? I just missed it. I want to make sure I don't inflate anything.

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

We don't provide that individual or that level of detail in

our reserving process, so I would just suggest you focus on our accident year ratios

at the end of the quarter, year-to-date numbers.

Matt Heimermann
JP Morgan

If I heard you correctly with respect to Bill's question on

the reinsurance, John, what it really sounds like you are saying is where you

are buying more reinsurance is property and so this whole issue of growing

reinsurance versus shrinking insurance risk is apples and oranges?

John R. Charman
Chairman & CEO

No, it's broader than

property where we buy across most of our specialty lines on the insurance side.

But I have never believed that in a softening market you increase your retentions.

I have been through about four major

cycles now in my career, four or five, and I believe that is the most prudent

thing to do.

Matt Heimermann
JP Morgan

The last question is the growth you see in the professional

lines and liability lines on the reinsurance side, you mentioned participation.

Could you just remind us what type of client that you are talking about here

and also just the contract form, excess of loss versus quota share and line of

business for example?

John R. Charman
Chairman & CEO

You picked up on the

fact that it is largely excess of loss in our reinsurance portfolio, apart from

the credit and bond portfolios we ride out of Europe,

are predominantly excess of loss and that has been so from the outset. That is

where we chose to position our reinsurance portfolio. I regret that I have forgotten about what your

first point was.

Matt Heimermann
JP Morgan

I just wondered in

addition to excess of loss, the type of customer or accounts that these are,

just specialty versus standard and maybe relative size of companies?

John R. Charman
Chairman & CEO

Well, we actually

have dealt with the diversity within that. We have dealt with them all. But we

have been very nimble. We have been very nimble; I said in the last quarter I

think that one of the things that is very important to our reinsurance people

is the fact they get direct feedback from our primary people in terms of

underwriting behavior. That substantially influences whether we are prepared to

deal with individual cedents or not. But without a shadow of a doubt,

professional lines reinsurance business in the U.S.

was impacted by some of the major companies retaining substantially more of

their business and some retained it all. But we have a very good spread of

cedents geographically and by designated size.

Matt Heimermann
JP Morgan

Is it fair to assume most of this growth is coming just in

the U.S.

operation?

John R. Charman
Chairman & CEO

Yes, for professional

lines, yes.

Operator

Your next question comes from Vinay Misquith - Credit

Suisse.

Vinay Misquith
Credit Suisse

You mentioned that your reinsurance business was affected by

some mid-size losses in the Midwest U.S. and Canada.

Do you have a number on that? I was wondering whether you are writing some

coverage in the Midwest and Canada.

John R. Charman
Chairman & CEO

Well, let me deal
with your latter point. We have a very diversified global portfolio of the reinsurance
catastrophe business and that ranges from Peru
to the U.S. to Europe
and to parts of Asia. So it is globally diversified.
Secondly, it is diversified throughout policy limits. There
has been no change in that. If anything, it has been towards higher layers as
opposed to lower layers, Vinay. All that has happened, and I think you might be
barking up the wrong tree -- if you will forgive me for saying so -- is the
fact that there were a series of losses globally. The UK
you know, Canada
you know, Midwest you know, Peru,
where relatively minor catastrophe losses occurred and we have been prudent in
the quarter in setting up reserves for them. Some we have had notifications
for; others we have had very little notification for. But as we get greater
certainty, we will either confirm those reserves or we will take them down.

Vinay Misquith
Credit Suisse

The only reason is that because for many of the other reinsurers,
you have not really seen this mentioned on the calls before, so I was just
curious why it was more of an issue with AXIS than for others.

John R. Charman
Chairman & CEO

I don't regard it as
material, Vinay, not in the global catastrophe portfolio that we have and
looking at the geographic dispersion of these losses and the number of them.
You know we reserve conservatively, so it's not a big deal.

Vinay Misquith
Credit Suisse

On the absolute level of profitability, pricing is going
down and you have expressed some optimism that reinsurers will not cut prices
drastically even though profitability has been strong this year. What is your
sense for the absolute level of profitability now and how it is going to trend
in the next year?

John R. Charman

Chairman & CEO

Reinsurers price accordingly and are there to make money for their shareholders and so are we. We take, just as every other reinsurer, substantial amounts of risk for the price we get paid. Just because we make a lot of money, that is great and we have given underlying cedents huge coverage and taken pressure off their balance sheet. I am very comfortable with the way that the vast majority of the reinsurance companies that I see, and I touch, and I talk to are transacting business and going about their business.

I am extraordinarily more concerned about the behavior of some of the primary underwriters and the erosion of their net margins. I have said to you many times before and I have said to other people on this call, I have been disturbed by the fact that the CEOs of a lot of companies are so detached from their day-to-day business activities, as well as not really understanding the robustness of their price monitoring in their underlying business, that they are going to have a nasty surprise when their net margins really show up.

So I am pretty comfortable from a reinsurance point of view going into this year end and actually through next year. Don't forget, we have had a pretty benign level of major loss in the reinsurance market.

Operator

Your final question comes from Susan Spivak - Wachovia.

Susan Spivak
Wachovia

John, could you just talk a little bit about how you see the M&A environment developing in the insurance industry over the next six to 12 months?

John R. Charman
Chairman & CEO

Well, you guys know far more about it than I do. We are pretty disinterested in it because we don't see a lot of synergy. Most people are trying to peddle the same wares in our industry certainly on the insurance side and the reinsurance side. There is not a lot of differentiation in first looks at businesses.

Investment bankers are still trolling around Bermuda and the

U.S. trying to fit businesses together, but there is not business logic and until the differentiation in price-to-book between the really good businesses in our industry and the not-so-good businesses in our industry -- with nowhere to go quite frankly -- until those shareholders of those businesses recognize that there is going to be a substantial devaluation in their price to books, I don't expect there to be a lot of M&A activity.

But I believe the pressures will come about during the course of next year that will lead to those weaker players having to do something because it will be more than obvious then.

Susan Spivak
Wachovia

So we are still about 12 months off then from any significant activity?

John R. Charman
Chairman & CEO

During the course of next year, I think an awful lot of people are finding it very tough. I don't comment about other people by name, but we know that a lot of our competitors are finding it really tough. You can undercut prices, but at the end of the day, sustainability in our business is a different factor and you are either a quality operation and there are some very good quality operators in the specialty marketplace, but there are an awful lot of [doffs] if you don't mind me saying so and the market needs to figure that out and properly price them. Then you will get M&A activity.

Operator

At this time, I would like to turn the call back to Mr. John Charman for any closing remarks.

John R. Charman
Chairman & CEO

Well, as usual, thank you all for taking the time to listen to us today. We hope that you are pleased with our results for the quarter and we look forward to talking to you again at in what seems to be a relatively short period of time. Thank you again.