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Markel Corporation NYSE:MKL

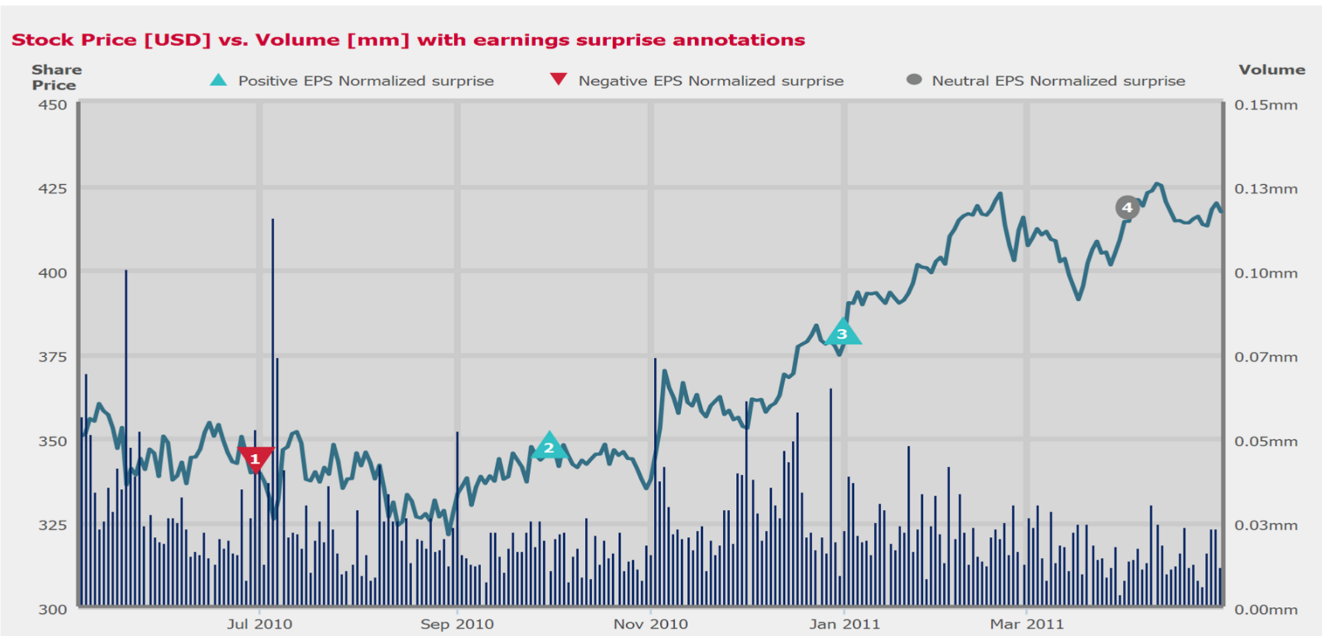
FQ2 2011 Earnings Call Transcripts

Tuesday, August 09, 2011 2:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ2 2011-			-FQ3 2011-	-FY 2011-	-FY 2012-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	4.06	2.99	(26.35 %)	4.47	13.03	17.31
Revenue (mm)	594.69	647.17	8.82	612.64	2438.84	2512.53

Currency: USD
Consensus as of Aug-09-2011 1:04 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2010	3.90	2.30	(41.03 %)
FQ3 2010	3.58	5.86	63.69 %
FQ4 2010	4.38	12.91	194.75 %
FQ1 2011	3.40	(0.14)	NM

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Call Participants

EXECUTIVES

Anne Waleski

Francis Michael Crowley
Vice Chairman

Richard Reeves Whitt
Co-CEO & Director

Tom Gayner

ANALYSTS

Beth Malone
Wunderlich Securities

David West
Davenport & Company

Jay Cohen
Bank of America Merrill Lynch

John Fox
Fenimore Asset Management

Mark Hughes
SunTrust Robinson Humphrey

Meyer Shields
Stifel Nicolaus

Michael Crowley

Richard Whitt

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Presentation

Operator

Greetings and welcome to the Markel Corporation second quarter 2011 earnings conference call. At this time all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. (Operator Instructions) As a reminder this conference is being recorded. It is now my pleasure to introduce your host, Tom Gayner, Chief Investment Officer for Markel Corporation. Thank you. Mr. Gayner you may begin.

Tom Gayner

Thank you. Good morning. I am Tom Gayner and it's my pleasure to welcome you to the Markel Corporation's second quarter conference call. Thank you for joining us. On today's call we will follow our normal line-up with Anne Waleski leading up with the financial results, followed by Mike Crowley and Richie Whitt with operational comments. Then I will discuss our investing and non-insurance activities.

After our comments, we'll all be available for your question. Before we begin, I am duty bound to remind you that during today's call, we may make forward-looking statements. Additional information about factors that could cause actual results to differ materially from those projected in the forward-looking statements is described under the captions Risk Factors and Safe Harbor and Cautionary Statement in our most recent annual report on Form 10-K and quarterly report Form on 10-Q.

We may also discuss certain non-GAAP financial measures in the call today. You may find a reconciliation to GAAP of these measures on our website at www.markelcorp.com in the Investor Information section under non-GAAP reconciliation or in our quarterly report on Form 10-Q.

With that, I'll turn it over to Anne.

Anne Waleski

Thank you, Tom, and good morning everyone. I plan to follow the same format as in past quarters. I will focus my comments primarily on year-to-date results. I'm going to start by discussing our underwriting operations followed by a brief discussion on our investment results and bring the two together with a discussion of our total results for the six month.

Moving right into the underwriting results, gross premium volume was just under $1.2 billion for the first six months of 2011, up 18% compared to 2010. This increase is due to higher gross premium volume in the Specialty Admitted in London Insurance market segment.

As of June 30, 2011, the Specialty Admitted segment included $110 million of gross written premium from our FirstComp workers compensation operations, which we acquired in late 2010. The increase in gross written premium in the London Insurance market segment was due in part to an increase in premiums written by Elliott Special Risks which is now been fully converted from an MGA operation to a risk bearing operation.

We also saw significant increases in premium volume within our Marine and Energy division due in part to offering large loan sizes and an increased pricing environment. Net written premiums were approximately $1 billion, up 17% to the prior year. Retentions were down slightly at 88% compared to 89% in 2010.

Current premiums increased 15% primarily due to the higher earned premiums in the Specialty Admitted in London market segments as a result of higher gross premium volumes compared to 2010.

Our combined ratio was 107% for the first half of 2011 compared to 102% in 2010. The increase was due to a higher current accident year loss ratio and a higher expense ratio, partially offset by more favorable development of prior years loss reserves compared to 2010. The combined ratio for the first six months of 2011 included $99 million or 10 points of underwriting loss for natural catastrophes including the US

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storms in the second quarter and the Australian floods, the New Zealand earthquake and the Japanese catastrophe that occurred in the first quarter.

Our 2010 combined ratio included $17 million or two points of underwriting loss related to the Chilean earthquake. Favorable redundancy from prior year's loss reserves increased to $151 million or 16 points of favorable development compared to $75 million or 9 points of favorable development in 2010. The increase was primarily due to more favorable development of prior year's losses in the Excess and Surplus Lines segment.

In 2010 favorable development of prior year losses was partially offset by unfavorable development of $63 million on the US errors and omissions program for mortgage servicing companies as well as Italian medical malpractice coverage and Australian professional indemnity coverage for construction professionals (inaudible). All three of these programs are now in runoff.

Our year-to-date 2011 expense ratio increased approximately 1.5 points to 42%. Our 2010 expense ratio benefited one point two one-time benefits, a favorable arbitration settlement and an anticipated insurance recoverable.

Now, turning to our investment results, investment income was up slightly in 2011 to $134 million. Net realized investment gains were $13 million, which were flat to 2010.

Unrealized gains increased $170 million before taxes in 2011 due to increases in both fixed and equity securities. Tom will comment with further details in his comments.

Looking at our total results for the first six months of 2011, we reported net income to shareholders of $39 million compared to $63 million in 2010. Book value per share increased 4% to $339 per share at June 30, 2011.

The effective tax rate was 40% in 2011 compared to an effective tax rate of 31% in 2010. A decrease in 2010 is primarily due to having lower estimated income before income taxes in 2011 as compared to 2010.

Now, turning to the cash flow and the balance sheet. Regarding tax flow, operating cash flows were $100 million for the six months of 2011, compared to operating cash flow of $64 million for the same period of 2010. This increase was primarily due to higher cash flows from underwriting activities in Markel International, due to increased premium volume.

Regarding the balance sheet, investments in cash held as a holding company were just over $1 billion at June 30th compared to slightly less than $900 million as of December 31, 2010.

The increase was due in part to $248 million of [court fees] from our issuance during the second quarter of unsecured senior notes with a 5.3% coupon to June 1, 2021.

At this point I want to turn it over to Mike to discuss operations.

Francis Michael Crowley
Vice Chairman

Thanks, Anne, good morning. Second quarter results for the North American operations reflected some of the same trends we saw in the first quarter of 2011. The rate environment was somewhat better in the second quarter. We saw some firming in property rates. However, [casualty] rates remain competitive but the decline in rates was consistent with what we experienced in the first quarter, especially in this segment gross written premium as Anne said, increased year-over-year in second quarter for the same reasons mentioned in the first quarter.

We experienced continued growth in our Equine and Livestock, Agriculture and Accidental health divisions in and FirstComp contributed an additional 51.7 million in gross written premiums. Year-to-date gross written premium in the segment was up 7.1% over the same period in 2010 due primarily to FirstComp where gross written premiums totaled a 110 million. At closing FirstComp gross written premiums were up 11% for Specialty Admitted segment in the quarter.

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Other highlight for Specialty Admitted segment including an agreement with Sally-Mae Insurance Services to provide tuition refund insurance to their college and student loan customers. We've also we're able to gain a new Virginia eight to 12 student access program, which previously written by Markel was very possible. We lost the account in 2007 and we are very pleased to regain it.

The Agriculture division successfully launched a Facebook page Markel [host] and we already have over 600 fans. This another entry into social media area testing the opportunities there for Markel.

We gained momentum on our core products of Equine mortality and farm business. Mortality premiums grew 13% year-over-year in the quarter in farm premium growth was 19% over prior year.

At Markel America, in our Personnel Lines operations we launched a new deductible reimbursement programs in six states and at FirstComp we made final preparations to enter two new states, Louisiana and Alaska and appointed 72 and 29 agencies respectively in those states. We completed product training for Markel's Specialty products at FirstComp and actively began selling Markel's [shop here] products to FirstComp's agency base. We also have appointed over 100 FirstComp agents today who previously did not have access to Markel's products.

In the ENS segment the second quarter also showed continuing trends from the first quarter. While overall growth written premiums declined 7% in the quarter, this shrinkage was due largely to the loss of two significant accounts. We mentioned the loss of a book of [fourth place] property business in the first quarter. We also lost a relatively large auto account. But I want you to keep in mind that we are comfortable losing revenue when it is not profitable or when pricing in our opinion becomes unreasonable.

Core regional premium for the quarter continued to increase by 2%. We are very encouraged by the continued growth in our contract binding business, casualty binding business was up 14% and property binding business was up 21% in the quarter.

Our wholesale broker [4-O] is progressing and we expect to go live in the third quarter. We've made improvements in the look, field and functionality of this website and in the underwriting and pricing of our binding business. This quarter we will make it much more attractive and easier for agents to do business with Markel.

Our wholesale regions also held underwriting seminars with agency personnel throughout the second quarter. We engaged over 500 agent representatives for product education and onsite quoting during these seminars.

Our underwriting product line leadership was also very active in the quarter. Our product line leaders are in various stages of updating and providing authority standards and metrics. We completed the updating of the environmental product line and expect to update inland marine and casualty in the third quarter. We also launched admitted errors and omissions and admitted architects and engineers product in the quarter. Numerous other product enhancements are in the works.

In summary, all of our North American operations continue to focus on increased interaction with our agents and brokers, product enhancements, new product and program development and increased renewal retention. We are encouraged by the growth in several of our business segments, however we recognize there is still much to be done and the challenges that we face from both the rate and economic standpoint still exists.

I'll now turn it over Richie Whitt.</TAG>

Richard Reeves Whitt
Co-CEO & Director

Thanks Mike and good morning everybody. Many of the things Mike described in the U.S. are true on the international side as well; as a result I'm going to keep my comments brief.

The rating environment that Mike described in U.S. is very similar to what we're seeing in the international market. Cat-exposed property business is moving up however non-cat and casualty business continues

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to be very competitive. While rates in these areas appear to be flattening out, there is still abundance competition.

The second quarter was again acted in terms of cat events as Anne said. This was highlighted by the devastating U.S. storms. In the second quarter, Markel International recorded 10 million of losses in the U.S. storm and increased reserves on the Japanese quake and tsunami by 7 million. As I discussed on the first quarter call, Japanese quake and tsunami situation was still evolving at that time.

During the second quarter, many seeding insurance companies and direct insurers increased their initial estimated losses and as a result we increased our reserves by 7 million in the second quarter.

Losses tend to develop and settle very quickly in the Japanese market. Our information on loss reports are much better today than they were at the end of the first quarter and as a result we feel we have established adequate reserves for these events. Obviously, given the magnitude of the quake and tsunami, our reserves are still subject to volatility.

Gross premium volume was up 22% on the international side in the first half of the year. As Anne said, this was primarily due to Elliott Special Risk in Canada being fully integrated and due to continued organic growth in our Marine and Energy book.

On the expansion front, we recently announced that we will be opening a branch office in Rotterdam, The Netherlands and we expect that this office will begin operations late in the third quarter. Also during the quarter we made a small agency acquisition in Sweden. This expands and strengthens our branch office in Stockholm. These activities are continuation of our strategy to build a global network of branch offices producing profitable specialty business in their local markets.

We are really pleased with the progress that all of our branch offices continue to make, in particular the Elliott Special Risk team in Canada has done a terrific job of renewing and developing their book of business in a really difficult Canadian insurance market.

Finally, I know we say it every quarter, but I am going to say it again, pricing in the property and casualty industry marked the increase. 2011 is all the proof you need with insured catastrophe losses of over $60 billion in the first six months, deteriorating reserve position and core investment returns especially given recent events.

It’s a fact; you can’t write an underwriting loss and think you’re going to make it up on volume; people are kidding themselves. At Markel, we remain disciplined and are looking for opportunities to increase pricing to more appropriate levels.

That’s it from me and now I’ll turn it over to Tom.

Tom Gayner

Thank you, Richard. I am pleased to report to you that we enjoyed a good first half of 2011 in our investments in industrial operations and I look forward to your questions. In the midst of turmoil in daily financial markets, it’s important to remember the longer-term underlying and unchanging principles we used to make decisions at Markel.

As I stated last quarter and probably the quarter before that, the strategic goal of the investment department are number one, to protect and preserve the balance sheet from high quality fixed income investments. Two, to allocate as much as possible the higher total return equity investments. And three, to increase the overall earning power and financial flexibility of the Markel Corporation through the ownership of a variety of profitable businesses.

None of that changes but as the U.S. government is rated AA or for those of you with long financial memories and about questionable financial episodes and some sense of irony is (inaudible).

I am happy to report that we touched all the bases during the first half and that we continue to be on track to accomplish our strategic goal. As to the numbers, during the first half, the total return for the

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investment portfolio was a positive 1.2%, equities were up 4.5%, fixed income was up 3.6% and the CapEx added between 6%.

Additionally, other revenues in Markel which are largely those of the Markel Ventures Company were $168 million for the first half, versus $77 million in the prior year, an increase of more than 100%. Markel's share of the associated EBITDA totaled $20.7 million versus $8.6 million of more than double the level in 2010. As always the reconciliation of EBITDA for net income is available on the website. The net of all of this is that even with the catastrophic events of the first half, we're reporting positive comprehensive income in Markel in a new record type of value per share of $338.66. In keeping with our first strategic objective of preserving and protecting the balance sheet for the fixed income portfolio, we continue to maintain a portfolio that is high quality and short duration.

Last quarter I said that we don't think you get paid fully for taking credit risk. This quarter I would amend that to say we now don't think you get paid at all and we sure don't think you get paid for taking inflation and currency risks. Consequently our portfolio reflects this belief. For yet another quarter it remains a matter of slack-jawed amazement to me that long-term interest rates are as low as they are given current policy and circumstances.

While, we have been and continue to be early in being cautious about these risks, we do not understand and will not accept the current market offer for taking them. We think it is more important to protect the portfolio entirely through interest rates.

As to our second objective of allocating as much as possible to higher total return on equity investments, during the quarter we continued to methodically increase the percentage of our portfolio invested in the equity. This has been our consistent pattern for the last few years. As June 30, the total public equity portfolio grew to $1.84 billion or 55% of our total shareholders equity.

As the major of the equity markets in the first quarter of [2009] equities comprised over 45% of our shareholders equity. Since that time we have been methodically and continuously investing in high quality public equities and the first half of 2011 continues that pattern. While on fixed income and equity investments have been remarkably similar in the recent years, I expect the normal historical relationships to resume and I think we will well served by maintaining and increasing our commitment to equity as time goes by. High quality equity now offer the biggest equity risk premiums since the 1950s. We think we are getting paid well to take that risk and we are doing well.

Fortunately through the aggressive actions of my insurance colleagues who have worked tirelessly to find new profits and new ways to serve our customers as well as with acquisition of Aspen, premium volumes are beginning to increase at Markel. With higher premium volumes and the capital strength and cash that we have right here, we are in a wonderful position to step on the gas a bit harder and accelerate our purchase of equities.

We can also do this and pick up investment income at the same time given the dividend yields of high quality common stocks. Given all those circumstances and current prices, expect to see us buy more stocks. We also think that this is not a common view in the industry and will serve to differentiate us as time goes by. As to our third objective of building the earning power and financial flexibility of the Markel corporation by earning the variety of profitable businesses, we continue to be very pleased with the ongoing growth of our Markel ventures. The businesses are producing results in line with our expectations and they are adding value to Markel.

During second quarter we purchased PartnerMD, a concierge medical practice with three offices in Virginia. We've known the principles of PartnerMD for years, and we are excited and confident about the future contributions to Markel. With a permanent capital base that Markel provides and the changing medical landscape, we think we offer an excellent home for general practice physicians to deliver high quality care to the patients.

While the initial transaction is small, we are optimistic about the future growth and profitability with PartnerMD. We also continue to work on other transactions and we expect ongoing organic and acquisition opportunities within the growing framework of Markel Ventures. Our portfolio and our acquisitions

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remain conservative. We believe that our fortress balance sheet which enabled us to withstand the sort of catastrophic and natural events we experienced during the first half and then withstood the sort of financial catastrophes that incurred in 2008 as well as the current drop in the barometer.
By having the balance sheet we built over the decade, we've been able to respond to opportunities in the insurance, investment and industrial world to the build the value of your own company. We continue to see opportunities on all fronts and are pleased to report to you that we have financials and human capital as well as the courage and creativity needed to make the most of it. With that I’d like to open the floor for questions.

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Question and Answer

Operator

Thank you. We will now be conducing a question-and-answer session. (Operator Instructions). Our first question comes from Beth Malone with Wunderlich Securities.

Beth Malone
Wunderlich Securities

At the beginning of the presentation, you talked about an account in Virginia that you had lost. There was an education account that now you got it back, lost in 2007, got it back today. What changed or why did that move back to Markel?

Francis Michael Crowley
Vice Chairman

I don’t have the exact answer to that. My guess is that you know, they were unhappy with the current environment and service from the current carrier.

Beth Malone
Wunderlich Securities

You pointed that out, is this typical of what's been happening for Markel, as pricing has been so soft and you all have refused to participate, is this an indication that the market is starting to appreciate the value of Markel's services or something? And we should anticipate that this is part of all pricing getting better or the environment improving for Markel?

Francis Michael Crowley
Vice Chairman

I think it makes sense to look at that from that standpoint to some degree. I can tell you that we are beginning to see some initial situations where business that we either decline for pricing reasons or we are not able to attract for pricing reasons, it is showing up in some of our submissions.

On the specialty side, just the other day I heard of several accounts that are coming to us, that are right up our alley that we think we’ll have an opportunity to ride because of a more favorable rate environment. But I want to caution you. I think this is just the beginning and we’ll see how it plays out, but we are encouraged by what we see.

Beth Malone
Wunderlich Securities

And then just on the topline growth in the international, you said that the acquisition of Elliott was a big factor there. Exactly what kind of rate increases are you seeing on the international book and how important is that to the growth you saw in the second quarter compared to a year ago in the international business?

Richard Reeves Whitt
Co-CEO & Director

I mean I think the only places that we’re really seeing rate increases would be cat-exposed property and in the energy classes, some of the energy classes. That is a pretty much it. What we are seeing there I think is flattening out in some of the other areas and Mike was talking about accounts that may be moved away from a few years that have shown back up and we are seeing some of that in London as well. We were dampened with losses in professional account over the last few years and all of a sudden they are coming back to us with the little bit better pricing and they may be unhappy with their current situation.

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So, I think as Mike said, there is a positive signs out there but to say that is much in the way of price increase and the growth that we are showing right now in London, very little. Elliot Special Risk is on a yearly basis about 100 million of premium and, so that we are seeing coming through by numbers though the first six months, about half of that. And then on the Marine Energy side, yeah we are seeing a little bit of price increase there. We got some organic growth just because of some of the dynamics in that market.

Beth Malone
Wunderlich Securities

Okay. And then just as a follow on with all the losses you guys described that you had in the industry experienced in the environment, the low interest rate, what do you think is the major reason that we are not seeing more of a across the board rate increase in the market place. Is this really due to the weak economy?

Tom Gayner

Yes, it think a lot of it and I think also in 0% interest rate, the acceptable rate of return that people are willing to lay their capital out for is supporting all that. That's why or really the normalized cost of capital that is out there but I think that's the reality of what happened on the day-to-day basis.

Beth Malone
Wunderlich Securities

Okay. And then one last question to you Tom, as the valuation of the market place has changed pretty dramatically over the last couple of weeks and the outlook, I am not sure what the outlook is anymore in terms of economic recoveries. But do any of these factors change your appetite for the types of companies that you -- I know you have a very defined thing that you are looking for but is this all through it all the kind of companies you are looking for to partner up with?

Tom Gayner

It doesn't alter what I am looking for all, what it alters is the ability to few clients what I am looking for. That's a price lower. So, I always look for profitable businesses, run by managers [inaudible] measures of capital integrity, they have the ability to use the capital and they are priceless. So, the only things changed in the [inaudible], they are priceless, there is stuff on sale, an opportunity to find those first reaction we sort of are looking for.

Beth Malone
Wunderlich Securities

Now that said, is there a limit as to how much capital you are willing to expose to that particular type of investment?

Tom Gayner

Absolutely. The shareholders equity account or stock, what's the ultimate amount of capital to allocate that risk, but you've got a lot of flexibility being where we are and not holding the number and reasonable reporting, and that's what we think will earn the best returns on capital which has some lovely attribute making its own capital assets.

Operator

Thank you. Our next question comes from the line of John Fox with Fenimore Asset Management. Please proceed with your question.

John Fox
Fenimore Asset Management

Number one for Tom, what were some of these more recent acquisition? Can we get an update on the run rate for revenues for ventures?

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Tom Gayner

Yeah. I think 275 to 300 million at the top line is the run rate here.

John Fox
Fenimore Asset Management

Okay. Terrific. I don't know who is disclosed first that 15 million year-to-date, I guess excess losses or reserve take up whatever. My question is are those actual losses or is that kind of bringing that up to the Markel standard margin of safety and it's the ladder where are you in that processes?

Richard Reeves Whitt
Co-CEO & Director

John, its Richie, you know we kind of talked about probably in the fourth quarter call that we expected FirstComp to be at a underwriting loss this year as we got to the third quarter.

John Fox
Fenimore Asset Management

Right.

Richard Reeves Whitt
Co-CEO & Director

Yeah. we though we have maybe $30 million underwriting loss this year at FirstComp as we sort of move toward our reserving standard as we layered our conservatives among the pick and all those sort of things and I think we're six month we are right on target for that. So things are going basically as we expected, actually maybe things going little bit better than we expected because we're starting to see a little bit of price move in the workers comp market and god knows it need it so we're hopeful.

John Fox
Fenimore Asset Management

Okay. So that run rate really is going to continue this year?

Richard Reeves Whitt
Co-CEO & Director

Yeah, we're right on target there.

John Fox
Fenimore Asset Management

Okay. And Richie while I have you, I think because you are the international guy. Could you talk about the 10 million in the Marine energy I mean you put in the cat table were they really cat. What were the nature of those losses?

Richard Reeves Whitt
Co-CEO & Director

They are energy losses basically. We are growing our marine and energy book significantly we're probably going to write, rough number is 250 million in marine and energy this year. So that book is getting substantial. As you know John the we keep as much as of it as we can possibly can. So we have a reinsurance program where we keep pretty much $10 million at the bottom of the program. So we had two relatively sizable losses in the book of $250 million book of business that and take a few of those dips.

John Fox
Fenimore Asset Management

Right.

Richard Reeves Whitt

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Co-CEO & Director

But these were fairly early in the year. So they are not really CAT but just large losses and we are going to expect to have a few of those in year on the $250 million book. And we will see how the rest of the year plays out.

John Fox
Fenimore Asset Management

And what's the catalyst for that loss and obviously have few type of damage that is kind of a one-off?

Richard Reeves Whitt
Co-CEO & Director

One was an offshore will platform that sustained some serious damage. The other one was a pipeline spill where there is some clean up costs and obviously fixing of the pipeline and various things like that. So, two pretty big loses to the market and we participated on those.

John Fox
Fenimore Asset Management

Okay and I think this is for Anne. And the June debt offering, what are your plans for the proceeds?

Anne Waleski

Well right now the parties I think we set any offering there for general purposes and potential acquisitions. We are generally viewing them as increasing our flexibility to take action, where we see opportunities for instance if had an opportunity which I don't think we will do at the moment to buy back some of the 2013 we would exercise that option and if had an M&A opportunity that we thought was really interesting, we can do this for that. So right now it's really just increasing our flexibility to do any number of things.

John Fox
Fenimore Asset Management

And the 2013, is there a call feature or why can't you repurchase them?

Anne Waleski

I do think that the purchase prices right now are very attractive. We can repurchase them. I just don't think we will at the moment.

Operator

Thank you. Our next question comes from the line of Mark Hughes with SunTrust Robinson Humphrey. Please proceed with your question.

Mark Hughes
SunTrust Robinson Humphrey

Thank you very much. The favorable development in the excess and surplus, anymore detail you can provide what the specific lines benefited is in this case?

Michael Crowley

It was pretty much a core business in our binding, property, casualty business.

Tom Gayner

Professional liability, right?

Anne Waleski

Yeah, primarily professional and products liability and it was within the '06 and '09 accident years.

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Mark Hughes
SunTrust Robinson Humphrey

Yeah. That's helpful. Thank you. And then the expenses in the Specialty Admitted and the London segment were fairly low this quarter. Would you expect that to be sustained or is this just a little random variation?

Anne Waleski

I think part of that is - if you are looking at the expense ratios being driven by the increase in earned premium as well as first Tom has a slightly lower expense ratio within Specialty Admitted.

Mark Hughes
SunTrust Robinson Humphrey

Right. So assuming the earned premium trends hold up and the expense ratios should continue to be a little more modest?

Anne Waleski

I think you can assume that, yeah.

Operator

Thank you. Our next question comes from the line of Meyer Shields with Stifel Nicolaus. Please proceed with your question.

Meyer Shields
Stifel Nicolaus

If we take out the primary development and the significant catastrophic losses, we still saw a four or five percentage point increase in the loss ratio for excess and surplus and Specialty Admitted. I was wondering if you could talk to that a little.

Anne Waleski

Meyer, what I can tell you at a high level is, some of that is related to mix of business Mike allude to some of the accounts that have moved on so there is some of mix of business in that. With the addition of Aspen within Specialty which is adding to that and then there were those large losses that we talked about and that Richie just covered.

Meyer Shields
Stifel Nicolaus

Okay.

Tom Gayner

One of the point its worth adding Meyer, is we've consistently stated this reference for decades on what else to -we try to reserve on day one in light of the levels that's more likely to be done in the specialty. So that you're seeing pretty normal reserve development this year, we will (inaudible) but we exit out in 2011 (inaudible) is the sort of thing that we try to look and have been practice here in Markel rather than extraordinarily.

Meyer Shields
Stifel Nicolaus

I understand that, and I have always assumed that. I was just wondering about the sequential change from the first quarter to the second quarter of 2011. With regards to 100 first [comp] agents that you said are emerging from Markel, is that for all Markel products then?

Michael Crowley

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No it would just be for our specialty product lines we'll chalk here so services and some things we expect to see duplication in terms of the kind of the current business as first comp we're writing. You know I think then in the first quarter that we had gone through all our first comp agents and identified about 400 agents where we thought there was opportunity to cross sell Markel products and we've now appointed about 100 of them.

Meyer Shields
Stifel Nicolaus

Okay, but that's for very specific products. It's not the entire portfolio?

Michael Crowley

Right.

Meyer Shields
Stifel Nicolaus

Okay. And last question for Tom if I can. Will you look at I guess where we're seeing incremental investments obviously the equity portfolio is growing a little bit. We're also seeing foreign governments and short-term investments grow very rapidly. Is that just timing or is there something particularly attractive there?

Tom Gayner

That would be some reflection as we run our business (inaudible) and just like we match the insurance liabilities in the U.S. against largely U.S. based securities when we write business overseas we tend to match that in a local currency investment and some sorts of that we build pay currency with on the balance sheet.

Meyer Shields
Stifel Nicolaus

Okay. So is the way you are addressing that through government issued securities of those equities?

Tom Gayner

Largely, but there are some equity that we own and that gets into nomenclature as well because you know for instance, you know its no secrets that we own Biagio, Biagio shows up on the statements as a UK-based company, and North America is their largest market. So it's a little bit definition to describe that in international numbers. Similarly that also appears in cat attractive and has done more business overseas and in U.S. for decades. That shows up that the U.S. based investments and I would largely describe that as more powerful which is outside of course of U.S. (inaudible)

Meyer Shields
Stifel Nicolaus

Okay.

Richard Whitt

Meyer, you also keep in mind, we had the debt offering in the second quarter and obviously we haven't gotten around to allocate that out to the portfolio yet. So until that happens, you put it in fairly short term treasuries and money funds and various things like that. And as Tom said, we are fairly measured in how we do things. So overtime, we will reallocate that into the longer portfolio or to Markel Ventures or to equity.

Operator

Our next question comes from the line of Jay Cohen with Bank of America Merrill Lynch. Please proceed with your question.

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Jay Cohen
Bank of America Merrill Lynch

Yeah, thank you. A couple of questions, first is on the ventures because you had talked about Tom what you thought a normalized level of revenue would be and the bottom-line, the income sequentially jumped up and obviously been adding to that business, should we look at this quarter as a fairly normalized earnings contribution as well as is there anything unusual in that number that either helped or detracted from the number?

Tom Gayner

No, we are quite too early in the history of Markel Ventures annualized third quarter. The businesses are doing well but as you might suspect from having known Markel for a long time we are not running them in 90 days for increments. We are thinking about the long term economics and I mean obviously with the way they are doing and we expect more of the same, but that doesn't come out on 90 day.

Jay Cohen
Bank of America Merrill Lynch

And then a number’s question, as we look at the operating earnings excluding net realized gains, it looks like the tax rates on the operating earnings in the second quarter is relatively low, and I am wondering if there is anything distorting that?

Tom Gayner

Jay that's just going to be the fact that pre-tax is dropping, but we have a pretty static allocation to tax exempt bonds, so that permanent item that tax exempt amount becomes a larger percentage of the pre-tax and that goes against the operations.

Anne Waleski

It’s also that we have a lower rate on the foreign operations in that.

Jay Cohen
Bank of America Merrill Lynch

Got it; that does explain it. And then if I could squeeze one more in for Tom Gayner, Tom, I wouldn't mind if you would reflect a little bit on this action by S&P, and specifically what it might mean for your muni-portfolio going forward?

Tom Gayner

Well, I don’t think that it really is a surprise to the marketplace quite frankly with respect to determine rank of the last 48 hours or so I don’t think it makes any difference at all. We’re well upon and in terms of your muni part of your question from Richmond, Virginia and that happen to note that the Commonwealth in Virginia is in surplus this year as it was last year and I think there were something like when we started 30 sticks AAA rated accountings in the country and we are calling from one of them and another one of them (inaudible).

When you look the state and municipal level of finance, actually it looks better than the federal government; largely that they are operating on a shorter winch and they have a balanced budget requirement, so actually pretty good about the [community] and one of the points that I noted to our Board, if you look (inaudible) the City of Atlanta as an example switch over to (inaudible) 401 (k) style plans from a defined benefits plan. That’s not a passion of conservatism to grow with the Atlanta City government so the fact that the reality was they needed to change to keep the doors open, they did and you’re saying basically valuable, makes tougher, harder and I would argue better decisions with (inaudible)

Jay Cohen
Bank of America Merrill Lynch

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It sounds like a very sane view, nice to hear something that sounds sane these days. Thank you.

Operator

Thank you. (Operator Instructions) Our next question comes from the line of David West with Davenport & Company. Please proceed with your questions.

David West
Davenport & Company

Returning back to expense questions a little bit. I wonder if there are any comments relative to the One Markel initiatives or are those pretty much winding down?

Anne Waleski

I don't know we had much in the way of comments really to one Markel as we talked about in prior calls that actually move to the regional model is now finished and implemented and working as we are getting good feedback from our distribution partners on how that's working relative to some of the IT initiatives that we were working on relative to that specifically this year, the data warehouse and the broker portal. The broker portal is in a beta test stage at this point and data warehouses moving along as we anticipated perhaps slightly slower that we anticipated going to deliver the results we had hoped for. So I don't see know that there is too much to talk about in the sense ratio other than normal run rate senses from the IT project.

Tom Gayner

And I think this the last big year of spend on that and next year I think its just sort of run rate, sort of IT investment, the things you have to do to keep your IT competitive with rest of the market.

David West
Davenport & Company

Very good and then the comp kind of returning back to Markel venture, is there any particular seasonality in the patterns of revenues and profits that you can see right now with your portfolio?.

Tom Gayner

Each do have some seasonality associated with them, but as that business grows and its spread widens different ones will be on different seasons. So I don't think we are going to see for now seasonality out of those types of businesses. I guess we are partners and there might be [inaudible] on that.

Operator

Thank you. Mr. Gayner there are no further questions at this time. I would like to turn the floor back over to you for any closing comments.

Tom Gayner

Well, thanks so much for joining us. We are available as always and we appreciate your loyalty and support and we will talk to you soon. Thank you. Bye.

Operator
Thank you. This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.

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