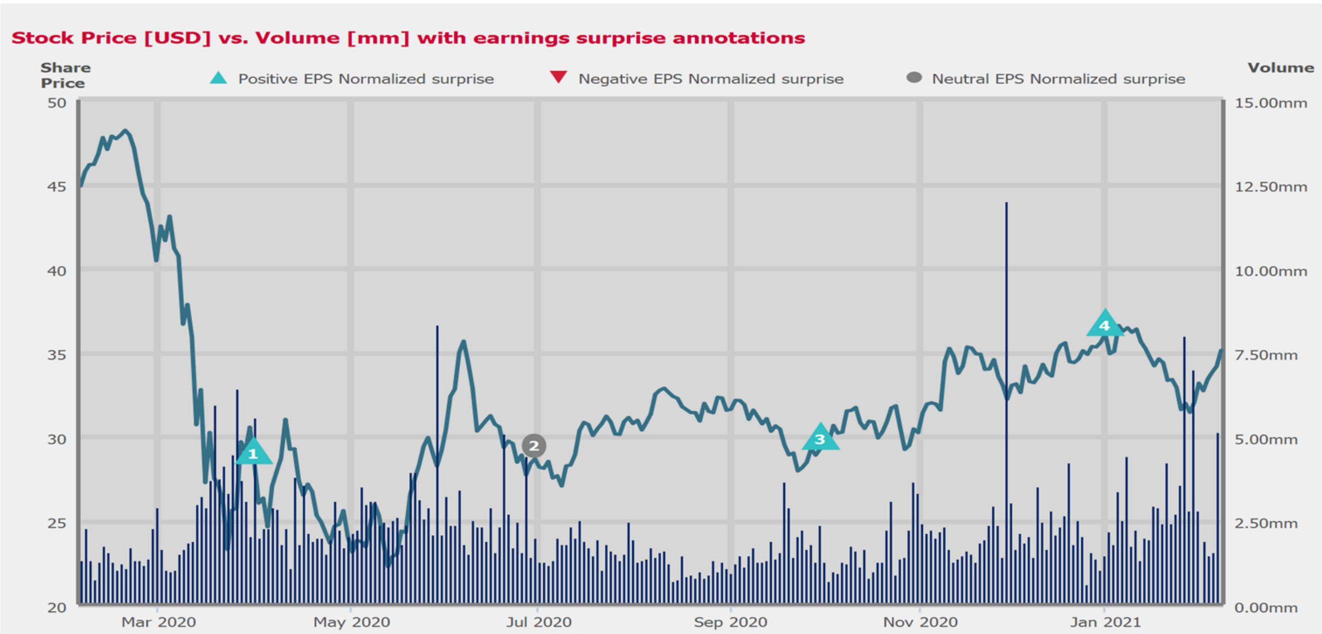
S&P Global
Market Intelligence

Arch Capital Group Ltd. NasdaqGS:ACGL
FQ4 2020 Earnings Call Transcripts
Wednesday, February 10, 2021 4:00 PM GMT
S&P Global Market Intelligence Estimates

	-FQ4 2020-			-FQ1 2021-	-FY 2020-			-FY 2021-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS
EPS Normalized	0.38	0.56	▲47.37	0.72	1.18	1.36	▲15.25	3.10
Revenue (mm)	1590.93	1660.30	▲4.36	2281.43	6940.69	6900.13	▼(0.58 %)	7913.37

Currency: USD
Consensus as of Feb-10-2021 10:36 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2020	0.41	0.46	▲1 12.20 %
FQ2 2020	(0.17)	0.04	NM
FQ3 2020	0.17	0.29	▲2 70.59 %
FQ4 2020	0.38	0.56	▲3 47.37 %

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Call Participants

EXECUTIVES

François Morin
Executive VP, CFO & Treasurer

Marc Grandisson
CEO & Director

ANALYSTS

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UBS Investment Bank, Research Division

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Deutsche Bank AG, Research Division

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Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Fourth Quarter 2020 Arch Capital Group Earnings Conference Call. [Operator Instructions] As a reminder, this conference call is being recorded.

Before the company gets started with its update, management wants to first remind everyone that certain statements in today's press release and discussed on this call may constitute forward-looking statements under the federal securities laws. These statements are based upon management's current assessments and assumptions and are subject to a number of risks and uncertainties.

Consequently, actual results may differ materially from those expressed or implied. For more information on the risks and other factors that may affect future performance, investors should review periodic reports that are filed by the company with the SEC from time to time.

Additionally, certain statements contained in the call that are not based on historical facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The company intends the forward-looking statements in the call to be subject to the safe harbor created thereby.

Management also will make reference to some non-GAAP measures of financial performance. The reconciliation to GAAP and definition of operating income can be found in the company's current report on Form 8-K furnished to the SEC yesterday, which contains the company's earnings press release and is available on the company's website.

I would now like to introduce your host for today's conference, Mr. Marc Grandisson and Mr. François Morin. Sir, you may begin.

Marc Grandisson
CEO & Director

Thank you, Liz. Good morning, and welcome to our fourth quarter earnings call. Overall, we are pleased with the current market conditions and the opportunities available to Arch as we close out 2020 and spring into 2021. One of our fundamental principles is that achieving growth and book value per share above the cost of capital over the long run is the best way to create and sustain shareholder value.

We believe we delivered on that front in 2020. Our disciplined underwriting and diversified business model enabled Arch to grow its year-end book value per share by 5.4% over the third quarter and by 14.7% for the last 12 months. We responded to broadly hardening market conditions and, as a result, all 3 of our segments grew their premium writings in the quarter.

In particular, the hardening markets allowed for significant growth within our P&C units, increasing our net premium written for the P&C by 32% for the full year. On the whole, for 2020, we achieved an operating profit of $557 million and grew book value to $30.31 per share.

Now as most of you know, cycle management is core to who we are. Arch leans strongly into improving markets because history has shown that times like these are when superior risk-adjusted returns gradually compound and accelerate book value growth. And Arch's position to significantly expand as others derisk, rethink their underwriting strategies or even retrench.

As we look at the opportunities ahead for Arch, I'm reminded of a situation in hockey that is exciting for any fan. In hockey, you get a 1 player advantage if the other team takes a penalty. It's called a power play. When that happens, a few things need to be kept in mind as you deploy your specialty power play unit to try and improve the odds of scoring.

You need to have a clear 5-on-4 strategy. You need to be defensively savvy enough to not forget to protect your own zone. And you need to have a sense of urgency because the clock will tick down, and you will soon be back to even strength. These are the few moments that make a difference in a hockey game.

The advantageous position we find ourselves in is similar to that hockey power play, where the odds are in our favor. I'm proud of how our team performed last year during the challenges of 2020. Now after spending a good portion of the last several years in a defensive position, we're embracing a more offensive mindset.

Here's what that looked like in the fourth quarter. Let's begin with our insurance segment. Across our worldwide insurance group, renewal rate changes increased approximately 12%, up 200 bps from the prior quarter's rate changes.

Our fourth quarter growth occurred in many lines, with D&O, property, energy and marine all exhibiting strong advances. E&S casualty and our alternative markets business also grew this quarter. We believe that rate momentum in these lines is healthy, and we also see it building in other lines, albeit at a slower pace.

Increasing margins helped improve our insurance accident year, ex cat loss ratio, which decreased by 4.6 percentage points in the fourth quarter. As you may know, the full effects of increased rate levels can take approximately 5 quarters to become fully reflected in underwriting margins.

So today, we are earning the higher rates from the past year. In addition, our operating expense ratio has benefited from rising production this past year. We are pleased with the continuing progress achieved by our insurance group in the last 2 years.

Turning next to our reinsurance segment. Underwriting results were significantly better than the fourth quarter of 2019 despite the impact of $94 million worth of cat losses. While market conditions are not uniformly strong in the reinsurance sector, dislocation from other carriers that are reducing their positions is creating pockets, with hardening rates that Arch is well positioned to capitalize on.

Reinsurance also benefits from the underlying insurance market rate increases through its clients. For 2020, we grew reinsurance net written premium by 53%, with the 2 main areas of growth being non-cat property and specialty.

At the January 2021 renewals we saw continued rate increases in most areas. However, we agree with the market consensus that property cat pricing moves were more subdued than expected or hoped as capacity for that risk still remains strong. Accordingly, we maintain a cautious approach to this business.

Our mortgage segment delivered good returns in both the fourth quarter and for the entire year despite the economic headwinds. We are confident in the continued earnings strength of this segment and, frankly, the uncertainty we were facing during the early stages of COVID has been largely mitigated.

Both premium rates and the credit quality of the new insurance written improved in 2020. And accordingly, the return on capital for our new U.S. MI business is essentially back to 2018 level, which was a strong year. Here's why MI has done well this past year.

First, housing markets have remained strong despite the difficult economic conditions. Second, the government forbearance program achieved largely what it was intended to do, which was to provide financial respite to many homeowners. And third, credit criteria in the mortgage sector tightened in 2020. And as you know, credit quality is a critical factor in determining underwriting profitability.

On a side note, just yesterday, the FHFA announced that the forbearance program has been extended an additional 3 months, which should help further mitigate the risk in our delinquency inventory. The delinquency rate of our portfolio decreased by 50 bps sequentially in the fourth quarter. At year-end, roughly 2/3 of our delinquent loans were in the government-sponsored forbearance program.

We currently estimate that 89% of delinquent borrowers in our portfolio at year-end have at least 10% equity in their homes. And as we have discussed on prior calls, the amount of equity in a home is the single most important factor in determining MI losses as it plays a significant role in mitigating claim activity. We are cautiously optimistic that delinquencies will continue to cure as vaccines enable the economies to reopen.

Importantly, record home purchases in the U.S. in 2020 supported a 5% price appreciation nationwide, while historically low interest rates accelerated housing and refinancing demand. This enabled Arch U.S. to report record NIW of $38 billion in the fourth quarter of 2020, up nearly 60% from the same period in 2019. Our outlook for continued growth in 2021 remains positive.

Turning back to the current phase of the P&C cycle. There are 3 conditions that we believe will persist and help sustain the improved underwriting environment. One, social inflation and reserving problems are now starting to apply pressure for companies that haven't been prudent enough. Two, anemic investment yields require a sharper focus on underwriting profit. And three, a return to a post-COVID world should accelerate economic activity and increase the demand for insurance.

Each of these conditions will put pressure on results for the industry. Our conservative approach to reserving over the past several years means that we are well positioned to drive results in P&C going forward since we expect our future returns to better reflect current and forward pricing. Finally, with better visibility into the overall economic conditions and with more clarity on the mortgage and P&C prospects, along with our strong capital generation, we see a compelling opportunity to invest in our shares at very attractive returns. François will talk to it in a moment.

This recent share repurchase is a testament to our capital strategy and designed to enhance shareholder value over the long term. We still have ample resources to deploy towards new growth and feel confident in our team's ability to be creative in order to capitalize on the opportunities before us. This is a time in the game where our cycle management strategy allows us to play offense and deploy capital dynamically to generate above-average returns.

And now I will turn the game commentary over to François.

François Morin
Executive VP, CFO & Treasurer

Thank you, Marc, and good morning to all. We at Arch hope that you are in good health and that 2021 is off to a good start. On to the fourth quarter results. As a reminder, and consistent with prior practice, the following comments are on a core basis, which corresponds to Arch's financial results, excluding the other segment, i.e., the operations of Watford Holdings Ltd. In our filings, the term consolidated includes Watford.

After-tax operating income for the quarter was $230.4 million, which translates to an annualized 7.7% operating return on average common equity and $0.56 per share. For the year, our operating return on average common equity stood at 4.8%, while return on average common equity stood at 11.8%. Book value per share increased to $30.31 at December 31, up 5.4% from last quarter and 14.7% from 1 year ago, again, an excellent result despite the strong headwinds from catastrophe losses this year, which is a testament to the resilience of our operations and our superior diversification strategy.

Losses from 2020 catastrophic events in the quarter, including COVID-19, net of reinsurance recoverables and reinstatement premiums, stood at $156.4 million or 9.4 combined ratio points compared to 2.2 combined ratio points in the fourth quarter of 2019. The losses impacted both our insurance and reinsurance segments, primarily as a result of a series of natural catastrophes in the quarter, including Hurricanes Delta and Zeta and other smaller events, as well as adjustments to our estimates for events that occurred earlier in 2020.

Our best estimate of ultimate losses for COVID-19, for occurrences through December 31, remain essentially unchanged from prior estimates. As of December 31, the vast majority of our COVID-19 claims are yet to be settled or paid, with approximately 2/3 of the inception-to-date incurred loss amount recorded as incurred but not reported, IBNR, reserves or as additional case reserves within our insurance and reinsurance segments.

As regards the potential impact of COVID-19 on our mortgage segment, as Marc alluded to, the delinquency rate at the end of the quarter was 4.19%, down from 4.69% at September 30. We are encouraged with the downward trend in delinquency rates over the last few quarters, which continue to come in significantly better than our earlier forecasts. Our latest assessment of this situation assumes a progressively improving economy in 2021, which should bode well for the housing sector and the performance of our book as we move forward.

In the insurance segment, net written premium grew 21.6% over the same quarter 1 year ago, 29.6% if we exclude the impact of the pandemic on our travel, accident and health unit. The insurance segment's accident quarter combined ratio, excluding cats, was 93.6%, lower by 800 basis points over the same period 1 year ago.

Approximately 360 basis points of the difference is due to our lower expense ratio, primarily from the growth in the premium base from 1 year ago and continued lower levels of travel and entertainment expenses. The lower ex cat accident quarter loss ratio reflects the benefits of rate increases achieved over the last 12 months and changes in our mix of business. Prior period net loss reserve development, net of related adjustments, was favorable at $1.2 million.

As for our reinsurance operations, we had strong growth of 44.9% in net written premiums on a year-over-year basis, which was observed across most of our lines and includes a combination of new business opportunities, rate increases and the integration of the Barbican reinsurance business. The segment's accident quarter combined ratio, excluding cats, stood at 82.1% compared to 92.3% on the same basis 1 year ago. The year-over-year movement is primarily driven by rate change activity over the last 12 months and a more normal level of large attritional losses compared to a year ago.

Most of the remaining difference is explained by operating expense ratio improvements, primarily resulting from the growth in earned premium. Favorable prior period net loss reserve development, net of related adjustments, was $40.5 million or 6.9 combined ratio points compared to 4.9 combined ratio points in the fourth quarter of 2019. The development was mostly in short-tail lines.

The mortgage industry had a second consecutive record-breaking quarter in terms of mortgage originations, which allowed Arch MI to produce $38 billion of NIW in the fourth quarter, a full 15.9% higher than our prior high watermark. With refinance activity leveling off from prior peaks, we saw our insurance in force increase by 2.5% across the mortgage segment.

The combined ratio was 45.1%, reflecting the lower level of new delinquencies reporting during the quarter. The expense ratio was slightly lower over the same quarter over 1 year ago. And prior period net loss reserve development was favorable at $8.2 million this quarter, mostly from our second-lien runoff portfolios.

Improving investor sentiment enabled Arch to issue 2 Bellemeade transactions during the fourth quarter at terms that are getting closer to pre-pandemic levels. You will recall that we discussed our 2020-3 transaction on the last call, an on-the-run deal covering our production from June through August of 2020.

Our latest transaction, Bellemeade 2020-4, provides additional protection on mortgages we insured in the second half of 2019 and already covered by our 2020-1 Bellemeade transaction by effectively reducing the original retention from 7.5% to 1.85% of the risk in force. At year-end, the Bellemeade structure has provided approximately $4 billion of aggregate reinsurance coverage.

Total investment return for the quarter was positive 246 basis points on a U.S. dollar basis, and we ended the year with our investment portfolio producing a 7.77% total return. While our fixed income portfolio generated an excellent return of 188 bps in the quarter, contributions from our equity and alternative investments were also significant and represented approximately 40% of the total return for the quarter. The duration of our investment portfolio decreased modestly to 3.01 years at year-end, reflecting our ongoing positioning of the portfolio towards shorter-term maturities.

The effective tax rate on pretax operating income was 6.8% in the quarter, reflecting changes in the full year estimated tax rate, the geographic mix of our pretax income and a benefit from discrete tax items in the quarter. We currently estimate the full year tax rate to be in the 10% to 12% range for 2021.

Turning briefly to risk management. Our natural cat PML on a net basis decreased slightly to $860 million as of January 1, which, at approximately 7.4% of tangible common equity, remains well below our internal limits at the single event 1-in-250-year return level. The decrease in our peak zone PML this quarter is mostly attributable to our E&S property unit within the insurance segment, where we reduced property aggregate in the Florida tri-county peak zone and made selective additions to our reinsurance purchases.

Our balance sheet remains strong, and our debt to -- plus preferred leverage ratio stood at 22.1% at year-end, well within a reasonable range. Finally, on the capital front. We repurchased approximately 251,000 shares at an aggregate cost of $8 million in the fourth quarter of 2020. It is worth noting that we have since repurchased an additional 2.6 million shares at an aggregate cost of $83.6 million in the first quarter of 2021 under a Rule 10b-5 plan that we implemented during this quarter's closed window period. Our remaining share purchase authorization currently stands at $833 million.
With these introductory comments, we are now prepared to take your questions.

Question and Answer

Operator

[Operator Instructions] Your first question comes from Elyse Greenspan with Wells Fargo.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

My first question is on -- related to your returns. Marc, I think in the prepared remarks, you associated with mortgage business going back to return on capital levels from 2018. And I'm hoping, just for all 3 businesses, insurance, reinsurance and mortgage, can you give us a sense of the return profile of the business you're writing today versus what you would have said if I had asked the same question 12 months ago?

Marc Grandisson
CEO & Director

Yes. I think the -- well, nice talking to you, Elyse. I think the high level of 2018 sort of long-term expected return on the MI was roughly in the mid-teens. So we're now going back to that level, which is a really good place for us to be. On the insurance, I think that we had a bit of a decrease in expected returns, even though the combined ratio did not get that much better for the industry.

But right now, if you factor in all the rate changes and everything, we think we're in the double digit in insurance return. And we think that reinsurance is a little bit in between those 2. So we have a really, really different risk return -- risk-adjusted return profile on our portfolio. That has improved and largely as a result of the price increase, naturally as a result of the investment return, as you know, Elyse.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Yes. And then my second question on -- I think you alluded to this a little bit in your prepared remarks, Marc, when you were mentioning a few issues that would help from the pricing momentum side, like persisting from here. A big question that I get is, does this momentum persist through 2021 and perhaps beyond?

And can you -- obviously, different dynamics in the insurance and reinsurance P&C markets. But can you just give us a sense, based off of what you know today, do you think that the pricing momentum can persist through 2021 in insurance and also reinsurance?

Marc Grandisson
CEO & Director

We expect it to be the case, Elyse, because of all the factors I mentioned, the social inflation. There's a lot of uncertainty in terms of loss ratio peaks, 4 years, specifically 2015 through '19, as we all know. It sort of makes for correcting some of the ongoing pricing. So that's definitely sustainable. We do not have as much protection from the investment returns, so that really puts a lot of pressure on the returns for the industry.

On uncertainty and lack of, if you will, coverage, we also had a fair amount of cat losses in the last 3 or 4 years. So there's a lot going on, a lot more risk out there. So I think, overall, collectively, as an industry, we all collectively think and know and believe that we need to get better rate and better pricing because the risk is not being rewarded accordingly.

As in every hardening market, the length is like how long is the piece of string, but I think that our hardening market does not only last 4 or 5 quarters. I think that you have this initial stages of the initial reaction of rate increases, then you get momentum building in the underwriters' mentality.

The brokers are sort of accepting as being sort of a new way to deal and do the business. And eventually, that builds upon itself. I would fully expect to be lasting to 2021 and into 2022. This is what we believe at this point in time.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Okay. And one last numbers question. You guys mentioned the PML going up a little bit. But in terms of your cat load, I think in the past, Arch used to talk to like a $40 million of quarterly cats. Obviously, we've seen growth in cat reinsurance and other property-related lines, like you mentioned. How should we think about the cat load from here?

François Morin
Executive VP, CFO & Treasurer

Yes. I mean, no question that we've written a lot more property premium in the last, I want to say, 4 to 6 quarters, we've really ramped up our property exposures. I mean there's a lot of -- in different areas, as you know, different lines of business, U.S., international, et cetera.

Yes. So the cat load, I think, on a quarterly basis, has definitely gone up from what we were in the old days, thinking about like $40 million a quarter. It's still evolving, but I would say it's probably more in the $60 million to $70 million range right now.

Operator

Our next question comes from Mike Zaremski with Crédit Suisse.

Michael David Zaremski
Crédit Suisse AG, Research Division

Follow-up on mortgage insurance and Elyse's question. If you're talking about kind of you're encouraged about the downward delinquency rates and assuming the economy progressively improves, I mean, I think you mentioned mortgage biz can throw off returns similar to 2018 levels. So are you saying kind of directionally we should be thinking about a combined ratio that continues to move south like kind of towards 2019 levels? Or have the capital assumptions changed since then?

Marc Grandisson
CEO & Director

Mike, in terms of the combined ratio, the capital is a different story because it's a bit of a lagging indicator based on the delinquencies we have. But if you look at the combined ratio, yes, we think that we're tending to go towards more -- so the run rate that we had in 2018. And we just caveat that there was some prior development -- favorable development in 2018. So I will probably adjust for that.

But certainly, the long-term range of 35% to 45% is not something that is out of the realm of real possibility if you look at 2018. And I think depending on what -- how the economy recovers, that could be in the lower end of that. And it's a couple of things to develop in a different direction. It might be a little bit on the higher side. But you're right, it should be getting closer to where we were in 2018 in terms of combined ratio.

Michael David Zaremski
Crédit Suisse AG, Research Division

Okay. That's helpful. Switching gears to the non-MI insurance segments. You've been -- the expense ratio has been better than expected for a number of quarters. I know you guys have called out some items. Maybe you can kind of remind us and talk to kind of what's -- what you think is kind of cyclical? And what's kind of structural in terms of the expense ratio improvements?

Marc Grandisson
CEO & Director

Yes. I think this is more structural, I would say, Mike, because right now, you have to factor in the fact that our platform grew on both sides, both in the sense of growing the top line for -- in our organic lines of business. And we also had the acquisition in London, and really pushed to be much more relevant, much more bigger in London. So our international operations also gained scale.

So if you now look at the overall structure or the way the company is laid out in terms of top line and the way the expenses is constructed between the units, I think it's much more of a structural change. I would say that it's probably 50-50, but the growth is certainly something that's really important in terms of helping that growth. So that could also get presumably a bit better over time.

But I would also tell you that the growth in our operating expense on the insurance side has lagged the growth in our top line, which is what we should expect, right, because a lot of the increase is not more work, even though we are writing more business. A lot of the increase in premium is just rate in and of itself. So I think that the company is flexing itself in terms of top line growth and expense deployment very, very nicely. So a bit more structural than I would have told you probably 2 years ago.

Operator

Our next question comes from Yaron Kinar with Goldman Sachs.

Yaron Joseph Kinar
Goldman Sachs Group, Inc., Research Division

I guess my first question revolves around MI. Do you have any comments or thoughts around the potential changes of FHA fees and its potential -- and what their potential impact on the MI business?

Marc Grandisson
CEO & Director

Yes. I can -- listen, it's still early on. It's a new administration change. There's a couple of things going on all over the place. Washington, I'm sure, they're very busy right now trying to -- changing things.

We hear the same things that you guys hear about the 25 bps potential price cut that FHA could put in there. And as a reminder for everyone, if you take a step back, the FHA was a large market share provider of MI insurance in the years where the PMI, the private mortgage insurers, were not in that great of a shape. And frankly, that was needed to fill the gap and fill the board, if you will, of the need for -- of the homeowners and the mortgage provider.

So this has changed. I think that the FHA's also ultimate role and core role is to provide mortgage insurance for the ones -- those that are probably -- could be perceived a bit more risky for the private sector. And so we've done the analysis, which means that, if you look at our portfolio, Yaron, we're high FICO, very high-quality. Most of our -- the borrowers that we have on our portfolio do not really need to consider FHA.

So from our perspective, we'll react, obviously, to whatever is out there. But we believe that this -- if it comes to fruition, that 25 bps rate cut in FHA will help in the lower-FICO and higher-LTV borrower, which is really not the ones affecting and the ones that we are currently having success with because our pricing is actually better. If you compare our pricing versus the FHA in that sector, our pricing is better and execution is cheaper for the borrowers. So we're not losing sleep over that.

Yaron Joseph Kinar
Goldman Sachs Group, Inc., Research Division

Got it. That's helpful. And then my second question, you previously talked, I think, about shifting capital deployment from MI more into P&C. I think last call, you used more of a basketball analogy that was easier for me to follow than hockey, but thank you for explaining.

But I guess, as market conditions kind of -- your views on market conditions change a bit, it seems like reinsurance may be a little less exciting than maybe a quarter or 2 -- the outlook was a quarter or 2 ago, and MI maybe a little better than the outlook was a quarter or 2 ago. Does your appetite for capital deployment between the 3 segments, has that shifted? Or will it shift into 2021?

François Morin
Executive VP, CFO & Treasurer

I wouldn't say it shifts in any major way. I think we see all 3 segments with very good opportunities in front of them. And maybe we'd argue some were overdue, especially on the P&C side. So we're bullish there. Mortgage has always been, in basketball, a 7-foot-6 guy down low and ready for dunks, and that hasn't really changed in our view.

So yes, I mean, we got -- certainly have more visibility into what the ultimate or what the current market conditions are especially in mortgage, given what we know the second half of the year, how things progressed. And that's good. I mean that's something that we take -- I think it works in our favor. So -- but in a big picture, we don't see major changes in how we deploy capital.

Marc Grandisson
CEO & Director

And Yaron, one thing I would mention to you that have -- it's always -- it's hard for people not to see us being a Bermuda, as being a property cat writer on the reinsurance side. But I would argue that, yes, the property cat side is not as good, and you've heard it from other people, and we certainly agree with that.

But we're still growing in areas that are nonproperty cat, right, exposed. So we're seeing a lot of other lines, to be honest, between you and I, that are actually better now or the prospects that we want better than they were in 2020. It's just that if we're not growing necessarily in the one that gets the better headline, if you will, from your perspective. But by and large, I think there are prospects that sits very, very long on the reinsurance side, very much so.

Operator

Our next question comes from Jimmy Bhullar with JPMorgan.

Jamminder Singh Bhullar
JPMorgan Chase & Co, Research Division

I had a couple of questions. First, if you could just talk about your sort of comfort level with your BI reserves, given that the developments in the U.S. seem to be favoring the industry for the most part. So do you feel like you're overly conservative on your reserves? And obviously, internationally, things haven't gone as well. And then I had another one as well.

François Morin
Executive VP, CFO & Treasurer

Yes. I think we're -- we never would say that we're overly conservative. We want to be prudent and conservative for sure in how we set reserves. I'd say, starting with international, which maybe has gotten a bit more headlight -- made the headlines a bit more -- our position hasn't changed in the U.K. Again, the book we have is a small regional book, well protected by reinsurance protection. So we feel that the reserves we have there, even after the, call it, slightly adverse rulings from the courts in the U.K. were -- aren't going to affect our bottom line. So we're -- no changes from our point of view there.

And in the U.S., for the most part, as you said, all the rulings have kind of been in favor of the industry, a couple of places where there's maybe some that didn't go as expected. But on those, our view is that the policies that were being challenged were manuscript policies, so not the standard ISO form that we typically use without necessarily the strong wording around virus exclusions and property damage to trigger coverage.

So on both those fronts, we got, as we said before, the vast majority of our policies, well north of 90% across the book, that has these -- both of these, call it, protections. So we're very confident that our results -- our reserves at this point won't develop adversely, and we're -- we will keep looking at it. But it's -- we're in a good spot.

Jamminder Singh Bhullar
JPMorgan Chase & Co, Research Division

And I think you said about 2/3 or 3/4 were IBNR as of last quarter. What's that number now?

François Morin
Executive VP, CFO & Treasurer

2/3. It went down a little bit. So we said, roughly -- from 75% to 67%, roughly. I mean it hasn't changed much. And it's -- so -- and some of that is around, as you can expect, mostly on the reinsurance side, right, where we -- a lot of our reserves are still on the reinsurance side, with significant IBNR and ACRs on that book.

Jamminder Singh Bhullar
JPMorgan Chase & Co, Research Division

And then on buybacks, you did a decent amount in -- you've done a lot of this year. So what's driving your sort of action there? Is it the stock price? Is it -- I'm assuming there's a decent opportunity to deploy capital in your businesses given pricing. But what drove the big uptick in buybacks versus what you've done in the last few quarters?

François Morin

Executive VP, CFO & Treasurer

Yes. It's certainly more visibility, right? I think that we said that from the start, we -- at the end of the first quarter last year, we said, listen, we're going to take a little bit of a pause because we need to know where things are going to -- how things are going to play out. And mortgage being a major driver in that performance, you've seen the results. So we were a lot more confident where the economy is going. Vaccines are rolling out. So there's a lot of things that, yes, will take some time.

But as we look forward, I think that gives us a lot more comfort that the worst is behind us, and that gives us more clarity on how do we deploy capital. We're still -- and in our mind, we're fully capable of doing both. We want to grow the book and also buy back shares. There's no reason why they have to be exclusive.

We think our growth is still very strong. We expect to keep growing in '21 across the book. But we also see a good opportunity at the current level of -- pricing levels for the stock to buy back at this point.

Marc Grandisson
CEO & Director

So before we go to the next one, I think I have to stop the broadcast. I think I believe we have a breaking news just hit the wire. So I think we have to go to François for some commentary that you want to share with us. François?

François Morin
Executive VP, CFO & Treasurer

Yes. That's long overdue, Marc, but just wanted to take advantage of the opportunity to fill everybody on the call on the latest developments with our proposed acquisition of a 29.5% ownership stake in Coface, the global trade credit insurer, to confirm what some of you may have seen across the Business Wire over the last few minutes.

They weren't paying attention to what we were saying, but we closed on this transaction with Natixis earlier today. And the reason for the timing is that we had to wait for their markets to close, which they have. So the consideration paid by Arch was EUR 9.95 per share for an aggregate EUR 453 million in aggregate, including related fees. In connection with our minority stake in the company, Arch now has 4 representatives on the Coface Board of Directors. As we stated before, we continue to view this transaction as an investment, and we currently do not intend to increase our ownership position in Coface.

From a financial reporting perspective, you should all expect us to include our proportionate share of Coface's results in our financials starting next quarter. We intend to report the contribution in a new separate line titled Equity Method Earnings from Operating Affiliates, which will be included in our definition of operating earnings. This line will also include the contributions from other nonconsolidated affiliates such as Premia Holdings.

So that's the breaking news, Marc.

Marc Grandisson
CEO & Director

Thank you, François, for the update. And Liz, if we can go back to Mr. Dunn, who is waiting in line, I believe.

Operator

Geoff Dunn with Dowling & Partners.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

A couple of questions on MI. First of all, what was the incidence assumption for the current period provision as well as the average severity factor this quarter?

Marc Grandisson
CEO & Director

Yes. So 9.4% for the new annuities in the quarter, and the average reserve per DQ was a little bit over $5,000, pretty much in line with the third quarter, Geoff, because the risk that came in were a little bit less coverage in this quarter. So that would explain the average being a bit lower or a bit more in line.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

Okay. And so as you think about '20 -- or the first part of '21 there, to my knowledge, they extended the forbearance period out to 15 months, but you can't enter a new forbearance activity. So what did your provision for nonforbearance loans or your incidence assumption for nonforbearance loans look like in the fourth quarter?

Marc Grandisson
CEO & Director

Yes. I don't think -- we did not -- the way we reserve, yes, we sort of try to make an overall all-encompassing assessment and put that in that number. So I think that's what you might have said -- might have thought in the past that our number could have been a bit higher. So we think that we have enough in the reserving, in totality, based on the factors we've used.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

Okay. But with forbearance options going away, fair to assume that, that incidence assumption will probably climb in the first half?

Marc Grandisson
CEO & Director

Yes, Geoff, we might. We'll have to evaluate when we get there. I think you're right. I mean so we have until February 28 to actually ask for this for -- be under the forbearance program. So we'll see how that develops. We have a surge in a couple of weeks of people asking for forbearance. That might help, again, more. We'll have to readjust, Geoff, as we see at the end of the quarter. We'll have another month of nonforbearance, effective -- not new forbearance. So we'll have to reevaluate when we get there.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

Okay. And then within the P&L, can you talk a little bit about what drove the pretty notable sequential drop in earned premium as well as some of the movement on both the expense lines? Was there any reallocation on the expense stuff?

Marc Grandisson
CEO & Director

Specific to any segment or in gen -- I mean...

François Morin
Executive VP, CFO & Treasurer

In general.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

All in MI.

François Morin
Executive VP, CFO & Treasurer

All in MI, right, Geoff?

Marc Grandisson
CEO & Director

All MI? I...

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

Premium line was down $15 million sequentially. And then you had some -- just -- looks like a little bit of abnormal movement, particularly in the acquisition expense line relative to third quarter. But just a little bit more volatility than we would tend to see.

François Morin
Executive VP, CFO & Treasurer

Yes. The first one, I'd say, A, was a, call it, an accounting catch up or true-up on our Australian business, how we -- on the written side. So that -- I'd say that's more of a one-off kind of blip that we had to adjust for or it was -- actually, was present last quarter and wasn't this quarter. So that's how we -- the -- that explains that movement.

On the acquisition, there's -- we entered into a quota share agreement starting last -- at the middle of the year, covering our U.S. MI book. And that actually gives us a benefit in terms of the acquisition. It's a reduction to the acquisition in terms of the ceding commission. So that is what is starting to flow through in our numbers. Yes.

Operator

Our next question comes from Phil Stefano with Deutsche Bank.

Philip Michael Stefano
Deutsche Bank AG, Research Division

Just continuing the MI questions, I guess. So you had mentioned that roughly 2/3 of the defaults are in forbearance. I was hoping you could give us a flavor for how many people are nearing the end of their forbearance window, and how many people in forbearance does it feel like are current on their mortgages?

Marc Grandisson
CEO & Director

Yes. So -- yes, the numbers we report to you are those that are in forbearance and then have skipped 2 payments, at least. So we have a few more, as you could appreciate, that are in forbearance and are still current. The data is coming in very, very haphazardly. So it's very -- I wish -- we are constantly asking and prodding for that kind of information.

I think that most of the forbearance that are still there are lower in the year. Most of the forbearance that were declared early in April, May, June, the vast majority of them are secured by now. So it seems to be the pattern of getting to forbearance and sort of staying in there for 5 -- 4, 5 months and then, eventually, things get back to normalcy. So that's what we would expect it to be the case going forward. So I don't have a definite answer to you. Yes, go ahead.

Philip Michael Stefano
Deutsche Bank AG, Research Division

No, no, no. That's -- so I think the 1 question that we're trying to get to, and I get a lot of questions about is, you had mentioned 89% of the delinquents have at least 10% in equity in the home. And you had talked about visibility allowing you to repurchase shares. I mean at what point do we get visibility that maybe the MI reserves are a little more redundant, and we can start to see a relief there? I mean how do we think about what you're looking for in the visibility to adjust that?

Marc Grandisson
CEO & Director

So from your [indiscernible] here, I hope you're right that it's going to be redundant. We'll see. Only time will tell for us. I think the way we look at reserve, Phil, is very simple. It's just -- we have to wait till we get the data that we feel confident that we're going to get there. And as you know, you've seen us do the reserving on MI and P&C for a long time.

You tell me when the forbearance program is done and when the unemployment rate goes down to 3 or 4 and the economy picks up again, then I'll have a better sense for what it is. So we hope -- but all -- having said all this, I have hope that by the summer, after the vaccines have been rolled out, that we'll have much, much, much better visibility as to what, if any, the reserve needs to be released, or it's not necessary to pick claims.

Philip Michael Stefano
Deutsche Bank AG, Research Division

Understood. Okay. And switching gears. On the reinsurance business, I appreciate the remarks you made in response to an earlier question. Is there any way you can help frame for us what the opportunity is for premium volume. So maybe it's -- how the 1/1s go versus last year? Or how should we be thinking about the growth potential in 2021?

Marc Grandisson
CEO & Director

I think the growth in 2021 should be more in line, at least, with what we were in last year. I think the opportunities on the reinsurance side -- oh, I have an echo here.

I think the reinsurance opportunities are still very, very solid, very strong. They're not necessarily, as I mentioned earlier, in a traditional property kind of re, but we're definitely, definitely looking at a lot of transactions. And a lot of them will have to do with what you would expect a reinsurance company to be providing, which is capital, as we get into a harder market, right?

And a lot of people are -- some of clients are looking for capital or at least looking for validation of their plan going forward and want to make sure that they re-underwrite and we repurpose their book of business, that we're there to help them, and we're able, in that case, to help them get through that transition period. So the opportunity in reinsurance was great last year. And I think it's actually very, very good.

Again, as we go this year, one interesting fact for everyone that one of the key leading indicator to us, to me, at least, personally, based on my history as to what is a leading indicator of the treaty reinsurance conditions are -- the facultative industry is still really, really strong. And it's typically -- you typically have a hard market or a hardening market.

For as long as a fac market goes, you'll have a treaty market staying strong, well beyond that -- a year to 2 years beyond that. So we expect that to be, yet again, a strong leading indicator. And we -- our facultative team is telling us that it's a really good market for them at this point in time, which is encouraging.

Operator

Our next question comes from Meyer Shields with KBW.

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

So 2 questions on the P&C side. First, Arch's confidence in the pricing cycle has clearly borne itself out. But is it safe to say that maybe this is as good as it gets on the property cat side because there is this level of capital available, so that cycle won't play out along historical lines?

Marc Grandisson
CEO & Director

Yes. All I will tell you, Meyer, is my experience. We did a lot of property cat writing in '01, '02. And if you remember, at Arch, we were not heavily focused on property cat XOL at the time. We're more on the liability side, and the market was going down in '04, well into '05. And we thought we had seen the last of the hard market for a little while, and Katrina was the reason why it happened. It changed the whole thing.

So my question to you -- my answer to you is I don't know. I don't know is the short answer. I think that there's clearly a lot of capital that, again, found its way over the last 4 or 5 years. And once capital fund is going to a niche, it gets sticky, right? It wants to stay there for a while and will sort of justify itself for a little while longer perhaps than it should. But I think we're always -- hopefully, it doesn't happen. But we could be 1 major event away from changing the perception of risk in that area.

And that, I think, will mean actually probably a much harder market that you would expect, Meyer, because the volatility and the knee-jerk reaction would be like an elastic, right, when this happens. I think you'll have a -- you may have a massive exit of capital out of the door, and that might create more opportunities for us. I'm not saying it will happen, Meyer, but I could see a scenario where your premise does not actually hold true. So there's always a chance.

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

Okay. No, I just wanted to sort of understand what you're thinking about. Second, you talked, I think, on the insurance segment about market dislocation. And I think maybe the sense is out there that, that has been a major factor or was a major factor in 2020, but now most companies are kind of settling down and are comfortable with their books of business. Are you still seeing like, today, that level of market dislocation?

Marc Grandisson
CEO & Director

Dislocation is -- you're right, there's some realignment. There's a couple of people going back to the market. This is truly happening, but it's not across the board. And there are still, we believe, bad news that needs to come find their way through the system, and that might make somewhat of a difference as we go forward.

But again, if you had a 20% rate increase on 1 transaction on the interim side this year, and you had -- this is on top of a 10% last year. If you get rate on rate on rate perhaps 3x, it's not a bad place to be. And plus, I think what we hear, Meyer, for what it's worth, and it's actually not insignificant, we're hearing terms and conditions finally changing and moving in the right direction.

So rates will move first, and terms and conditions sort of follow right behind. And we're hearing that this is what's happening in the marketplace. So even though we may not have a headline growing as high in terms of rate change as much as it was over the last 2, 3 years, I think the underlying conditions in their policies could actually help improve it way beyond the number that we see on the headline number.

Operator

Our next question comes from Brian Meredith with UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

A couple of them for you here. The first one, Marc, first, I wonder if you could just confirm. It used to be that your determination on whether you buy back your stock or not is that if you could actually recoup the premium you paid relative to book value over a 3-year period. Is that still the case? And if it is, does that basically mean that you could -- you'll continue to be pretty aggressive with your share buyback, given where your stock is trading right now?

François Morin
Executive VP, CFO & Treasurer

Yes. I think that rule of thumb is still in place. I mean, obviously, it's not a black and white. I mean there's always factors we consider around deploying, whether there's business opportunities, and et cetera. But yes, we still think in those terms of the buyback, the premium we bake and that we want to earn it back over -- no more than 3 years.

And you're right, I mean, I think the fact that the price -- the stock price is not as -- is below that level, suggest that maybe we'll be out there buying more stock as we go through the year. We'll assess, obviously, as we -- every day, every quarter, we will look at what's in front of us. But for the time being, I think we're -- certainly, it's something we're considering, and we probably will do more of.

Brian Robert Meredith
UBS Investment Bank, Research Division

Got you. And then just on that topic. So just maybe a little bit on uses of capital or cash kind of here going forward in the next 12 months. It sounds like you've got $453 million that's going out here. We've got Watford that I think is yet -- you get to close. Is that at all going to be to constraining your ability to actually buy back stock, given the -- also, the capital you need to fund your growth in your business, and particularly what Marc just said on the reinsurance business, is going to be capital kind of generated-type transactions?

François Morin
Executive VP, CFO & Treasurer

No. Because we -- I mean, we raised $1 billion of capital, as you know, last summer. We didn't deploy it fully until -- right, it was all part of that kind of 1/1, looking ahead as to what the 1/1 would do. We know these transactions were on the horizon. And we have a lot of faith in our ability to generate earnings moving forward on our -- I mean -- so self-funding the growth, I think, is something that is part of the plan, and we don't really have a whole lot of constraints other than that.

Marc Grandisson
CEO & Director

And Brian, both these acquisitions that you mentioned will actually be accretive and grow book value for us. So they're capital positive for us.

Brian Robert Meredith
UBS Investment Bank, Research Division

Got you. That makes sense. And then last question, I guess, just now that you've disclosed Coface, maybe you can give us a little bit of color on what the title insurance market looks like in Europe kind of return profile. What should we expect here?

François Morin
Executive VP, CFO & Treasurer

It's been about, what, 20 minutes that we announced this, so you're going to have to give me a couple more quarters.

Brian Robert Meredith
UBS Investment Bank, Research Division

I think [what you gave us] is challenging.

Marc Grandisson
CEO & Director

No, we have it. But listen, we're going to think it through. We are going to have directors on there that are going to be working very closely hand-in-hand with Coface. And we're very excited, as you know, Brian. I think there's more than meets the eye in this one. I think, strategically, it's going to be a very, very valuable thing for us, way beyond just the initial investment. I think it's a formidable established company across so many countries with so many client contacts. We're really excited about that.

Operator

I'm not showing any further questions. I would now like to turn the conference over to Mr. Marc Grandisson for closing remarks.

Marc Grandisson
CEO & Director

Thank you very much, everyone. Have a next -- a nice several months ahead for the -- ahead of the first quarter returns. It's an exciting time to be at Arch, and we're very pleased that you are there with us to enjoy. Thank you.

Operator
Ladies and gentlemen, thank you for participating in today's conference. This concludes the program. You may all disconnect.