S&P Capital IQ

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W. R. Berkley Corporation NYSE:WRB

FQ2 2015 Earnings Call Transcripts

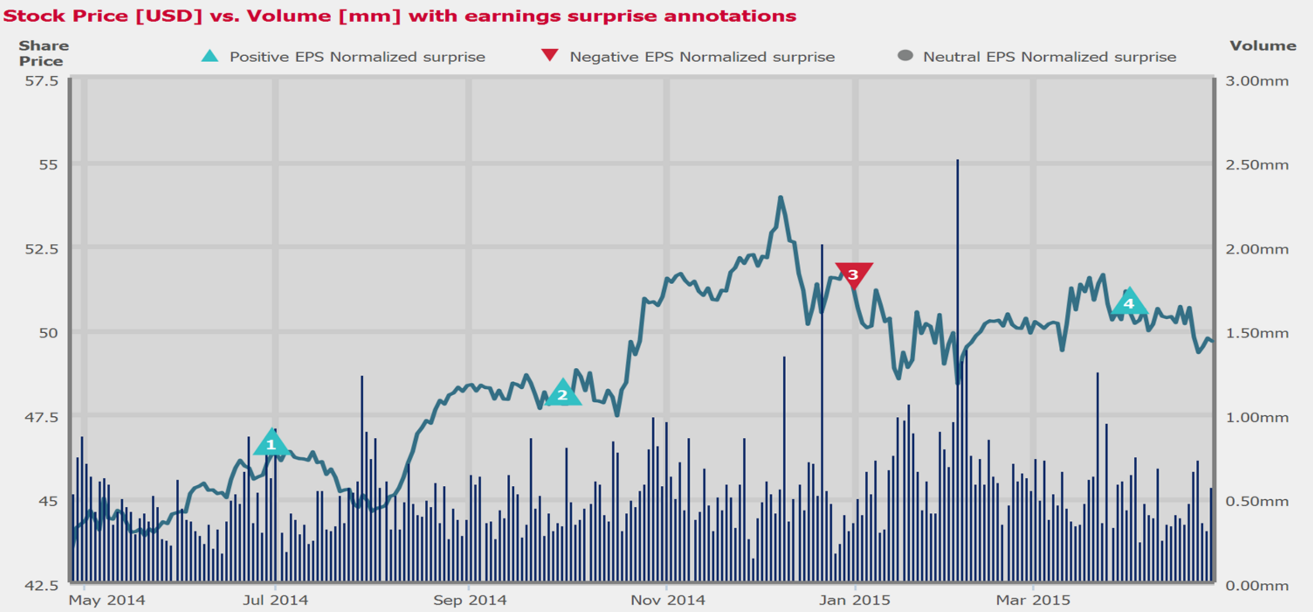
Monday, July 27, 2015 9:00 PM GMT

S&P Capital IQ Estimates

	-FQ2 2015-			-FQ3 2015-	-FY 2015-	-FY 2016-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.80	0.81	▲1.25	0.87	3.44	3.75
Revenue (mm)	1789.00	1789.76	▲0.04	1815.40	7206.20	7973.78

Currency: USD

Consensus as of Jul-27-2015 9:18 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2014	0.76	0.82	▲7.89 %
FQ3 2014	0.90	1.06	▲17.78 %
FQ4 2014	0.82	0.73	▼(10.98 %)
FQ1 2015	0.75	0.80	▲6.67 %

Call Participants

EXECUTIVES

Eugene G. Ballard
Executive Vice President of Finance

William Robert Berkley
Founder and Executive Chairman

William Robert Berkley
Chief Executive Officer, President and Director

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RBC Capital Markets, LLC, Research Division

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Ryan James Tunis
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Presentation

Operator

Good day, and welcome to the W. R. Berkley Corporation Second Quarter 2015 Earnings Conference Call. Today's conference is being recorded. The speakers' remarks may contain forward-looking statements. Some of the forward-looking statements can be identified by the use of forward-looking words including, without limitation, believes, expects or estimates. We caution you that such forward-looking statements should not be regarded as a representation by us that the future plans, estimates or expectations contemplated by us will, in fact, be achieved. Please refer to our annual report on Form 10-K for the year ended December 31, 2014, and our other filings made with the SEC for a description of the business environment in which we operate and the important factors that may materially affect our results. W. R. Berkley Corporation is not under any obligation and expressly disclaims any such obligation to update or alter its forward-looking statements, whether as a result of new information, future events or otherwise.

I would now like to turn the call over to Mr. William R. Berkley. Please go ahead, sir.

William Robert Berkley
Founder and Executive Chairman

Thank you very much. Well, it was an interesting quarter, exciting in many ways, challenging in many ways. We're pleased with our results. And why don't I start by turning this over to Rob.

William Robert Berkley
Chief Executive Officer, President and Director

Okay. Thank you. Good afternoon, everyone. The second quarter, as suggested a moment ago, has been a period of significant change for the industry, but much of that change stemmed from the level of M&A activity that persisted through the quarter. Having said that, while it has given people something to talk about, the reality is that the underlying market conditions has been reasonably consistent, though, in some cases, perhaps incrementally more competitive.

On the markets that we participate in, the domestic insurance market remains the bright spot. Workers' comp, GL, as well as select parts of the professional market remained particularly attractive. Having said that, unfortunately, commercial auto, aviation and marine remain challenging and, more recently, offshore energy has become notably competitive.

As it relates to the international insurance environment that we operate in, it remains also quite competitive, with the U.K. and Europe standing out as particularly challenging.

And finally, the global reinsurance market, it remains painfully competitive as well. Having said that, the pace of erosion seems to be slowing, which has given reason for, perhaps, the guarded optimism that we are approaching the bottom.

Turning to the company's performance during the period. Net written premium came in at $1.54 billion, that is up about 3.5% when compared with the corresponding period last year. The domestic segment led the growth, coming in up 7%. The growth was primarily driven within the domestic segment by our workers' compensation activities as well as parts of our professional liability activity. It's worth commenting that of the 7 points of growth, just shy of 2 points were associated with rate, and the renewal retention ratio remained at approaching 80%.

Partially offsetting this growth was the international segment, which was down 11%. Eugene's going to be giving you a bit more detail on that, as well as the reinsurance segment, which was approximately flat.

With regards to the loss ratio, it came in at 60.7, which is an improvement of approximately 0.5 points. And this was primarily driven by improvements in the reinsurance segment as well as a bit of improvement coming from the international segment. It's also worth noting that our paid loss ratio came in at an attractive 53%. With regard to the expense ratio, this was a little bit of a bittersweet situation.

The expense ratio did tick up to a 33.5. We are pleased with the continued improvement in its domestic segment. Having said that, this was offset by some activities in the international segment as well as the reinsurance segment. Eugene's going to also be giving you some numbers in this area. Having said that, a couple of quick comments from me. As far as international goes, as I've mentioned in the past, we're going to need, on occasion, take 1 step back in order to take 2 steps forward. Some of the expenses spike that we saw in the second quarter in the international segment, we believe, is a short-term phenomenon, which will spill over into the third quarter we would anticipate and may, in fact, affect the fourth quarter. But by the time we get to next year, we believe this will be behind us. And as it relates to the reinsurance segment, our internal cost is actually in a pretty good place and Gene's going to give you some color as to, again, what's driving that.

When you put it all together, the company achieved a 94.2 for the quarter, which included $22 million of net positive development. This is the 34th quarter in a row of net positive development. In spite of the challenges that exist in the international insurance market as well as the global reinsurance market, we believe that the domestic market still has a meaningful amount of gas in the tank. And quite frankly, the level of M&A activity is likely to create further opportunity, for example, as we've already announced a few new activities in the third quarter.

So all things being equal, we are quite optimistic as to where the domestic business is. We think things will, over time, be improving for the reinsurance segment. And we think we're well on our way to making meaningful progress with our international business. Thank you.

William Robert Berkley
Founder and Executive Chairman

Thanks, Rob. Gene, you want to pick it up?

Eugene G. Ballard
Executive Vice President of Finance

Okay. Thanks, Bill. Well, as Rob said, for the second quarter, we reported operating income of $105 million or $0.81 per share, which is almost unchanged from 190 -- $109 million or $0.82 per share a year ago. The slight decline in earnings was a result of higher underwriting profits that were offset by a modest decline in investment income. I'll go over the details -- some of those details starting with underwriting.

Again, as Rob said, net premiums written were up 3.5%. It was led by the domestic segment, which was up 7%, with increases in all major business lines. Our largest line, workers' comp, was up 15%, and professional liability was up 29%. In the international segment, premiums declined 11% to $198 million. Most of that decline was due to changes from foreign exchange rates. In original currency terms, international premiums were down 3% as growth in South America and Canada was offset by lower premiums in the U.K. and Continental Europe. And reinsurance premiums were essentially unchanged, $143 million, as growth in the U.S. was offset by lower premiums in Asia and Europe.

Our overall pretax underwriting profits were up 9% to $87 million. The accident year loss ratio of 4 catastrophe losses was a 60.5, up slightly from 60.1 in the second quarter of 2014 and below the accident year loss ratios for each of the immediately preceding 3 quarters. Cat losses were relatively benign for our second quarter with only 1 cat event with a net loss greater than $5 million. Overall, our cat losses were $25 million or 1.6 loss ratio point in the quarter, and that's down from $40 million or 2.8 loss ratio point a year ago.

We reported favorable reserve development of $22 million this year compared to $24 million a year ago. Almost all of that favorable development was from the domestic segment, but all 3 segments did have positive development. That gives us the reported loss ratio after cats and reserve releases of 60.7, down 0.5 points from last year.

The overall expense ratio for the second quarter was 33.5, up 0.3 points from the second quarter. The domestic segment improved -- expense ratio improved by 0.8 point to 31.5. That's right in line with our expectations. On the other hand, the reinsurance expense ratio increased 7 points. However, 5 of those points was due to what we call structured transaction, which are transactions that have much higher profit commissions that's more than offset by lower loss ratios. In fact, the internal expenses for the reinsurance segment other than commission was actually down 0.8 point from the second quarter of 2014.

The international expense ratio increased almost 3 points to 41.6 for 2 main reasons. One is the decline in premium I mentioned, and the other is slightly elevated cost in Europe that are related to the integration of our U.K. companies as well as the setting up a new European platform and to some ongoing Solvency II cost. We expect those cost to subside in early 2016. That gives us an overall combined ratio of 94.2, down 0.2 of a point from the second quarter of '14. As Rob said, the paid loss ratio was 53.0, down from 56 in the second quarter of '14, and our loss reserves increased to $250 million from the beginning of the year to just over $10.6 billion.

Investment income was $128 million, that's down $11 million from a year ago. The decline was primarily related to lower earnings from our merger arbitrage account, which broke even in the quarter compared with income of $7 million in last year's second quarter.

Earnings from fixed income securities were down $2 million to $107 million, and earnings from investment funds were unchanged at $22 million. The overall portfolio yield was 3.2% compared to 3.6% in the second quarter of '14.

In addition, we had realized gains of $28 million in the quarter, that's primarily from the sale of interest in investment funds. And that compares with realized gains of $109 million in 2014, which included a large gain from the sale of a real estate investment in the U.K.

At June 30, 2015, our average rating and duration of fixed income portfolio were AA- and 3.3 years. And our aggregate unrealized investment gains before taxes were $343 million. The duration of the portfolio of 3.3 years is a full year less than the duration of our loss reserves. Interest expense for the quarter was up $3 million. That's due to interest on $350 million of debentures that we issued in the third quarter of last year, which was partially offset by a reduction in interest from $252 million of senior notes that we repaid in May of this year. The overall effective tax rate was 34 -- 30.4% down from 31.5% in the second quarter of 2014. The decline was mainly due to lower investment gains that are generally taxed at the full 35% tax rate.

In the first quarter of 2015, we repurchased 4.4 million shares of our stock at an aggregate cost of $218 million. Our cash flow more than doubled to $272 million in the quarter due in part to lower tax payments. And in summary, for the quarter, that gave us a pretax ROE of 15.5%, an after-tax ROE of 10.7%, and an ending book value per share of $36.76.

William Robert Berkley
Founder and Executive Chairman

Thank you, Gene. So I thought I'd talk a little more about our strategies and some of the things that I think reflect upon our longer-term view and what we're looking at, and then open it up for questions.

So first of all, we think management of capital is really a cornerstone issue. We bought a lot of stock back. We look at our book value in the sense of what we assess as our real book value. So for instance, as we've mentioned in the footnote, we have a $400 million gain that's not reflected on our balance sheet in HealthEquity. That's a couple of dollars aftertax per share not reflected. There are a number of other assets that we think more judgmentally, but are undervalued on our balance sheet, some of our real estate, some of our other key investments.

So we think that our real book value is probably, because of things like that, not reflective of our balance sheet stated book value because we follow accounting rules. That's the way it is.

We're also optimistic that our business continues to generate an outstanding pretax return. We are cursed with being a domestic insurance company. So you might look at other people who report return on capital, return of equity of 12%, 13%, 14%, it's a nontax return. So we're -- this quarter-end from now on, we're going to put in our pretax returns, so you can measure our results based on management's performance because we think that's what that shows. We're going to have to, over the long run, find a way to deal with this issue. Some of our competitors are likely to find ways that don't suit us, but there will be a way to find a solution.

We also think capital management reflects a different view that we have than many of our competitors, where they think getting bigger and having more permanent capital is a good solution. We think, if anything, capital markets are more opportunistic, more flexible. And there are things to do to have capital that's available to you. And therefore, maintaining ever-increasing permanent capital can be more like an anchor than a sail in the wind that helps you move ahead. So we're trying to maintain our level of capital, being sure we have enough always, so we're not rushing to shrink our capital base, but not build capital when we don't need it, when we can find other places to get it if we want it for short or long duration, and leverage the returns that we can deliver to our common shareholders.

We're really optimistic about where we see the business going. In the short term, it may be a bump or 2. The global economy has never been as uncertain in my recollection. Not that there's a huge crisis here, but there's lots of uncertainty. The spread between the duration of our bond portfolio and the duration of our liabilities is as great as it's ever been being a year because we're worried about inflation. We don't know what's around the corner, but we know it's out there given economic activities and economic policies. We have the same view of our loss reserves, you have to, at least, recognize what's going to happen. So while we're aggressive in seeking out opportunities, of finding great teams of people, we being willing to jump into something where we see an opportunity, we're cautious when we look at what can go wrong in the insurance business. We want great returns, but we don't want to take them at any price. We continue to feel that we'll be able to deliver on that high 15%-plus after-tax return over the long run while it may be bumpier in the short run to get there.
Okay. We're happy to take any questions.

Question and Answer

Operator

[Operator Instructions] Our first question comes from the line of Kai Pan of Morgan Stanley.

Kai Pan
Morgan Stanley, Research Division

Bill, the first question on your -- you gave a lot of sort of detail, your thoughts about capital. 2 issues there. One is for the tax issue, you've been a vocal critic of the offshore tax treatments and that it is an indication that you think the law will not change and you have to find a way to reduce the tax rate for W. R. Berkley shareholders?

William Robert Berkley
Founder and Executive Chairman

Well, I think that your return on capital serves 2 purposes. One, it tells you what your shareholders are getting to keep, but it also is a measure that people have evolved to use -- to tell how well a company is managed. So I thought it was important, and we discussed it here at great length, that we put the number up there so you can look at us compared to so many companies who pay no tax, so when you look at us, you don't say, "Hey, they earned 10.5% return on equity and this other company earned 13%, 14%, 15%." You have -- to measure management, you have to look at it in a consistent way. So we're putting the number up their first of all, so you can measure how we do compared to everyone else. I don't think they're going to pretend they pay taxes, so we have to pretend we don't. Number two, I think that, ultimately, the system of taxation in our country only can work when business done in the United States pays tax on a universal basis. Otherwise, everyone will find ways to do business here and move their incomes offshore. That is not how it works in the insurance business at the present time. So that being said, I think there will be someone, something done to address tax issues. But I have been an optimist for 5 years, and I have been wrong. Actually, it was more than 5 years, probably 7 years. But the fact is I've been wrong. And we're constantly looking at alternatives and how and what -- and how the world works. And I'm an optimist. I always think I will find a solution or the government will find a solution that makes the country work better. So no, I don't have an answer, but I'm working on it.

Kai Pan
Morgan Stanley, Research Division

Okay. Then, on your second point, on the capital optimization. It looks like you are probably presuming a more capital-light business model because of capital available in the marketplace on demand that you don't need to maintain a big buffer in terms of your capped balance sheet. Does it mean that you will be very active in buying back your own shares that you probably will not grow your shareholders' equity unless there is business need.

William Robert Berkley
Founder and Executive Chairman

I think what it means is just as now, for a couple of years, we've tried to maintain our capital level at roughly the same level because external capital is available at very low costs. Much lower cost than our average cost of capital. So we're not going to reduce our capital, but we also don't see that we're going to be able to grow our business at huge amounts. So if we can grow our business 5% or 7%, there's external capital that we can find ways of obtaining that amount of growth. If we can start to grow our business more, we're going to grow our internal capital more or get more permanently provided external capital. We have many people who talk to us about being our partners and doing things all the time.

Kai Pan
Morgan Stanley, Research Division

Okay. Lastly, on industry consolidation. Bill, you've been running the company for almost 5 decades. You have seen this play out before. What do you think about the current wave of consolidation? What do you think it would do for the industry? And particularly, what it will do to W. R. Berkley? Do you think yourself more as buyers or seller?

William Robert Berkley
Founder and Executive Chairman

First of all, on October 31, I will step down as Chief Executive, and Rob is going to take over. So it will be not 5 decades, but I'll be out at this box at that point, and he'll take care of it, then I'll be Chairman. And then, I get to harass everybody else. But the fact is I think consolidation serves a purpose. In the case of our business, regulators and regulatory pressures makes it important not to stay small. We're big enough that we can deal with it. We've always had the same view. We're here to do what's right for our shareholders. We'll always do what's right for our shareholders. But that being said, we can continue to generate great returns over the long run for our shareholders. And if somebody comes up and says, "Hey, we'd like to talk to you about something." We're always willing to talk. And if it's good for our shareholders, it's good for us. In the meantime, we're big enough that we think there's not much that we can't do. And if we can't do it ourselves, we have lots, as I said lots of people who come to us with billions of dollars of capital and offer to be our partners to do some other things. So I think that the consolidation that's happening now is frequently about management ego or management rewards and less amount -- less than it is about what you need to run your business. Now there are exceptions, because to be a global company and to do the business globally, scale is certainly of value. But that's a small part in dollars at the marketplace. So there are a few companies that need to be global to serve customers. Our global ambitions have to do with doing business with great customers wherever they're located.

Operator

And our next question comes from the line of Amit Kumar of Macquarie.

Amit Kumar
Macquarie Research

Two quick follow-up questions, I guess, to the previous discussion. First of all, just going back on the discussion on capital management. In the past, we have talked about a special dividend, too. Is that still on the table down the road? Or is that off the table?

William Robert Berkley
Founder and Executive Chairman

Amit, I've talked to you for many years, and I've always said exactly the same thing. My view about our company is simple: we do what we think is best for our shareholders no matter what. If someone comes in at a high price and wants to buy the company, we'll talk to them. If something -- if we think the most attractive for our shareholder is to buy back stock, we'll buy back stock. If we think we have more capital than we need and there are alternatives to it, we'll pay a special dividend. We paid a special dividend a couple of times, we bought back stock opportunistically. And each period of time, on a consistent curve, we look at our capital account, we look at what alternatives we have, we look at what we see the future to be and we try to make those decisions. But the only benefit we have with our size is we can be nimble. All the decision-makers fit in 1 room and we talk and try to figure out the right thing to do. So nothing is ever off the table. We do what we think is best for our shareholders at any point in time. The answer is not off the table.

Amit Kumar
Macquarie Research

Got it. And maybe this might be for Gene. Were all the buybacks working in the open market? Or was a piece of it under a 10b5-1?

Eugene G. Ballard
Executive Vice President of Finance

All open market.

Operator

And our next question comes from the line of Michael Nannizzi of Goldman Sachs.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

I have a couple of questions, if I could. One is just on the temporary capital point. What might -- I mean, what might a structure look like that you kind of alluded to? And are there any that you have kind of that you're putting together on a small scale today that might come to fruition? Or is there -- like where are we in this process of W. R. Berkley being able to leverage external capital? Are we -- is it like first thing in conversation or...

William Robert Berkley
Founder and Executive Chairman

Michael, you have the most advanced firm in structuring alternative capital in the insurance business. When I was in the annuity business, your firm structured alternative capital for me.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Yes. But those are the smart guys on the other side of the wall, they don't talk to guys -- they don't talk to us.

William Robert Berkley
Founder and Executive Chairman

The answer is that there are people out there who come and talk to us all the time about wanting to find ways to put capital at risk in the insurance business. And we talk about various alternatives and things that we consider. We don't have a plan now, but between their discussions with Rob and Gene and me, we're very confident. If we wanted to do any one of a number of things, we could easily do it. We haven't chosen a plan, but we're pretty comfortable being financially versatile that we could come up with something no matter what the option was that could help us get by without raising new common stock, which really was -- our historic view was you raise common stock, you raise preferred, you raise debt, that was -- that's sort of what it was. And I don't think that's the alternative mix that is what a company in 2015 needs to look at in our business. I think there are a lot of other alternatives. And we see many of them in the marketplace now. And there are also variance that aren't in the marketplace, but offer attractive options.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Okay. So I mean, I guess, the question is like is this something that you expect, I mean, that you think you could put together in the next year, 2 years, 5 years? Or is it -- like if we look over time, it's the ability for Berkley to either leverage external capital to grow or utilize external capital and sort of shrink its own capital base?

William Robert Berkley
Founder and Executive Chairman

We think we can always find capital which we will do on an opportunistic basis when we see reason or need. And we're not -- if I was talking about -- to 3, 5, 7 years, I wouldn't be talking about it. This is something we see in the next year or 2 or 3, where we think there'll be an opportunity to do something. Do we have it now? It's not 2 or 3 months from now. But it is within a time frame we think that one can see. But tell me what pricing is going do, tell me how opportunities are going to arise, we think they're there.

Michael Steven Nannizzi

Goldman Sachs Group Inc., Research Division

Got it. So I mean, so then -- so you would be comfortable of moving in that capacity towards, at least part of your business, more of a fee-based model if that were to present itself in a way that was somewhat sustainable or...

William Robert Berkley
Founder and Executive Chairman

Those are your words, not mine.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Okay. All right. And then, on the tax rate. I mean, if nothing comes to fruition from the government side, I mean, with reallocating your portfolio back towards munis, I mean is that something that you would consider doing to reduce the tax rate? Or...

William Robert Berkley
Founder and Executive Chairman

Yes, but -- the answer is yes. We could shift back towards the muni market. But we're -- the muni market is a much better longer-term market, longer-duration market than a shorter-term duration market. So you don't get the real benefits in the shorter term. So you need some changes in the investment marketplace for us to do that as well as higher yields for us to be willing to go out to 10, 12, 15 years.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Okay, got it. So tax strategies maybe on the investment side, maybe other strategies, but with the goal to try and reduce the tax rate. But at some point, if government rules don't change, then you...

William Robert Berkley
Founder and Executive Chairman

Although there are lots of things that are in offer now because the government is taking note of more and more U.S. companies going overseas.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Got it. And then just last question, if I could, maybe in the domestic business. The expense ratio, Gene, you answered it came down year-over-year, it higher than we had. And I think we kind of talked over the last few quarterly calls that the expense ratio should continue to come down to reflect the growth that you guys have had over the last couple of years. Are we at a point now where this is kind of where you expect the expense ratio to be? Or is there still leverage on the expense side as you continue to earn through that growth?

Eugene G. Ballard
Executive Vice President of Finance

Mike, there's still leverage there and we expect it to continue to improve. When you look quarter-to-quarter, some of this is sort of volume-dependent with the new DAC rule, when your volume drops, you take a little bit more of a hit on your expense ratio than you used to. But -- so it's hard to look at it quarter-by-quarter, but yes, we definitely expect it to continue to improve.

Operator

And our next question comes from the line of Josh Shanker of Deutsche Bank.

Joshua David Shanker
Deutsche Bank AG, Research Division

I'm going to continue on the same line of questions. And I don't -- I hope you'll bear with me. In terms of the current view of, hey, you're going to report both a pretax and an after-tax ROE and you'll reiterate your long-term goal of 15% ROE or better, is that the optimism you're talking about? Do you believe that the taxation situation will change in a way that allows you to do that? Or do you expect to be able to hit that 15% ROE over the long run without any improvement to the tax situation?

William Robert Berkley
Founder and Executive Chairman

I do.

Joshua David Shanker
Deutsche Bank AG, Research Division

You do, okay. And in terms of thinking about the -- Rob talked about, it's 2 steps forward, 1 step back for international work. Can you talk about a little bit of how you're looking at the situation from this quarter? And then -- and it's a 1-quarter issue. What should we expect going forward?

William Robert Berkley
Chief Executive Officer, President and Director

Josh, it's Rob. So on the international front, first off, there are some expenses, as Gene referenced, associated with Solvency II, which we will be working our way through as we make our way to the end of the year. We would expect those expenses will begin to diminish at a material rate as we make our way into '16. And then we have some other plans as it relates to some reorganizations that we're doing within the segment, some of which was accomplished in the second quarter, some of it will occur in the third quarter, and we would expect that, that can culminate -- will be quieting down in the fourth quarter. So I think the way that people should be looking at it is that, the third quarter, you may see it tick up a little bit more from where it is now. The fourth quarter, you should see somewhat of an improvement. We would hope from the third quarter and by the time we're in '16, we should be certainly in or on our way to a materially better place.

Joshua David Shanker
Deutsche Bank AG, Research Division

Perfect. Perfect. And in terms of thinking about the opportunity set of hiring new talent, how does the international market look compared to the domestic market?

William Robert Berkley
Chief Executive Officer, President and Director

I think the answer is that we see opportunity on both fronts. Obviously, we look at each opportunity individually, and it needs to stand on its own 2 feet.

Joshua David Shanker
Deutsche Bank AG, Research Division

And is that true -- anything about a greenfield business that you guys are willing to develop yourself? I mean, the opportunity exists for you to create a new idea for a business, maybe internationally, whereas the U.S. market is somewhat more developed, do you see an opportunity there? Or would you -- are you more interested in proven track record, an international idea that's already underway?

William Robert Berkley
Chief Executive Officer, President and Director

Josh, I guess, again, it depends on how you define greenfield. But if you look at most of our activities, most of the business that we have started, it's been a situation where we have an individual or a team of people that come together that have a significant amount of expertise that they've developed over the years within a particular niche. And we don't expect that we would deviate from that approach.

Operator

And our next question comes from the line of Ryan Tunis of Crédit Suisse.

Ryan James Tunis
Crédit Suisse AG, Research Division

I guess, my first question is just on the expense ratio, I guess, bigger picture in international. It's been elevated for some time and it looks like premium growth is slowing somewhat. Just curious how much longer-term improvement there is contingent on revenue growth relative to managing down costs?

Eugene G. Ballard
Executive Vice President of Finance

I'll just make a comment. It's definitely a combination of both. I mean, there's a number of initiatives underway that we know are going to improve things from the expense side. Rob could comment more on the premium side, but I think it's going to take a combination of both to get it where we would like it to be.

William Robert Berkley
Chief Executive Officer, President and Director

So as Gene suggested, it's going to be a combination of both. Certainly, top line and earned premium levels have an impact. Certainly, currency to a certain extent has an impact as well in some cases. But fundamentally, much of the action that Gene was alluding to earlier that I touched on as well has to do with, quite frankly, just trying to find ways to make the business better, to make it more productive, to make it more efficient. And we think that we are getting some traction in doing so, really not because of what we're doing here at the holding company as much as, really, a lot of the good things that our colleagues that run these businesses are doing. So long story short, would more earned premium in the backing be helpful? Absolutely. But I think the way we are going to get to a better place is because of some of these delivered activities that we referenced earlier.

William Robert Berkley
Founder and Executive Chairman

I think the bottom line is we would expect that, that expense ratio is going to come down. And putting aside currency issues will -- we've got to have somewhat improvement in the volume. So I think that while in the short run, i.e. a quarter, you may not see much dramatic improvement, I think if you look at these numbers a year from now, it would be substantially better.

Ryan James Tunis
Crédit Suisse AG, Research Division

Okay. And I guess just along the consolidation line, curious if you could maybe opine a little bit on how the consolidation might potentially give you guys some near-term advantages. If we should be thinking about this as something that, over the next year or 2, could actually create revenue opportunities?

William Robert Berkley
Founder and Executive Chairman

Why don't I let Rob talk about some of the opportunities. He's -- from an operating point of view, and then I'll talk about it from a broader perspective. So why don't you start?

William Robert Berkley
Chief Executive Officer, President and Director

Just to make sure we're clear, we're talking about the consolidation that we see going on in the marketplace, correct?

Ryan James Tunis
Crédit Suisse AG, Research Division

Correct, correct.

William Robert Berkley
Chief Executive Officer, President and Director

Okay. I think that it creates opportunity on multiple levels. I think the fact of the matter is, that whenever you have this type of activity going on, it creates a distraction within organizations that are directly involved in the activity because they are somewhat inwardly focused on what they're trying to do. And when they're distracted in such a manner, it makes it more challenging to remain focused on the distribution system as well as, ultimately, the insured or whoever the customer may be. In addition to that, our experiences, and often times back to the point around distribution, that when there are large mergers, it creates a question within the minds of some of the distribution, how many eggs they want to have in 1 basket? And then, finally, you have the other component, which oftentimes also can create opportunity for us or any other market participant, where there are talented people that for whatever the reason may be, become disenchanted with their future and are looking for another alternative.

Ryan James Tunis
Crédit Suisse AG, Research Division

Okay. And then, I had one more, I guess, a nittier one, just on NII. What was the impact this quarter from the energy portfolio? And is there any visibility on what you think the impact might be next quarter?

Eugene G. Ballard
Executive Vice President of Finance

For the energy investment, yes. They're profitable this quarter, and we expect them to be profitable next quarter.

Operator

Our next question comes from the line of Jay Cohen of Bank of America Merrill Lynch.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Yes, on the tax rate issue, Bill. At some point, would you be willing to essentially redomicile offshore, whether it's on your own or through some sort of M&A?

William Robert Berkley
Founder and Executive Chairman

The answer is we're always willing to do what we think is in the best interest of our shareholders. We think we have some level of obligation to this country. We just think, at the moment, the way the tax rules are, we won't be able to compete in the long run when we're paying taxes at 30-plus percent and are -- we have many competitors who are paying very low tax rates. And they do it -- forget about what they show on their statements, they do it in many ways through loss portfolio transfers because then they don't pay tax on the discounted value of their reserves, through all kinds of vehicles, some of which they feel are justified and some of which they don't. But the bottom line is, how much cash taxes do you pay? And it's a competitive disadvantage that in the long run you can't continue with. We look at it all the time. We've worked on Congress. I have no idea how come it has been so difficult to persuade Congress. And I have no idea how some insurance commissioners think, for some reason or another, it's a good thing for people not to pay taxes in the country. But Jay, we work at it every day. We make that decision and we look at it all the time. And at some point, we'll have to come to the conclusion we can't continue in the current posture. But each time they do something to make the differential less, it makes it less certain. But we would look at every alternative and we do every day and we talk to people about it.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Got it. And then maybe a question for Gene. Looks like your debt-to-capital is a little over 32%. Would that act as any sort of constraint when you think about buybacks at this point?

William Robert Berkley

Founder and Executive Chairman

No, I don't think so. I mean, the fact is our net -- you have to remember, first of all, we have $400 million of statutory capital because we carry HealthEquity at fair market value. So our statutory capital and our GAAP capital aren't the same, so we've had an increase in the statutory capital, that you don't see, of $400 million from just HealthEquity. So there -- and there are other things that we've had increases in statutory capital because they are -- it's not GAAP numbers. So statutory capital has gone up, whereas GAAP capital has not. And we haven't gone -- but we haven't bought more stock than our net earnings have. So if you look at our aggregate earnings, the amount of stock is what basically matches our earnings. So we don't think it's a problem.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

And Bill, at what point is that a reasonable assumption for us to use that your buybacks and dividends would be roughly equal to your earnings?

William Robert Berkley
Founder and Executive Chairman

I think that in -- over any period of time, that'd be a general thing. Gene needs to make a comment about -- just hold up the numbers on his partnership things.

Eugene G. Ballard
Executive Vice President of Finance

I misspoke on the energy fund, I got a quarter ahead of myself with the 1 quarter lag, but they actually, in the quarter, we just reported they had a small loss but we don't expect that to go forward. So I just want to correct that.

William Robert Berkley
Founder and Executive Chairman

But at this point, just -- I think, they don't have a lots of our attention because the velocity of change now is much less. Okay, Jay?

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Yes.

Operator

Our next question comes from the line of Ian Gutterman of Balyasny Asset Management.

Ian Gutterman
Balyasny Asset Management L.P.

Bill, I was hoping if, first, you could talk a little bit about your outlook in the Latin America part of your international business. Just forgetting about the currency for a moment, right, but just -- it seems like those economies are getting a little tougher. And does that impact your ability to grow or are the lines you're participating in not seeing pressure from the economies there?

William Robert Berkley
Founder and Executive Chairman

I think in the broadest sense, Latin America is a growing marketplace. It has more volatility as every developing market does. We have been successful in Argentina because we have great managers in Argentina. And they've done a great job and we have the same in Brazil, and we're expanding in Colombia now. But the cornerstone of this business is great managers and great people. And we think that we've been able to get those kinds of people to work for us. Now that said, it's a lot bumpier ride at the moment than it was 18 months ago. And -- but I think that we're pretty happy with our participation and, if anything, we'd like to use an opportunity of uncertainty for us to expand further.

Ian Gutterman
Balyasny Asset Management L.P.

Got it. Great. And then just on the tax so just -- I mean the one advantage, I think you'd agree, I mean, the one advantage of being in the U.S. is access to business, right? And the offshore companies frankly can't get at the great specialties you have because they don't have that -- that kind of business doesn't make it offshore, right? So...

William Robert Berkley
Founder and Executive Chairman

No, no. The way they do it is they set up domestic subsidiaries.

Ian Gutterman
Balyasny Asset Management L.P.

Right, right. But then a 1/4 share part of it, they can't get 100% offshore.

William Robert Berkley
Founder and Executive Chairman

No, but they -- first of all, they can make it into a loss portfolio or transfer, so they move their reserves offshore, so they don't pay discount on the loss reserves. And then they quote a share, a large percentage of what's left. So they bring the tax rate down from 35% or 39% down to less than 10%. So when you can do that, it's a pretty big competitive advantage.

Ian Gutterman
Balyasny Asset Management L.P.

No, I understood. I guess, what I was getting at is sort of the opposite side is, would any potential solution to improve your tax rate in any way affect your ability to control the type of business you want to control, right? You know what I mean? The companies offshore, even though some of them have bought U.S. businesses, haven't seemed to have the success accessing business in the same way because they seemed to be perceived differently by being offshore.

William Robert Berkley
Founder and Executive Chairman

I don't think it's the perception of being offshore. I think they have it all, have great people, but I think that some of them have great people and do really well and others don't. But I think being here, doing this now for almost 50 years, we have a competitive advantage because we have people who are old and gray and have been doing it for a while, and most of the others are young and spry. So we're hopefully replacing the old and gray people with the young and spry people, and we'll have the combination that will be okay.

Operator

And our next question comes from the line of Mark Dwelle of RBC Capital Markets.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

Just 1 quick question. Back at the top of the discussion, I think Rob had mentioned weakening in the commercial auto line. I was wondering if you could just expand on that. I guess I had been under the impression that, that was a line of business that, relative to many, was actually holding up somewhat better.

William Robert Berkley
Chief Executive Officer, President and Director

Yes. Maybe I miscommunicated, but from our perspective, commercial auto is very challenged. While it would seem, by and large, there's opportunity for additional rate, I still think the economic result that will deliver is not particularly rewarding at this stage. So while it may not be rapidly deteriorating or deteriorating at all from a rate perspective, I think even with the rate increases that many in the industry are getting, it's not where it needs to be.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

I see. So the comment was directed more towards the relative profitability weakening rather than sort of...

William Robert Berkley
Chief Executive Officer, President and Director

That is correct. I'm sorry if I misspoke.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

No worries. That was the only clarification.

Operator

[Operator Instructions] Our next question comes from the line of Howard Flinker of Flinker and Co.

Howard Flinker

Howie Flinker. I'll take your side on the question of capital. You're writing at about 0.91 to 1, if you include total capital. And if you want to include equity, it's 1.3. You could write as much business as you want, you don't need capital. And as you have learned since you went into business, you learned 2 things. One, the best form of capital is retained earnings. And the second, when you were very young, when your businesses are young, you saw what happened to insurance companies like St. Paul and GEICO and Safeco, when they used too much leverage. The bill comes at the wrong time and it's a large bill. So I'm on your side on this one.

William Robert Berkley
Founder and Executive Chairman

Thank you.

Operator

And at this time, I'm showing no further questions. I would like to turn the call back over to William R. Berkley for closing remarks.

William Robert Berkley
Founder and Executive Chairman

Well, thank you all very much. We are optimistic that this is the time that will give us great opportunities in many fronts. The ability to be nimble and select the opportunities that reward our shareholders best is something we've always prided ourselves on. You can only be sure of one thing: we will always do what we think is right for our shareholders, and you can count on that in this company no matter what. Have a great day. Thank you.

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