S&P Global
Market Intelligence

W. R. Berkley Corporation NYSE:WRB

FQ4 2019 Earnings Call Transcripts

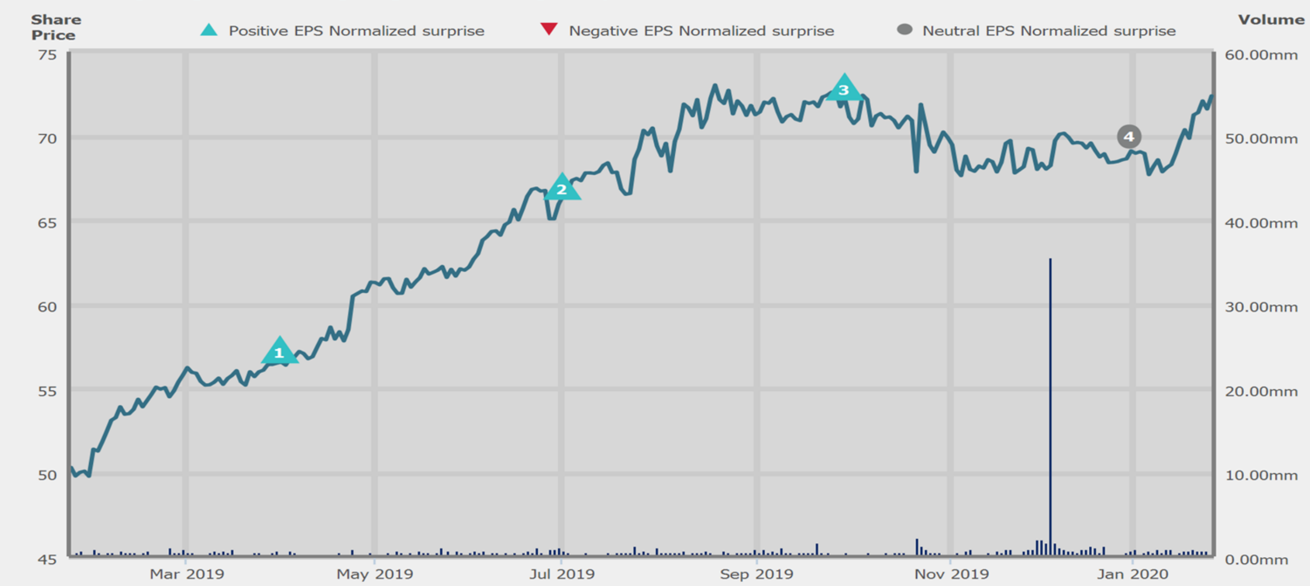
Tuesday, January 28, 2020 10:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2019-			-FQ1 2020-	-FY 2019-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	0.72	0.71	0.00	0.75	3.06	3.02
Revenue (mm)	1709.10	1716.78	0.45	1730.63	6612.95	6633.29

Currency: USD
Consensus as of Jan-23-2020 12:40 PM GMT

Stock Price [USD] vs. Volume [mm] with earnings surprise annotations



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2019	0.63	0.66	1 4.76 %
FQ2 2019	0.64	0.82	2 28.12 %
FQ3 2019	0.67	0.85	3 26.87 %
FQ4 2019	0.72	0.71	4 0.00 %

Table of Contents

Call Participants

EXECUTIVES

Richard Mark Baio
Executive VP, CFO & Treasurer

W. Robert Berkley, Jr.;President, CEO & Director

ANALYSTS

Amit Kumar
The Buckingham Research Group Incorporated

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

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Crédit Suisse AG, Research Division

Michael Wayne Phillips
Morgan Stanley, Research Division

Ryan James Tunis
Autonomous Research LLP

Yaron Joseph Kinar
Goldman Sachs Group Inc., Research Division

Presentation

Operator

Good day. And welcome to W.R. Berkley Corporation's Fourth Quarter 2019 Earnings Conference Call. Today's conference call 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 be -- in fact, be achieved. Please refer to our annual report on Form 10-K for the year ended December 31, 2019, 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. Bob Berkley. Please go ahead.

W. Robert Berkley, Jr.;President, CEO & Director

Carmen, thank you very much, and good afternoon, all, and thank you for dialing in today to chat with us about our fourth quarter results.

On this end of the phone, in addition to myself, again, you have Bill Berkley, Executive Chairman; and Rich Baio, our Chief Financial Officer.

We're going to follow a similar agenda to what we've done in the past. Rich is going to lead off with some comments on the quarter, and then he's going to hand it off to me and I'll offer a couple of relatively brief comments, and then you'll have the 3 of us at your disposal for any Q&A.

Rich, if you would, please?

Richard Mark Baio
Executive VP, CFO & Treasurer

Great. Thanks, Rob. We reported net income of $119 million or $0.62 per share and continue to see an acceleration in the growth of our top line, both from a gross and net premiums written basis. Our underwriting results improved on a current accident year basis excluding cat losses, while we experienced some variability on the investment side that we've alluded to during earlier earnings calls.

Focusing first on the underwriting results. Gross premiums written grew 10.1% and net premiums written grew 9.3% in the current quarter, bringing the full year growth to 7.3% and 6.7%, respectively.

Total premiums for the group were $1.66 billion in the current quarter, comprised of approximately $1.5 billion in the Insurance segment, representing an increase of 8.2% over the prior year quarter. And $176 million in the Reinsurance & Monoline Excess segment or an 18.9% increase quarter-over-quarter.

The Insurance segment's net premiums written grew in all lines of business with the exception of workers' compensation. The growth in the quarter was led by professional liability of 12.9%, followed by 11.8% in other liability, 11% in commercial automobile and 10.2% in short-tail lines. The Reinsurance & Monoline Excess segment grew in property reinsurance by 22.5%, casualty reinsurance of 19.9% and monoline excess of 8.3%.

Pretax underwriting profits increased more than 71% to $115 million compared with $67 million a year ago. The improvement was primarily attributable to an increase in net premiums earned of 6% and lower underwriting expenses relative to the growth in net premiums earned.

The current accident year loss ratio, excluding cats, was 61.4% in the current quarter, which was slightly better (sic) [higher] than the prior year quarter and comparable with the full year of 2018 and 2019. In addition, cat losses decreased from $45 million in the prior year quarter to $20 million in the current quarter, representing a reduction of 1.6 loss ratio points. Cat losses in the current quarter were 1.2% of net premiums earned.

Finally, prior year loss reserves developed favorably by [$2 million], representing approximately 0.2 loss ratio points. Accordingly, our reported loss ratio was 62.4% for the fourth quarter of 2019.

The expense ratio was 30.9% or 2% lower than the prior year quarter, and improved 0.6% from the preceding consecutive quarter. Although we continue to see an improvement in our expense ratio, the current quarter is not expected to be the ongoing run rate for 2020. We anticipate that the full year rate for 2020 is more likely to be in the range of 31% to 32%.

As we've mentioned in the past, please remember that our expense ratio may experience some variability as we continue to make investments in the business. The current quarter benefited from the increase in net premiums earned, along with reduced acquisition costs due to favorable seating commissions and operational efficiencies we've referenced in recent past. This brings our reported combined ratio for the fourth quarter of 2019 to 93.3% and our current accident year combined ratio, excluding cats, to 92.3%.

Now focusing on our investment results. Net investment income from our core portfolio remained flat quarter-over-quarter. Our book yield for the quarter and full year for the fixed maturity portfolio was 3.4%. We have maintained an average rating of AA- and an average duration of 2.8 years for fixed maturity securities, including cash and cash equivalents.

As we've mentioned in the past, our investment funds do have some variability over time. This quarter was evident of this situation. We had a couple of isolated funds with unfavorable mark-to-market adjustments and likely see them recovering. Even with this variability in the quarter, our full year book yield was 5.2%, a result within our expectations. We believe the alternative investments will continue to produce above average long-term returns.

Pretax net realized and unrealized losses was $23 million. The loss in the quarter was primarily attributable to a decline in the fair value of preferred stock and Fannie and Freddie, which under the accounting rules is now reflected in the income statement rather than directly reported in stockholders' equity. Excluding the $30 million of unrealized losses due to these mark-to-market adjustments, we realized pretax gains of $7 million in the quarter.

The effective tax rate was 18.4% for the quarter, which largely benefited from a lower effective tax rate due to the partial release of our valuation allowance against deferred tax assets associated with net operating loss carryforwards in our international operations. In addition, we reflected a favorable adjustment truing up our 2018 tax accrual to file tax returns. We expect 2020 to return to a more reasonable level.

Stockholders' equity was approximately $6.1 billion or $33.12 per share, representing an increase of 11.7% from the beginning of the year. For the full year, book value per share grew 17.3% before dividends and share repurchases. We returned capital of $176 million in the quarter and $326 million for the full year. Our return on equity for the quarter on an annualized basis and for the full year was 8.8% and 12.5%, respectively, on net income.

We had strong cash flow from operations in the quarter of $349 million as well as approximately $1.15 billion for the full year.

And finally, it is worth reminding folks that the new accounting treatment for credit losses on financial instruments is effective in the first quarter of 2020. Accordingly, you will see a cumulative effect adjustment to stockholders' equity, which should not be material to our financial statements. More importantly, this change in accounting treatment may add some additional variability to the income statement as we reevaluate each reporting period, the allowance for credit losses associated with fixed maturity securities, loans, receivables and other financial instruments. Thanks, Rob.

W. Robert Berkley, Jr.;President, CEO & Director

Rich, thank you very much. That was a lot, it's good there's a transcript for everybody. So when I -- right before I came down to get on the call, I was taking one last look at the earnings release, and I was looking at the header that we have referencing the top line growth and the return for the year, which I think is clearly attractive. But if it were solely left up to me, which it isn't, I would have gone for a header or a title that's more akin to, it is happening, with a footnote that would say, ex workers' compensation. And what I mean by that is what we have been discussing and others have been discussing for an extended period of time as far as the challenges that the market faces, the realities that stem from a low interest rate environment, frequency of cat activity and, of course, social inflation, has finally gotten to the point where it is no longer solely being talked about, but is actually being acted upon. And this is a meaningful sea change that became very visible in our opinion in the fourth quarter, and there is no sign of that slowing down.

The comment or the note about ex workers' comp. Look, the reality is that workers' comp has had its moment in the sun. And the clouds are beginning to build a little bit as a result of the actions that are taken -- being taken by state rating bureaus. Having said that, I would caution people not to overreact and assume that it's doom and gloom overnight. There is this thing called negative trend, which is partially mitigating the actions that are being taken by state rating bureaus.

Having said that, going the other way, we certainly are paying close attention to severity in the workers' comp line, and those that are not keeping an eye on that, that may prove to be a challenge in the future.

But putting aside comp, when we look at our business, every component of the commercial lines marketplace that we participate in, to a greater or lesser extent, we are seeing rates moving up and our sense is that the trend will continue and, in many cases, will not only continue but may very well accelerate from here.

Rich did a great job talking about the quarter and putting a bit of a bow around it. I'm going to just piggyback on a few of his comments and offer you a couple of observations.

Maybe starting out with the top line. The growth was more than we've seen. I don't know, and forget about quarters, I don't know how many years, but it's been a long time. Rich is trying to mouth me how long it's been, but I can't really tell what he's saying, but it has been a while.

Top line up more than 10% on the gross. On the net more than 9%. It's worth maybe taking a step back or peeling a layer or two back and really understanding this. We are seeing significant growth in submissions, particularly in our specialty businesses, and even more so in our E&S operations. It has been building for a while, and it's really accelerating in the fourth quarter.

We are seeing as a result of that, clear evidence that there is leverage on the rate side. In our release, I think we said approximately 9%, to put a slightly finer point on it, it was 8.9%, ex workers' compensation. A figure that we've shared with you from time to time is our new business relativity, which is a metric that we use to try and compare on an apples-to-apples basis, how much we're charging for new business compared to our renewal book. In our new business, we are charging 100 -- or excuse me, 1.042 or 4.2% more for new business compared to renewal business. This is an important metric because it gives us confidence and comfort, we are not buying new business. In fact, new business in theory, one knows a little bit less about than your renewal book, so you should be surcharging that.

As far as the renewal retention ratio, this continues to be pretty steady hanging in there at approaching 80%. It's shocking to us at times, how that number doesn't move. But I think it's important to connect the dots, that renewal retention ratio isn't moving in spite of what we're doing with the rates.

Pivoting over to a couple of comments on the loss front, as Rich suggested, it was, by and large, what we had expected. But I do want to drill down a little bit more here and touch on, I guess, what's become of topic of the day, though, from our perspective, it should have been the topic of discussion for the past several years.

To that point, we started talking about social inflation back in 2016. We started pushing for rate back then. We have been pushing for rate since we started to see this, but putting aside rate, we started taking other types of underwriting action, whether it be terms, conditions, deductibles or just pure risk selection.

The fact of the matter is that social inflation, while it's being more actively discussed and acted upon today, it is not a new phenomenon. It is an example that you do need to pay attention -- it is an example that expertise make a difference. It is an example of how you need to be not solely consumed by the rearview mirror, but you need to be looking out the front windshield as well.

We've heard from some people over the past few years when we've been talking about the type of rate increases that we've been getting, the question has come up, "Well, why aren't you dropping your loss picks if you're getting all of this rate?" And the simple answer is, "Because we saw this out there in the environment, and we needed that rate and the underwriting actions in order to be able to reconcile the loss pick we are using." Having said that, as we are getting, approaching 9 points of rate at this stage, it's very hard for us to imagine. We are not comfortably outpacing loss cost trend at this level.

Maybe switching over briefly to the expense ratio. And again, Rich touched on this, I'll just put in my two cents here briefly. We do have some IT and data-related initiatives that have been going on and will continue to go on. They are significant investments that certainly can have an impact on our expense ratio. Having said that, going the other way, I think we're going to continue to benefit from higher earned premium as the business is growing and much of that growth is coming from higher rates so that will help mitigate the additional spend.

Rich also touched on the investments, I'll offer my two cents there. Again, as he said, the core portfolio was right in line with expectations. We did have a little bit of noise coming out of the funds. And the noise really came from a couple of isolated places. We are not particularly bothered by this. It's just the reality is as part of our total return approach occasionally, you're going to get a little bit more volatility. And our sense is what moves in one direction in the quarter is likely to move back in the other direction over time. So I would caution people not to read too deeply into the funds. My sense is, and I think Rich's sense and other people's sense is it is likely to move back to what is a more historical level in relatively short order.

I guess, last comment on the investment portfolio is something that we've discussed in the past, and that has to do with gains. And I referenced this idea around total return. We are focused on building book value for shareholders through underwriting as well as investment activity. We are -- we take a long-term view. Part of our effort, particularly in this extended low interest rate environment has been to try and find other ways to generate return. Our alternative portfolio investment funds, included but not limited to that, has proven to be, as Rich referenced, a great source of return for our shareholders. We have discussed in the past that, give or take, people should be expecting $100 million a year or roughly $25 million a quarter in gains, but we also have reminded people that is going to be lumpy. I believe we did a little bit more than that in '19. And while we certainly cannot promise or guarantee anything, when we look out at 2020, we think that there is a good chance that we will exceed the traditional guidance.

A couple of quick comments on capital management. We're very focused on trying to strike the appropriate amount of capital. We don't want the porridge too hot. We don't want it too cold. We want it just right. However, let's talk about what does just right mean. Just right means what we have today, and in addition to, that what we see our needs could potentially be tomorrow. The business has been generating more capital than it could use for some period of time. Our preferred approach has been special dividends. But as we've discussed in the past, we tend to award those or pay those out as we have more visibility. I think that it is likely that special dividends will continue to be an important part of how we return excess capital to shareholders. Having said that, we are not opposed to other levers such as share repurchase or debt repurchase if we think the opportunity is there and it makes sense.

So final couple of comments from me, and then we'll be turning it over to you for any questions.
Upon reflection of the quarter and putting aside our numbers, just the environment overall, one of my takeaways is, this is the type of environment that we're moving into, that this business is built for. This is the type of environment that we are able to do disproportionately well for 2 reasons. One, because of how we're structured, and we're able to respond in a more timely manner than others; and two, because of the type of business that we write. Moments like this when you see not just the standard markets, but others

starting to reexamine their appetite, in many cases, narrow it or curtail it and certainly, at a minimum, people begin to think about risk and return and adequate pricing in a different way than they have for the past couple of years, that falls right into our strike zone.

So we are excited about what we see in front of us. We were enthusiastic earlier in '19. I think what we saw in the fourth quarter of '19 just built on that enthusiasm, and while there are some that would suggest that we tend to be an optimistic organization, and I think that is a fair statement, we are an optimistic organization. The data that we see in our own business, and the data that we can all see in the industry, I think, clearly supports this optimistic view.
So Carmen, let me pause there. And if we could please pivot to the questions. Thank you.

Question and Answer

Operator

[Operator Instructions] And our first question is from the line of Amit Kumar with Buckingham Research.

Amit Kumar
The Buckingham Research Group Incorporated

Congrats on the print. Just a few quick questions. The first question is on the -- I was hoping you could help me tie your pricing commentary and the loss cost discussions. Does this -- are we at a point where this translates into margin expansion for 2020 versus 2019? Or just based on how long rate takes to earn, we should think about margin expansion for the back half of 2020 versus 2019?

W. Robert Berkley, Jr.;President, CEO & Director

I mean, obviously, different parts of our business earn premium in a different way. Having said that, certainly, by the second half of 2020, you're going to see a meaningful amount of that fourth quarter '19 premium earning through. That '19 -- fourth quarter '19 premium is going to start -- it's already started to earn through and that will continue to accelerate.

As far as margin expansion goes at a macro level, and I think it's best that we not get into the weeds, but when you're getting close to 9 points of rate, even our, what I would suggest is a very measured approach to trend, i.e., we're trying to make sure that we are erring on the side of caution, it's hard to imagine that we are not outpacing trend by some number of hundreds of basis points.

Amit Kumar
The Buckingham Research Group Incorporated

That's a fair point. The second question is on expense ratio. And I wanted a clarification here. I was reading earlier transcripts. And Rob, there was a comment you made in that industry presentation, you talked about, our goal is to push through 31%, and over time, we would like to push it through 30%.

W. Robert Berkley, Jr.;President, CEO & Director

That's correct.

Amit Kumar
The Buckingham Research Group Incorporated

You made these comments. I was just trying to think, I completely agree that the ER is a function of higher earned premiums. However, has there been any shift in the allocations towards the ramping up on IT and data analysis? Is that also changed? Or maybe just help me understand what has shifted versus the discussion we had a few months ago?

W. Robert Berkley, Jr.;President, CEO & Director

Well, I think my comments were meant to be sort of intermediate and long-term in nature. And what I'm trying to message to you, picking up on Rich's point, is that the expense ratio was good this quarter. And we certainly would like to continue to push on that. But the simple reality is we are making some investments today that will enable us to get to where we want to, not just on the expense ratio front, but being able to run the business efficiently and effectively. We think investments on the systems front as well as the data and analytics front that we already have been making are likely to accelerate, and that comes at a cost, but that's going to allow us to continue to get where we want to go.

Operator

And our next question comes from Michael Phillips with Morgan Stanley.

Michael Wayne Phillips

Morgan Stanley, Research Division

First question, Rob, you said in recent quarters, that once rates get to a certain level, you'll look to grow more aggressively. It sounds like from what you're saying today, that's where we are today. You're looking to grow more aggressively because rates might already be there. I guess, one, is that true? And then if so, to your comment of, you see no signs of it slowing down. I guess, maybe talk a little bit more about that because if we're at a point where margins are going to start to expand, how long does this last into 2020? Or kind of your thoughts on that.

W. Robert Berkley, Jr.;President, CEO & Director

Sure. So I think as we've perhaps discussed in the past, it's tricky to use too broad of a brush here because, again, ex comp, all -- basically, all of the commercial line space is in some form of hardening where we're seeing rates go up, but it's not happening in lockstep.

So we see that happening. We see that accelerating. There are certainly what I would define as parts of the market, our products, our products in certain territories, where we're seeing a green light, and we are looking to push and push hard, not just on rates, but we want to right -- we want more count, if you will, policy count. There are other places where it's more of an amber light, and we're just going to focus on the rate, and we're not looking to push the count.

But once we get that green light, we're not just going to open up the spigot. We're going to rip it out of the wall and we're going to let a pour in, and we'll call a plumber later. And how long is it -- as far as how long is it going to go for...

Michael Wayne Phillips
Morgan Stanley, Research Division

Well, I asked that question in the backdrop of the industry that it typically takes a long time to turn rate positive and when it does, it doesn't last very long. So...

W. Robert Berkley, Jr.;President, CEO & Director

Yes. Look, I think it never lasts as long as you'd like, and that's sort of reality. At the same time, from my perspective, I think from our perspective, there's still a lot more pain to come. And if you look at what's driving the change, it's pain. And we've sort of gotten a glimpse of the tip of the iceberg, but there's a lot of iceberg that's below the sea level. And there's just more to come. So from our perspective, we don't see this slowing, we see it accelerating and at a minimum, in some cases, maintaining from here, but in more cases they're not accelerating. How long will it go on for? I think that's a tricky one to speculate, but we think that there's a fair amount of runway ahead of us.

Michael Wayne Phillips
Morgan Stanley, Research Division

Okay. No, great. That's helpful. I think the commentary on, there's more pain to come is a great way to say it.

So to my second question then on the lovely social inflation term. You guys have said you've seen it since 2016. And from your earlier comments, even in the past year have said, you saw it in certain lines, certain segments and maybe not in others. And so I guess the question is, do you see it more widespread today than you did a couple of years ago? And is that part of the pain that you're talking about?

W. Robert Berkley, Jr.;President, CEO & Director

We -- yes, it is certainly part of the pain that I think the industry is facing. We saw early in a couple of lines in '16, and then we saw it more broadly in '17. So our recognition that this was not just a 1 line issue, but this was a broad issue, was something that we were grappling with definitively in '17.

Operator

Our next question comes from Josh Shanker with Deutsche Bank.

Joshua David Shanker
Deutsche Bank AG, Research Division

I'm sure Rich already filled you in. The last time you grew at this pace was at 4 -- it was 2Q '14. And you were growing for 15 consecutive quarters through that point based on rate increases. If I start a clock back in 4Q '10, during the last time pricing was driving up growth, it took Berkley about 2 years to show underlying combined ratio improvement and 3 years to show GAAP combined ratio margin improvement. Can you sort of give a compare and contrast a little bit between this sort of what's happening right now and what's happening then? And whether the lag in pricing, leading to better margins is likely to repeat like it did before? Or will it likely come faster this time around?

W. Robert Berkley, Jr.;President, CEO & Director

Well, my two cents, and Josh, I haven't -- we can have an off-line conversation where I can sort of examine our historical data with greater granularity. But my sense is that I wouldn't say we're comparing apples and oranges, but we're kind of comparing apples and pears, if you will. And so I can speak right now about the situation that we're facing.

We have a sense as to what we believe our loss costs are running at. We have a sense as to what our margins are. We have a view as to the rate that we're getting. And from our perspective, when you see the type of rate increase that we got in the fourth quarter start to earn through, while we are not going to move too early, in a vacuum, one would think that, that should -- it's certainly our view, that it will benefit our margins.

But we are not going to shoot from the hip. We're going to -- as we always do, on day 1, we try and book things in a measured way. And as it seasons out, then we will start to recognize it because, again, we do not want to declare victory prematurely. But at a high level, when we look at what we believe our trend is running at, and we look at the rate that we are achieving, we think when the dust settles, it is likely that margin improvement is incurring.

Joshua David Shanker
Deutsche Bank AG, Research Division

Okay. And then let me try and get at one other way about your level of optimism. So we're at rates around 9% excluding workers' comp, if I look at the Insurance segment, we're at about 8% net written premium growth, up from 5% of the premium -- previous quarter. To what extent is exposure growing in those numbers versus just rate?

W. Robert Berkley, Jr.;President, CEO & Director

It really -- it depends on the -- if you will, the line of business. I mean, there are parts of our insurance business, where the exposure growth is growing. But when we talk about rate, that 9%, that is pure rate, that's not premium, if you will.

Joshua David Shanker
Deutsche Bank AG, Research Division

So is exposure as of right now? Has it changed from the previous quarter?

W. Robert Berkley, Jr.;President, CEO & Director

It's probably, give or take, flattish. It would be my best guess. And again, that's because from our perspective, I think as we've talked in the past call or 2 or maybe more, that for the moment, we have been more focused on rate. But as we are seeing the rate get to a certain level, you're going to start to see our count grow.

Operator

Our next question comes from Yaron Kinar with Goldman Sachs.

Yaron Joseph Kinar

Goldman Sachs Group Inc., Research Division

So I guess, my first question just, Rob, is more around the loss trend itself. You've talked a bit about the acceleration in rate pointing to social inflation, more pain for the industry to come. But can you try and quantify what you're seeing in terms of loss trends?

W. Robert Berkley, Jr.;President, CEO & Director

So generally speaking, we don't really get into that level of granularity as far as loss trends go. From our perspective over the past few years, we think the industry has seen them accelerating with the exception of workers' compensation. But what I would tell you, I think, as we mentioned earlier, we think that the rate increase that we got in the fourth quarter very comfortably outpaces our loss cost assumptions in the aggregate.

Yaron Joseph Kinar
Goldman Sachs Group Inc., Research Division

Okay. And then specifically maybe in the Reinsurance segment, where I think if we strip out catastrophes, we did see some deterioration in the accident -- in the loss ratio. Can you maybe talk about what drove that uptick?

W. Robert Berkley, Jr.;President, CEO & Director

Richard, do you recall? I don't -- we don't have it at our fingertips, but we'd be happy to try and give you a better answer than that. If you want to, just follow up with Karen, if you wouldn't mind.

Yaron Joseph Kinar
Goldman Sachs Group Inc., Research Division

Sure. Yes, I'd be happy to do that.

Operator

Our next question comes from Mike Zaremski with Crédit Suisse.

Michael David Zaremski
Crédit Suisse AG, Research Division

First question, in terms of the discussion around the industry experiencing more loss inflation than expected, do you have a view on whether a large portion of that pain, I guess, per se, will come from the very old accident years due to the statute limitation changes in a number of states? Or is this predominantly a last kind of 5 accident year coming from the stuff during the last 5 years?

W. Robert Berkley, Jr.;President, CEO & Director

Look, from my perspective, the change as far as the statute of limitations around sexual abuse, are probably just another compounding factor that has added to the pain. But I think that the industry would have found itself in the position it's in with that or without that, it's just another pressure point, if you will. So I think that the industry made certain assumptions putting aside the change in the statute of limitations on sexual abuse. I think the industry has been making certain assumptions that this -- what has been, for many years, a very benign loss environment that, that would continue. And I think the industry got hooked on that. And I think the industry is going to pay the price for that.

Michael David Zaremski
Crédit Suisse AG, Research Division

Okay, that's helpful. And I -- yes please.

W. Robert Berkley, Jr.;President, CEO & Director

I think -- just one thing that I think is -- I think it is a price that the industry is going to pay. I think it is going to create pain. But I also think that there is a silver lining there. And it's circumstances like this that serve as the catalyst for the industry to get a dose of reality and for it to start to operate in a more sensible way. And while the pain is unpleasant, it does force that change in behavior. And that's what helps us get to a better place as an industry.

Michael David Zaremski
Crédit Suisse AG, Research Division

Okay. That's helpful. And you touched on the loss environment, was benign for a while, and clearly, that's changed on the casualty side. And that kind of seems like it dovetails to the workers' comp comments you've been making the last couple of quarters. If you can elaborate that? I think you said during your prepared remarks that you're watching the severity piece of the equation. So are you saying that severity is moving north, kind of what we're seeing in the -- in I guess, broader CPI? And is that one of the reasons you're pulling back exposure?

W. Robert Berkley, Jr.;President, CEO & Director

Look, we're -- if you look at our business as far as the premium, I think Rich may have mentioned this or it certainly was in the release, as far as comp goes, we're looking at the rates coming down. And as we see rate adequacy becoming less available, you're going to see us shrink that business.

While severity is a problem, probably the even bigger driver is just the action that we're seeing state rating bureaus take. And the other piece is, we're seeing both monoline and multiline players that are really chasing the business very hard. And we have a view as to what's adequate from a rate perspective, and we're just not going to chase it. We'll go right up to the line of adequacy, and we're not going to trip over that. And certainly, we'll do our best not to.

But I think the severity component just is something that people need to pay attention to. I think as we've maybe commented in the past, there are a lot of great things that come about as a result of science and technology and the things that health care can do to not to save people's lives, but also improve them. Those are wonderful things, but they come at a cost.

Michael David Zaremski
Crédit Suisse AG, Research Division

Okay. Lastly, in terms of the kind of the plain vanilla fixed income investment portfolio, is there -- do you have a rough idea of what the gap is between your new money yields and the existing portfolio yields?

W. Robert Berkley, Jr.;President, CEO & Director

It's roughly 100 basis points.

Operator

Our next question comes from Ryan Tunis with Autonomous Research.

Ryan James Tunis
Autonomous Research LLP

Just keeping on workers' comp, I had a couple there. First of all, I wanted to -- it sounded like in Rob's prepared remarks, you said that you guys are assuming negative trend. Is that true? Is the view into 2020, the trend is negative in workers' comp?

W. Robert Berkley, Jr.;President, CEO & Director

The answer is, yes, but very modest, very modest.

Ryan James Tunis
Autonomous Research LLP

Understood. And then I think, following up on the last question, clearly, workers' comp is a pretty significant piece of your top line. And you just talked about a little like the potential for reduction there.

I'm curious how much variability -- if we have another year of soft rates, I mean, could we see that book shrink by 25% or 50% or something more manageable? Where would we see that reduction first?

W. Robert Berkley, Jr.;President, CEO & Director

I don't think you're going to see it shrink that much that quickly. That's for starters. But what I would tell you is, I think, the upside in the rest of the portfolio and the momentum that we're seeing there is going to way outstrip the reduction on the comp front for us. So even with our underwriting discipline that we will demonstrate in all lines, including in comp, and the consequence of that will be that portfolio may continue to shrink, the growth that we will see in the rest of the business will significantly overshadow that.

Ryan James Tunis
Autonomous Research LLP

Got it. And then, I guess, going back to the discussion around the expectation that this quarter rate is an excessive trend, but Rob, you mentioned that for the past few years, you haven't been dropping your picks just because there's some margin of uncertainty out there. Should we take that to mean that if you're right, and it is an excessive trend here for 2020 that it might be more logical that where we end up seeing that or getting paid for that as shareholders could potentially be down the road in the form of favorable prior year development as opposed to in the near term on the accident year loss ratio line?

W. Robert Berkley, Jr.;President, CEO & Director

I think the answer is both. But no one's going to know that except through the passage of time. There's a lot of moving pieces out there, and that's what's sort of driving or creating the circumstance that we're navigating through. I think it's pretty clear that we are comfortably, again, outpacing loss cost trend. I think that we will be in a position over time to recognize that with a greater degree of confidence. But we're not going to go too early on that. We're not going to declare a victory prematurely. So do I think that it's going to come through? Yes, I do think it's going to come through. Do I think that as this year unfolds, we will have more and more evidence? Yes, I think we will have more evidence. And do I think that you will see that coming through, not over time just in development, but will you see that coming through in the current year? Yes, I think if things unfold the way we expect them to, you will see that. .

But again, we -- as we've shared with you all in 2019, in Q1, these are ex comp, we got 6.3% in Q1; in Q2, we got 5.4%; in Q3, we got 7.3%; in Q4, we got 8.9%. You can see the momentum is building, and we're going to watch that come through. And as it comes through and as there's clarity, we will take action. But we are comfortably convinced that it is going to come through. But even though we are comfortable, we are not going to respond prematurely.

Operator

Our next question is from Meyer Shields with KBW.

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

Two really quick questions. One, is there a risk of social inflation specific to workers' compensation?

W. Robert Berkley, Jr.;President, CEO & Director

Is there a risk to social inflation as it relates to workers' compensation? Yes, one could come up with ways that it could apply. But practically speaking, at this stage, benefits are clearly prescribed by each one of the states and as a result, it's pretty clear what that is and how that will be awarded and what those sums would be. To the extent that states decide to adjust those benefits more aggressively, yes, it's a possibility. But you got to remember, to a great extent because of how comp is priced off of payrolls, that's helping you keep up with certain types of inflation as well.

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

That's helpful. I was also wondering about on the frequency side, whether you could just be ramped up attorney advertising or something?

W. Robert Berkley, Jr.;President, CEO & Director

Yes, you see that. But generally speaking, the attorneys are not really chasing comp dollars. They're chasing auto liability, general liability, umbrella, et cetera, types of exposure or other capacity or coverage.

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

Okay, fantastic. And then second, so you sound, I think, very optimistic about growth prospects. I was wondering whether you could talk about reinsurance purchasing as a component of that as the fundamental profitability of business, fixed adds. Can we expect a change? Should we expect a change in the percentage of premiums that are used for reinsurance?

W. Robert Berkley, Jr.;President, CEO & Director

Well, obviously, we look at reinsurance as just another spend, and we try and be thoughtful about it. One of the benefits of our business because the vast majority of what we write are relatively modest limits that we are not captive to the reinsurance market, anything approaching like some others are. So there are some covers that are really important for us to buy, but there are certainly many covers that we buy that if we don't think they make economic sense anymore, we are not compelled to buy them.

Operator

Our next question is a follow-up from Amit Kumar with Buckingham Research.

Amit Kumar
The Buckingham Research Group Incorporated

Just 2 quick cleanup questions. The first question is on the discussion on the growth prospects and the opportunities you're seeing in both your E&S and primary. I know in the past, you've talked about your sweet spot, and you've said that where you can have limits, you try to go for $2 million or less and 90% of your book is that -- of your policies have that. I'm curious, based on the flow of new business showing up, has there been any thought process in terms of shifting those limits or maybe picking sort of a larger account size? Or maybe just help me understand are you letting all of that business pass by?

W. Robert Berkley, Jr.;President, CEO & Director

We write business that we feel like we have expertise in. That's sort of where it starts and where it ends. We, generally speaking -- well, we have tended to focus more on small accounts. But there are pockets of our business that we'll write some larger accounts. And we are an organization that is opportunistic. And each one of the people that run the businesses in the group and their respective teams understand the goal of the exercises, risk-adjusted return. .

So while our focus is on smaller accounts, and I don't expect that you will see our mix shift dramatically, certainly, there are components of the market that are feeling more challenged than others. And to the extent we think there are opportunities to deploy capital in those areas, we will do so. Fortunately, we have the people with the knowledge and expertise to do that in a thoughtful and responsible way.

Amit Kumar
The Buckingham Research Group Incorporated

Got it. The second follow-up was on the discussion on the GL line for the industry and the hard market. And in the past, you said we are 12 to 24 months away from a hard market. Has that time line accelerated since we've last talked about, just based on the level of issues that seem to be cropping up?

W. Robert Berkley, Jr.;President, CEO & Director

Yes. So I don't know when it was, that I said 24 months. I think what I was at least trying to suggest, if I'm thinking -- if I'm recalling it correctly, was I had referenced how perhaps commercial auto was towards the front of the pack, and how we saw property coming along. I think we offered some commentary on professional liability, D&O, in particular, really accelerating and making up ground and GL being a bit behind.

But I think what's happened is, as people are grappling with the broad circumstances that the market is facing, they are figuring out the GL -- the issues that they saw in auto and the issues that they saw in other places apply to GL, it's, A, it's coming into focus; and B, to people's credit, they're extrapolating from the noise they had in other lines and applying it to GL. So I think that while GL has been a bit the caboose, I think it's going to make up some ground quickly or it is making up ground quickly.

Operator

And we have a question from the line of Brian Meredith with UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

A couple of quick questions here for you. First, Rob, can you just talk about retail versus your E&S business? Are you seeing the same opportunities in retail, ex workers' comp, obviously? Is that market just as firming up as the E&S market and your Lloyd's business?

W. Robert Berkley, Jr.;President, CEO & Director

I would tell you, well, first of all, the vast majority of what we write on an E&S basis is outside of Lloyd's. So I think it's important to keep that in mind, though we do have a meaningful Lloyd's presence, and hopefully, it will be becoming more meaningful over time.

But the place that we're seeing the most extreme opportunity would be in the E&S space and a bit in the facultative market, followed by just the general specialty market, which is both E&S and admitted. And some of it is wholesale and some of it is retail.

Brian Robert Meredith
UBS Investment Bank, Research Division

Okay. So like I'm just thinking of your Continental Western Group, is that an area that you're seeing much rate activity?

W. Robert Berkley, Jr.;President, CEO & Director

So we're seeing opportunity there. But I would suggest to you that overall, they are not seeing the same type of opportunity in the regional businesses that we are seeing in our E&S businesses. But there -- it would seem as though they're catching up. It's accelerating.

Brian Robert Meredith
UBS Investment Bank, Research Division

Great. That's helpful. And then a second one, just a quick one, Rob. I recall, and you do have some exposure down in Australia. Anything that we need to think about here with respect to these Australian wildfires and exposure to those?

W. Robert Berkley, Jr.;President, CEO & Director

No. First of all, property is not a big part of what we do down there. And number two, based on what we've seen so far, obviously, it's a horrific situation, and our hearts go out to those that are affected on a personal level, but from a business perspective, while we may have a little bit of activity, it would really be just very modest, is our expectation.

Operator

And I am not showing any further questions in the queue. I would like to turn the call back to Rob Berkley for his final remarks.

W. Robert Berkley, Jr.;President, CEO & Director

Thank you, Carmen. We appreciate everyone calling in, and we certainly appreciate the questions. As suggested earlier, from our perspective, this is the type of market that we are built for. And we look forward to the opportunities that will continue to come our way. We think those opportunities will be accelerating from here. And we look forward to updating you in the coming quarters as to how we all are, as a team, capitalizing on those opportunities. Have a good evening.

Operator

And with that, ladies and gentlemen, we thank you for participating in today's conference call, you may now disconnect.