S&P Global
Market Intelligence

W. R. Berkley Corporation NYSE:WRB

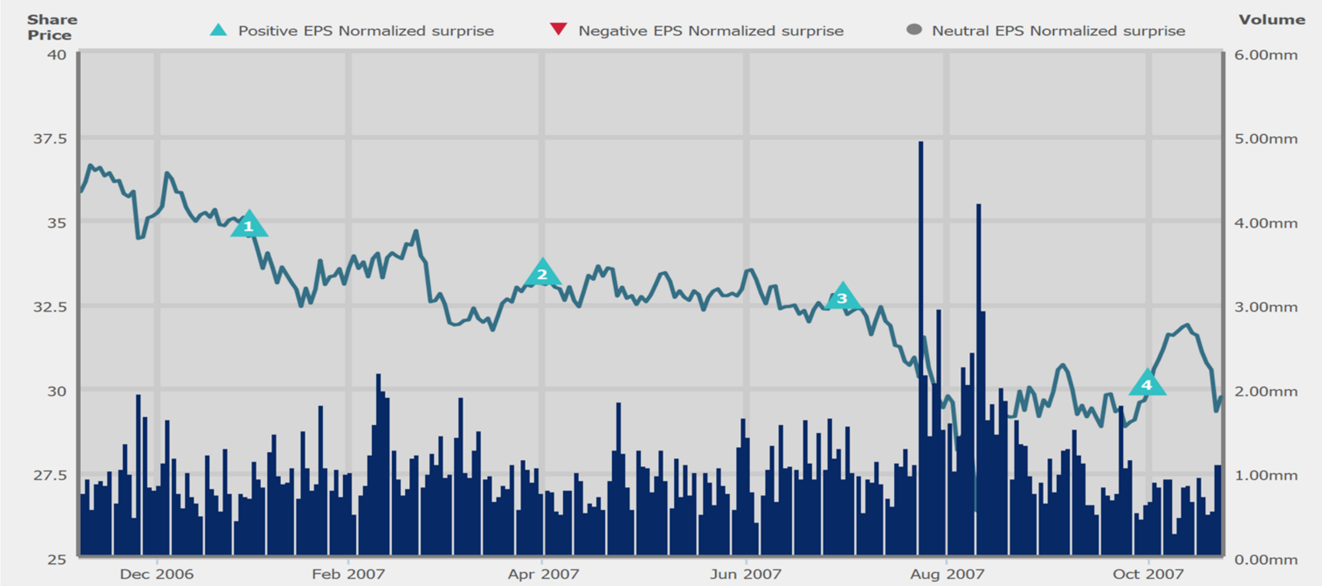
FQ4 2007 Earnings Call Transcripts

Monday, February 11, 2008 1:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2007-			-FQ1 2008-	-FY 2007-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	0.94	0.97	3.19	0.91	3.70	3.73
Revenue	-	-	2.05	-	-	-
Revenue (mm)	1371.94	1400.00	-	1383.50	5508.33	5553.64

Currency: USD
Consensus as of Feb-11-2008 1:10 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2006	0.88	0.98	10.11 %
FQ1 2007	0.89	0.91	2.25 %
FQ2 2007	0.91	0.92	1.10 %
FQ3 2007	0.91	0.93	2.20 %

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Call Participants

EXECUTIVES

Eugene G. Ballard

William R. Berkley

ANALYSTS

Brian Meredith
UBS

Charles B. Gates
Credit Suisse First Boston

Jay Cohen
Merrill Lynch

Joshua D. Shanker
Citigroup

Meyer Shields
Stifel Nicolaus & Co.

William Wilt
Morgan Stanley

Presentation

Operator

Good day and welcome to the W. R. Berkeley Fourth Quarter 2007 Earnings Conference. Today's 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, believe, expect or estimate. We caution you that such forward-looking statements should not be regarded as a representation by us in the future plans, estimates or expectations, contemplated by us will be in fact... will in fact the achieved. Please refer to our Annual Report on Form 10-K for the year ended December 31, 2006 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. Berkeley Corporation is not under any obligation or expressly disclaims any such obligation to update or alter its forward-looking statements, whether as a result of new information, future events or otherwise.

At this time, I would like to turn the call over to Mr. William R. Berkley, Chief Executive Officer and Chairman of the Board. Please go ahead sir.

William R. Berkley

Hi. We are very pleased with the quarter and with the year. I think that recognizing that our results continue to strengthen and our results continue to be excellent. Overall, we are pleased with where we stand. The market is getting softer without a doubt. Prices are down year-over-year, something approaching 5%. This is on top of the decline last year of a little more than 3%, so you've had decline in price for 2005 to now of about 8% on average. It varies from prices actually increasing in some lines of business, to be down somewhat more than 8% over the past two years. But there was... there is lots of margin, business still continues to... with the... written at... underwriting profits although, things are certainly moving in the wrong direction at the present time.

Before I talk about each areas of business, I am going to let Gene Ballard, our Chief Financial Officer, talk about our financial results.

Eugene G. Ballard

Okay. Well as Bill said, we've finished 2007 with another strong quarter. Our operating return on equity was 22% which makes more than five years of consecutive quarters with an ROE above 20% and our operating income per share was $0.97, that's up from $0.96 a year ago.

For the full year, our operating earnings per share were up 9% at $3.73, which is also a return on equity of 22%. Our per share earnings reflect the impact of our ongoing stock repurchase program and the repurchase of 15.2 million shares in 2007 of which 3.2 million shares were purchased in the fourth quarter. The average cost of those shares was $30.12 for the full year and $28.93 in the fourth quarter. We still have 16 million shares available for repurchase under the repurchase authorization.

Our net premiums written were $1.1 billion in the fourth quarter, which was an overall decline from 5.5% from the prior-year period. But if you look at all the businesses other than reinsurance, you will see that they performed much better than the average of the modest decline of 0.3% in the quarter.

The regional and international premiums were up 3% and 23% respectively, while the Specialty and Alternate markets premiums were down 5% and 4% respectively. Reinsurance business on the other hand has been much more competitive in both the treaty and facultative market and our reinsurance premiums were down 30% in the quarter. We have seen significant declines in reinsurance business throughout 2007. Our treaty premiums for all of 2007 were $287 million, down 15%; our facultative premiums were

$224 million, down 12%. Lloyd's premiums were $131 million, down 10% and all other reinsurance premiums where $40 million, down 25%.

Our overall loss ratio was 58.9% in the fourth quarter compared to 59.6% in last year's fourth quarter. Reserve releases in the quarter were $34 million, compared to reserve increases of $7 million in the preceding year quarter. And for all of 2007 reserve releases totaled a $105 million, with most of that coming from the Specialty segment. That compares with reserve increases at $27 million for all of 2006.

Weather-related losses were minimal in the quarter at $3 million, down slightly from $8 million a year ago and our paid-loss ratio was 46% in the fourth quarter, 42% for the full year, as our loss payments continue to run well below our expected loss payouts.

At year end 2007, our net loss reserves were $7.8 billion which is an increase of $221 million for the quarter and $875 million or 12% for the full year. IBNR reserves were $4.7 billion and now represent 60% of our overall reserves and approximately 100% of our earned premium for 2007.

The expense ratio was 29.8% in the quarter, compared to 27.4% in the prior year. That increase reflects the impact of lower premium volume as well as higher accruals for contingent commissions and the continuation of start up cost for some of our new business. So, overall our combined ratio was 88.7 for the quarter with combined ratios by segment of 85.3 for specialty, 90.9 for regional, 85.4 for alternative markets, 97.4 for reinsurance and 87.9 for international.

The carrying value of our investment portfolio was $13.2 billion at the end of the year. That includes $11 billion of fixed income securities, $855 million of arbitrage securities and approximately, $1.3 billion invested in common and preferred stocks and in partnerships and affiliates.

Our municipal holdings made up approximately $5.2 billion of fixed income investments at year end. And you'll see on page nine of this quarter's earnings release that we have showed... shown the ratings profile for the municipal portfolio. Approximately half of the municipals are uninsured and have an average rating of AA plus. In the other half that is insured, has an average rating for the underlying security, that's without considering any insurance enhancement, of AA minus. And the aggregate for all the fixed income cum securities, the average rating with insurance enhancement is also AA plus and without enhancement is a straight AA.

Page nine also presents some details on the residential mortgage-backed securities which totaled $1.6 billion at year end and as the schedule shows, most of those mortgage-backed securities were issued by government or government-sponsored agencies and there are no sub-prime exposures. Our earnings from the investment portfolio were $173 million in the fourth quarter, up 5% from a year ago. The average yield on the overall portfolio was 5.3%, down from 5.6% in the prior-year quarter.

On the tax equivalent basis that is adjusting for the tax benefit of municipals, the average yield is 6.1% for both of fourth quarter and the full year. For the arbitrage trading account, the average yield was 6.8% in the quarter down from 11.8% in the prior-year period. And the overall duration of the fixed income portfolio was 3.4 years at year-end. On a cost basis, the carrying value the portfolio increased 11% for the year, as our operating cash flow continues to be strong with the cash flow of $350 million in the fourth quarter and approximately $1.5 billion for the full year. Of course, both investment and investment income are less than they otherwise would be, as a result of the stock repurchases which totaled $450 million. All that gives is an ROE of 22% and a growth in book value per share, again after stock repurchases of 14% on a pro forma basis adjusted for the stock repurchases, book value per share grew by 19%.

William R. Berkley

Thanks Gene. Unfortunately I might add that while we believe over a period of three or four years, stock repurchases benefit all those individual numbers, in the short run they do tend to confuse them and in some cases have an adverse impact.

Let me try and take you through the general outlook about our business, first by segment and then overall. Specialty business, a very competitive, it is the place where the business now is being entered by new competitors. Lots of the people in Bermuda who were primarily reinsurers who decided specialty business is attractive and the marginal specialty business is now being entered by the standardized companies, who soften their underwriting standards to accept certain kinds of risks that heretofore were viewed as not acceptable and went to the excess in surplus alliance market. So it's a place where we're concerned about our volume.

The reinsurance business has been the first place where volumes has been hit as Gene mentioned and it's an easy place to just enter and in both those areas, it's not only pricing that's gotten soft but terms and conditions, especially things moving over from the E&S market to the standard markets. The terms and conditions of the policies are substantially different. So, it's much more attractive to move to that standard market. The same is true in the reinsurance market. People are accepting business without the kinds of safeguards and verifications that we think are necessary. So reinsurance down substantially in premium volume and we see our specialty business beginning to be impacted on a greater level than our standard market business.

Regional business pretty much holding its own, prices are down modestly, very modestly probably less than 1% overall. We are pretty pleased with where they stand. The biggest risks in that market are being impacted the most, the smaller risks the least. But that business continues to do well and hold its own.

Alternative Market business; the core parts of the business continues to do well. The service areas where we're managing assigned risks plans and so forth are being adversely impacted, because when you are in a softening market, less business goes with the assigned risk plans. So you're seeing business we leave there.

In the International area, we are pleased with the results and we are holding up well in Argentina. Berkley Europe continues to do well, although pressure there is beginning to increase and we're seeing London markets becoming more competitive. Overall, our new businesses which are spread amongst a number of divisions are contributing to our business, but not in enormous amount. They are inline with our expectations with almost everyone at/or exceeding our expectations with one exception.

Overall, we think business will be okay for us for 2008. We think our returns are clearly going to go down. It'll be struggle for us to make 20% return and it's certainly is going to be difficult. We're not ready at this point to make a forecast, although we're optimistic that business will continue to be good. 20% is what we're hoping for the year. But at this point in time, investment income softer, how many shares will we repurchase, there's lots of issues out there. We're pretty comfortable where we stand however.

I think that our balance sheet at the moment is not particularly leveraged. Our capital account is strong. We've continued to list the crises that have affected many of our competitors. In the case of sub-prime, not only do we have no consequential investments in sub-prime, not only did we avoid some of those kinds of risks, but from an insurance point of view we have no consequential exposures as far as we can see.

I think a lot of people have said we have no exposure and if you'd listen to everyone in greater composite that means there'll be no losses in the insurance industry for sub-prime which is not what we think. But we think that the losses will be focused on financial institutions. They will be focused on mortgage brokers and real estate agents and those kinds of things and we don't have a lot of exposure in those areas. I am sure we will have some losses as will every insurance company in some way or other, because it's likely the losses, like every other kind of very large loss, people will be searching their pockets to contribute. We don't think it is going to be of anything substantial for us.

In general, we are pleased with the year. We are pleased with the quarter. The environment is going to continue to get more competitive. We continue to look for niche opportunities where we think we can find ways of doing business. We see them out there, whether we can do transactions or expand into those areas. One never knows, but we are optimistic that we will be able to continue to deliver outstanding returns.

With that I am happy to answer any questions.
Question And Answer

Question and Answer

Operator

Thank you. The question-and-answer session will be conducted electronically. [Operator Instructions]. And we will take a question from Charles Gate with Credit Suisse.

Charles B. Gates
Credit Suisse First Boston

Hi, good morning.

William R. Berkley

Good morning, Charlie.

Charles B. Gates
Credit Suisse First Boston

I have three questions, two are numbers questions. My first; the reduction in reserves for earlier losses during the period were $34 million?

Eugene G. Ballard

Yes sir.

Charles B. Gates
Credit Suisse First Boston

Okay. The second, I didn't understand footnote number two, on page six of your news release?

William R. Berkley

Footnote number two on page six. The fourth quarter weather-related losses were $3 million and $8 million, respectively. For the full year of 2007 and 2006, weather-related losses were $34 million and $39 million, respectively.

Charles B. Gates
Credit Suisse First Boston

I guess we are in a different footnote number, right? The one where it shows representing insured bonds for which the underlying securities are not rated?

William R. Berkley

No, it's not on page six.

Eugene G. Ballard

Page nine.

Charles B. Gates
Credit Suisse First Boston

I am sorry.

William R. Berkley

You might have read the page digit as upside down. Okay. Represents insured bonds for the underlying securities that are... well there is some... we see number two, the $155 million.

Charles B. Gates
Credit Suisse First Boston

Got you.

William R. Berkley

Those are not rated, but there are a number of people who have issues with the bonds don't get rated for some reason or other. Frequently, when they get rated, they are put behind a guarantor or there are small issues, but the same issuer has a rated bond with the same characteristics. So it would be that where we have an identical issue or with the same exact terms, conditions and so forth, but they didn't get that peculiar bond rated for some reason or the other.

Eugene G. Ballard

And the other thing I would like to add to that Bill is, on the table we put those in the NR category, but when we calculated the overall average rating for the portfolio, we treated them as BBB minus. So, which is very conservative, we didn't give tem a zero for non-rated but we treated them with a very conservative rate, even tough we consider them all to be investment grade, based on the ratings of similar securities for the same issuers.

William R. Berkley

In other words, what we did was sort of confusion. And that is when we took the ratings for the comparable securities with the same terms and conditions, it would have been A. But since we were making the assumption that, that would be the ratings we chose to use a lower rating for the average, because the accountants want to be conservative. But it wouldn't have changed the average Charlie, if they had used that as they assured me. But it wouldn't have gone to higher than a AA, whether they used an A or BBB minus, the average would have been AA.

Charles B. Gates
Credit Suisse First Boston

Could you elaborate... this is my third question, could you elaborate on the comment that you made in your prepared remarks about standard market companies seeking to build basically positions in excess and surplus volumes. It was... the Bermuda Company is doing the same thing.

William R. Berkley

Well, first of all they really do two different things. The Bermuda companies are trying to get in the excess and surplus lines business, through wholesalers just in the same way we are in this business. The standard markets are doing some thing different. They are trying to extend or by amending the kind of underwriting guidelines they use; for example, a simple example would be, someone who write restaurants but they don't write sushi restaurants, because if you sell sushi, you have certain inherent additional exposures because of raw fish and all that.

Well they took away the exception we don't write sushi restaurants, that which would have in the past gone into the E&S market, they now totally become qualified for the standard markets. A health club is where probably not really in the standard market, they were marginal. So in 2006 they have decided that health clubs were okay and in 2007 they decided health clubs and tanning machines were okay. So what they are... is they're changing their underwriting guidelines to allow things that have heretofore have gone into the E&S marketplace, come back into the standard market.

The real problem is that they are charging standard market rates. So, what will ultimately happen here is they are going to charge for that risk half or even a quarter of what the E&S market would have charged. So, it will prove to be unprofitable in a few years and will go back into the E&S market.

Charles B. Gates
Credit Suisse First Boston

If you were an analyst and you were sitting here in New York, how would you attempt... and it's my last question, how would you attempt to monitor them?

William R. Berkley

Well, first of all, you told me you're going to ask three and now you asked a fourth.

Charles B. Gates
Credit Suisse First Boston

I apologize.

William R. Berkley

But that's all right. Second of all, I think it's a very difficult thing to monitor. I think that the most important thing to look at it is if you see someone growing substantially, you probably have to start to ask more questions. This is not a market where growth is going to be attainable very easily. When you see the overall insurance marketplace declining by 5%, 6%, which is what price declines are, it's difficult to grow, but it can grow. You can add new lines of business, you can expand, you can buy things and there are opportunities. But anyone who is growing I think requires or analysts ask a lot more questions.

Charles B. Gates
Credit Suisse First Boston

Thank you.

Operator

And next we'll move to Meyer Shields with Stifel Nicolaus.

Meyer Shields
Stifel Nicolaus & Co.

Thanks, good morning. I am trying to think how to ask this. Is the underwriting cycle that we're in now, deteriorating faster than previous cycles?

William R. Berkley

No, I don't think it's deteriorating faster. I think there are a couple of things that are happening that are different. I think first of all many people are releasing reserves much more quickly. So you're seeing the historic redundancies coming out more quickly, because people are worried about redundancies. I think that there is less total craziness. There is not anyone out there whose being a lunatic at the moment. There are people who are being aggressive. I think that what people haven't figured out is that in a general sense, if your price is down 8% over two years and inflation of let's just say 6, 7 or 8, you have 15% change in pricing and that means it's going to be very hard for many companies to report underwriting profits and investment income especially if you have any kind of a short-term portfolio. It's going to be at pretty low levels.

So I think that we have very quickly gone to where profitability for certainly average underwriting companies is going to be gone in 08. I think good underwriting companies will still have good profitability in 08, but not as good as it was. So I think the end result of those things is the cycle will take people down and I think there are going to be people who will generally be reporting numbers more quickly and more accurately and I think that's a part of the results to Sarbanes Oxley. But I think you are unlikely to get this huge build-up of short reserves that you've seen in the past. And I think that because of how bad things were in the last cycle in 99 and 2000, I think there is a lot more attention being paid to the situation, in this case.

So I think overall, I don't think the business itself is any different. I think how it's reported and how people are reacting is a bit different. I think that there is a lot more people looking at things with mathematical models which creates their own problem. Though, I think that you are going to see more truth in labeling and I think that's going to make the cycle to be more honest. So it will look like it's happening more quickly.

Meyer Shields
Stifel Nicolaus & Co.

Thanks for great thorough. With regard to the Bermuda coming into the specialty lines through the wholesale brokers, is there any... can you just talk on, maybe changing the compensation structure for the wholesale agents that are competitive too?

William R. Berkley

I think that I am sure some of the wholesale brokers would like that's be the case, but I think that it's in our best view not something that's here now and we certainly are not going to consequently change the compensation of wholesale brokers.

Meyer Shields
Stifel Nicolaus & Co.

Okay.Thank you so much.

Operator

And Brian Meredith with UBS will have our next question.

Brian Meredith
UBS

Good morning, couple of quick questions here. First, on the reinsurance; there was anything unusual in the quarter as far as unearned premium going out or something just because there's a big drop off we saw underwritten in the year and the expense ratio popping up a little bit?

Eugene G. Ballard

Yes and the expense ratio I think which had more to do with contingent commission accruals.

William R. Berkley

Contingent commission accruals, right. Yes, I think we had a substantial contingent commission accrual on some of that. But I think that there wasn't a lot for... I think that, or generally speaking I think that we have really been pretty selective about getting out of certain segments of the reinsurance business and the facultative area much to our surprise was softer than we would have expected.

Brian Meredith
UBS

And following up on that Bill, are you yourself trying to take the opportunity to actually buy additional reinsurance you had won. I mean is there... we're getting to the point in the market where you can arbitrage the reinsurance marketplace, given what's going on with terms conditions in pricing?

William R. Berkley

Well one of the problems with arbitrage reinsurance is you have to have reinsurers who have the capacity to pay them.

Brian Meredith
UBS

Okay.

William R. Berkley

And a number of people have tried that and haven't always paid. I think that there certainly are some aggressive reinsurers who will be around and as you can do that. But we don't think the best strategy to follow at the moment. But even if we do, we wouldn't say it because then we couldn't do it.

Brian Meredith
UBS

Understood. And last question, looking at your loss picks for 2007, looks like they are roughly 150 basis points on average across the company. Given that pricing continues to deteriorate here and maybe a little bit quicker than it was part of 07, should we expect loss picks kind of similarly to go up by 150 and maybe even worst than 200 basis points in 08?

William R. Berkley

Yes, first of all I think, there are of more than 150 points. You have to adjust the fact that we try and take out any what we think would be redundancies from the prior years. So I think our loss picks are probably up more like 300 basis points than a 150 to where we thought to be and maybe in some cases as much as 400 basis points. We think that probably sort of reflects where we think our pricing is at the moment, recognizing that some of that is our best estimate from where we look on our expected redundancies that we're pretty confident though. If anything, we think that our current loss picks and the ones for 2005, 2006 and 2007 continues to be parts of services.

We're always looking for something bad to happen and just because something bad hasn't happened doesn't mean they won't. And one of the things we pride ourselves on is we in spite of what some of our people will evaluate our company for rating agencies, I think we have an embedded risk management system that is everyone who works for us and who runs the company is scared to death of being stupid. So we try very hard to look ahead and I think that we are concerned that there is something bad out there, because that's been the history of the industry.

Brian Meredith
UBS

Okay, thank you.

Operator

And next we'll move to Bill Wilt with Morgan Stanley.

William Wilt
Morgan Stanley

Hey, good morning.

William R. Berkley

Good morning.

William Wilt
Morgan Stanley

Couple questions. First California workers comp, looks like data coming out of the WCIRB late last year showed an upward inflexion point in medical loss trends and in California workers comp. I was wondering if you are seeing the same thing or have any observations about trends, medical trends in the workers comp plan?

William R. Berkley

In general medical costs overall in the whole industry have been the real risk Bill for cost inflation, the overall inflation's been zero. 1.5% or 2% of medical inflation has been 6%, 8%, 10% depending on where and what. Certainly better cost inflation in California is substantial, is a concern. There is lots of stuff going on. Everybody is worried about the impact in California. I would say in general, things have in fact stopped getting better in California and they are getting somewhat worse, since prices have come done and it's still a profitable line of business. It's just not as wonderful as it was.

On the other hand if you go back prior to sort of 2002. It was a pretty terrible line of business for a long time. I guess on average, it's probably been a breakeven line of business. In the aggregate to the prior kind of 15 years and now it's reasonably and rationally profitable, but it's not wonderful results that we saw for a few years.

William Wilt
Morgan Stanley

Okay, that's great. And the second one very general question, Bill how do you think about the intersection of... sounds like a rapidly softening market and arguably I guess the rapidly, softening economy in what term. What were the risk factors are hiring your radar screen, softening the terms and conditions. I don't know what's claiming behavior of policy holders, changes during an economic downturn. But, in general how do you think about the intersection of those two or confluence of those two events?

William R. Berkley

I think clearly there is real concern and I think in general our industry is less impacted by a softening economy than most industries. However, I would say the place that's most impacted is generally property markets and arson claims and those kinds of things increased. It's not a significant part of our business. But there are other claims, there is stuff that happens they will have an impact. I think it requires more careful examination, I think specially important are things like workers compensation where you have historically picked up lots of premium, some audit premiums and you are not going to get back.

So you are not going see the boost in the fourth quarter or the first quarter that may come about from audit premiums and when you're looking and expecting historic results, that's going to probably be a change from your pattern, because this is not expanding. I think that clearly you are going some claims that are more difficult to resolve because of the financial difficulties of your payments and/or your insurance. I think it will have some impact, unless it's an extended recession, it's not going to generally be a huge impact. But my guess is it will be a modest impact on top of the declining profitability. So it's likely that it will make the second half of 2008 worse than it would have been otherwise and that's assuming we have a modest recession. But if we have a severe recession, it will start to have a greater and greater increase.

William Wilt
Morgan Stanley

That's great, thank you. And if I may, one last numbers I want; Eugene, just the reserve releases this quarter by segment of the $34 million?

William R. Berkley

We generally don't go through that. On the converse, well Bill I am sure Gene will go through whatever you'd like if you give him a call.

William Wilt
Morgan Stanley

Perfect, thanks.

Operator

[Operator Instructions]. Next, we move to Joshua Shanker with Citi.

Joshua D. Shanker
Citigroup

Good morning.

William R. Berkley

Good morning, Josh.

Joshua D. Shanker
Citigroup

Two questions; the first question is that if we continue to see declining of volumes for your business at 5% to 10% over the next one or two years, what's that going to do to your expense ratio and the second question relates to something you answered with Meyer, you said that average companies are probably producing underwriting loss this year. Do you think this year is a year for industry underwriting loss, given a normal distribution of storm activity?

William R. Berkley

If you have a normal distribution of storm activity, I would say it's underwriting breakeven to underwriting loss, for the industry as a whole. Well, first one, as underwriting profits decline and even though I think we will have an underwriting profit this year, we will be paying less contingent commissions. Number two; well we don't plot and fire people, that's not what we do. Everybody here is conscious that you can't ignore your expenses when volume goes down, and from our offices here that everyone of our operating units people are quite conscious that expenses are something we need to be cognizant of. Our positions are getting filled and we're attempting to examine what we do and how we do it. There are some expenses from start ups that we're just prepared to eat. But that's really the price of starting things instead of buying them. It doesn't help in the short term, our incomes reported... as reported, but it gives us more confidence in expanding new businesses for the next half cycle. But overall we are far more conscious of expenses as our ability to generate new volume declines.

Joshua D. Shanker
Citigroup

Is there some kind of ceiling for expense ratio that we can think about in terms of the way you do your business?

William R. Berkley

I'm not sure what you mean.

Joshua D. Shanker
Citigroup

I mean, clearly it goes up as your have less business and of course you're trying to monitor that. But is there a cost of doing business ceiling I guess, like I mean, you don't expect your expense ratio could go up another 300 basis points?

William R. Berkley

We would be very disappointed, I think that if we try... when all else fails, we direct the people and the operating unit to what to do, but at the moment what we do is tell them this is an issue and we try and persuade them to understand the issue and to get focused on it and let them decide how or they're going to do. I think that before it comes to that point, we probably would step in and be more directive. I think one of the cornerstones of trying to have a decentralized operation as we do is not only giving the authority, but conveying the idea that people have the responsibility to deal with these issues. It's a hard thing because nobody likes to not hire people, nobody likes to fire people, nobody likes to say no ways, nobody likes to do that stuff. We started a year and a half ago telling people this was going to be an issue, this is going to be a problem. They know, we're very serious and I think that I'm not particularly concerned that it's going to be out of control at all.

Joshua D. Shanker
Citigroup

: Okay well, thanks there.

William R. Berkley

But I can assure you, long before it gets up 300 basis points, we will start, we will end up... we wouldn't be tugboat anymore, we will be lashing people to the decks.

Joshua D. Shanker
Citigroup

I'll wait for that.

William R. Berkley

I hope not.

Joshua D. Shanker
Citigroup

Very good, very good. Thank you.

Operator

And next we'll hear from Jay Cohen with Merrill Lynch.

Jay Cohen
Merrill Lynch

Yes, two questions and maybe they're related and maybe they're not. The first is Bill, when you talk about the industry and pricing created inflation, you made an assumption on claim inflation but clearly one goes back one two or three years on the liability side and the claims inflation has been much more modest than what you talked about. So I'm wondering what your view is on underlying claims inflation on the liability side? And then secondly or qualitatively how do you feel about your loss reserves today of year end 07 versus year end 06?

William R. Berkley

Well first of all the answer is of course do relate because the reason our loss reserves are conservative is because we make conservative assumptions about inflations, because we don't want to be wrong. And the reason our assumptions are more conservative than everyone else is reporting is because we think medical cost inflation is built in at a higher level than some of my competitors think. So we think 6% or 8% for medical cost inflation is probably an okay number, which means you take on a smaller number for real cost inflation and then you put in 6% or 8% of medical costs and you come up with a higher inflation number for claims.

We don't have an answer per se, but I think that we would tell you that our reserves have become more adequate over the past few years, because the risks of inflation and the risks of bad things happening have increased. I have the view that our reserves are probably somewhat redundant, but the nature and the process of our establishing reserves includes a lot of weight, although not a 100% weight on the financial officers, the actuaries and the presidents of our operating units. The ultimate decision is made here but we have to feel very strongly. Our actuarial team here, our financial team here, the people who operate the units, myself and Rob, we have to feel very strongly that things have gotten to where the redundancies are just overwhelming.

The numbers would tell you that if you went back to 2002, our numbers would be... the IBNR would be about between 80% and 90% of our earned premium. But things have changed from 2002. The risks of inflation are greater, the other risks are greater, but it says that we are probably more cautious. But being more cautious is appropriate, when you are in these uncertain economic times. So yes, we've made some more cautious assumption than history might say, it's based on what we see is medical cost what we see is the risks of inflation. That's why we are concerned about as out liberal court turned as opposed to conservative court turn. It's our effort to have enterprise risk management, to try and say what are things aren't as we think they are going to be. What can go wrong? That's what our job is to be sure that is things go wrong, we are not stuck. So yes, we are probably a bit more cautious and conservative than some others.

Jay Cohen
Merrill Lynch

Thanks Bill.

Operator

And we'll take a follow-up question from Charlie Gates with Credit Suisse.

William R. Berkley

Mr. Gates.

Charles B. Gates
Credit Suisse First Boston

I am still here. I have my phone on mute. Hey, the one question that I had was, given the ...

William R. Berkley

Charles, this is your fifth question.

Charles B. Gates
Credit Suisse First Boston

Yes, I apologize. Hey, years ago I followed a company, where if you'd ask the CEO what the stock price was, he wouldn't have been able to answer. Clearly you are something different. Here is the question. Given the pressure on your stock, I would have foreseen that you would have bought back more stock during the period, than you did.

William R. Berkley

Well here I think that where... we bought back $450 million worth of stock last year that we bought back 1 million on a 1.3 million shares this year. So far, we certainly welcome if anybody is on the phone has a flock of stock they want to sell us, give us a call. We are happy to make a bid for block a little, there are all kinds of restrictions. How we buy, how much we buy, so you have to remember Charlie on the day when everyone wants to sell, we only can buy 375,000 shares that they eventually call as the day, I didn't say tomorrow we would like to sell your block at stock.

So we can't always buy everything we want. There are all these restrictions on how you do and how much do and all that stuff. If we were able to buy on the days everybody wants to sell, we buy a lot more stock. But there are other people who want to buy the stock too and we try and use our best judgment on when to buy the stock and where? I don't think the stock has been under any particular undue pressure. We certainly... and yes, I own 28 million shares. So I do have a vested interest.

Charles B. Gates
Credit Suisse First Boston

Thank you.

Operator

And we'll take a follow up question from Meyer Shields with Stifel Nicolaus

Meyer Shields
Stifel Nicolaus & Co.

Thanks, Bill earlier you said that you think that company is going to see deteriorating underwriting results at the year-end including some breakeven.

William R. Berkley

I said, I'm sorry?

Meyer Shields
Stifel Nicolaus & Co.

That on an industry-wide basis we expect either breakeven or modest industry-wide loss?

William R. Berkley

Yes.

Meyer Shields
Stifel Nicolaus & Co.

Do potential sellers of small insurance companies recognize that in the pricing expectation?

William R. Berkley

The problem isn't whether they recognize or not, the problem is do they recognize how they priced the business yesterday in their loss reserves. I think the answer is many people are still very optimistic about the level of business, where business is and I think at the moment there is probably more optimism in general than is wanted. Most of the companies for sale are being sold because people say taxes are going to change, the environment is worse, insurance cycle is worse, I want to get out and they think that the buyer doesn't know any of those things. So, their pricing for sales is not that realistic. But in fact that will change. We just need to give it a little time and then I think some of the issues, Bill Wilt brought up which is difficult at time, we will make the insurance business a bit more difficult and prices are declining still and that's going to make it more difficult. So, my guess is that people who want to sell and who care about their companies will hear from us. But it's hard to find good companies at rational prices. Hello?

Operator

This line is still connected.

Meyer Shields
Stifel Nicolaus & Co.

No I am fine thank you

Operator

There are no further questions. I will turn the call back over to Mr. Berkley for any additional or closing remarks.

William R. Berkley

Okay. Well I thank all of you. We are real pleased with the quarter, we are quite optimistic about the year. We think that 2008 will be an excellent year. As they say, at this moment we're still optimistic that we can get to that 20% return. But it's certainly not a sure thing with a huge number of variables in the economy and in investments returns. So we're going to wait and see we will update you as we get into the first quarter further. Thank you all very much. Have a great day.

Operator
And that will conclude today's call. Thank you for your participation.