S&P Capital IQ

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Arch Capital Group Ltd. NasdaqGS:ACGL

FQ1 2016 Earnings Call Transcripts

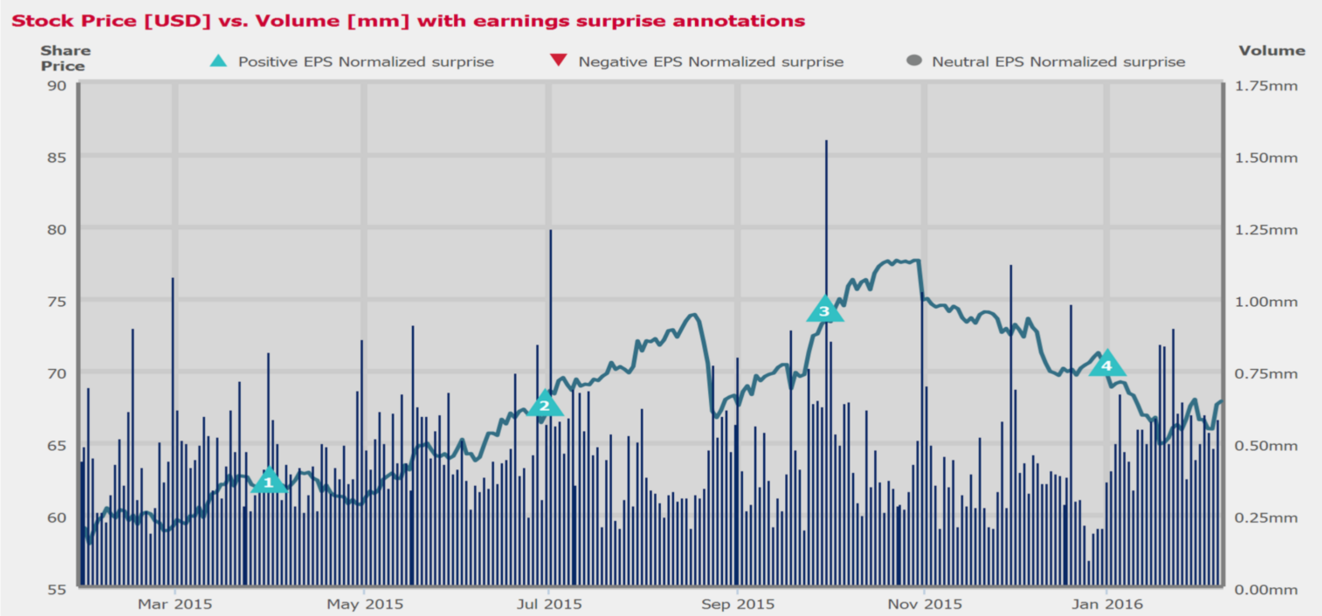
Thursday, April 28, 2016 3:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2016-			-FQ2 2016-	-FY 2016-	-FY 2017-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.10	1.17	▲6.36	1.03	4.17	4.27
Revenue (mm)	1028.31	1121.24	▲9.04	976.00	3990.00	3981.29

Currency: USD

Consensus as of Apr-28-2016 1:00 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2015	1.08	1.17	▲1 8.33 %
FQ2 2015	1.07	1.16	▲2 8.41 %
FQ3 2015	0.96	1.01	▲3 5.21 %
FQ4 2015	1.06	1.15	▲4 8.49 %

Call Participants

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President and Chief Operating Officer

Mark D. Lyons
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Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Arch Capital Group First Quarter 2016 Earnings Conference Call. [Operator Instructions] As a reminder, this conference is being recorded.

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

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

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

Management will also make reference to some non-GAAP measures of the financial performance. The reconciliation to GAAP and definition of operating income can be found in the company's current report on Form 8-K furnished to the SEC yesterday, which contains the company's earnings press release and is available on the company's website. I would now like to introduce your host for today's conference, Mr. Dinos Iordanou, Mr. Marc Grandisson and Mr. Mark Lyons. Mr. Iordanou, you may begin.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Thank you, Abigail. Good morning, everyone, and thank you for joining us today for our first quarter earnings call. We're starting the year on a good note of first quarter. It was terrific from virtually all perspectives. Our reported combined ratio was excellent at 87.1, which was aided by low level of catastrophe losses and continue favorable loss reserve development in each of our segments.

Investment returns were also very good as our fixed income portfolio benefited from the interest rate declines we saw in the first quarter. There are no significant changes in the property casualty operating environment from last quarter, although there are some signs that reinsurance terms, especially ceding commissions may be bottoming out. Within the insurance sector, we saw slight deterioration in terms and conditions, while the mortgage insurance industry remains quite healthy. We're in a market where the importance of cycle management, not only in preserving capital, but also maintaining balance sheet integrity is paramount. Navigating through this phase of the cycle requires that our underwriters remain disciplined, opportunistic and laser focused in execution.

Within the reinsurance segment, we are focusing more on special situations that utilize our underwriting expertise and capital strength and our ability to respond quickly. In our insurance segment, we continue to focus on less volatile smaller accounts, both in term of limits, but also account size, and with reinsurance purchases, helping us to reduce the volatility on large accounts and our high-capacity business.

The operating environment in the mortgage insurance space remains healthy, and we're generating excellent returns and continue to make significant progress in the segment. Marc Grandisson will give you more details in all of our segments in a few minutes.

On an operating basis, Arch earned $145.7 million or $1.17 per share for the first quarter of 2016, which produced an annualized return on equity of 9.7%. On a net income basis, we earned $149 million or $1.20 per share for the 2016 quarter, which results in a return of equity of 6.4% on a trailing 12-month basis.

Remember that net income movements can be more volatile on a quarterly basis as these earnings are influenced by changes in foreign exchange rates and realized gains and losses in our investment portfolio.

Groupwide, our gross written premium increased by 6% to $1.39 billion in the first quarter over the same period in 2015, while net written premium rose 3.7% to $977 million, driven primarily by growth in our mortgage segment along with modest growth in our construction and alternative market business within the insurance segment.

Our investment results were excellent on a relative basis and acceptable on an absolute basis, given financial market conditions. Net investment income per share for the quarter was $0.57 per share, up $0.04 sequentially from the fourth quarter of 2015. Despite volatility in the investment and foreign exchange markets, in the first quarter of 2016, on a local currency basis, total return on our investment portfolio was a positive 1.48%, as returns on our fixed income investments were partially offset by declines in our alternative investment portfolio. Including the effects of foreign exchange, the total return was 1.82 in the quarter, a healthy result.

Our operating cash flow was $257 million in the first quarter as compared to $16 million in the first quarter of 2015. Mark Lyons will discuss the cash flows in more detail in a few minutes.

Our book value per common share at March 31, 2016, was $49.87 per share, a 40% increase sequentially from the fourth quarter of 2015.

We -- while some segments of our business have become more competitive, we believe that groupwide and on an expected basis, due to our mix, the present value ROE on the business return in the 2016 underwriting year should produce ROEs in the range of 10% to 12% on allocated capital.

Before I turn the call over to Marc Grandisson, I would like to discuss our PMLs, which remain essentially unchanged from January 1. As usual, I will like to remind and point to everybody that our cat PML aggregates reflect business bound through April 1, while the premium numbers included in our financial statements through March 31 and that the PMLs are reflected net of reinsurance in all retrocessions. As of April 1, 2016, our largest 2015 year PML for a single event remains the northeast at $494 million or about 8% of common shareholders' equity. Our Gulf of Mexico PML decreased slightly to $438 million and our Florida Tri-County PML increased slightly to $385 million. I will now turn it over to Marc Grandisson for comments on market conditions before Mark Lyons discuss our financial results. And after their comments, we will take your questions. With that, Marc?

Marc Grandisson
President and Chief Operating Officer

Thank you, Dinos. Good morning to all. We continue to face the challenges of softer pricing as property casualty industry continues to report favorable prior year loss developments and benefiting from below average cat losses, which obscures we believe the adequacy of risk-adjusted rates in the property market. However, in every market, there are some dislocations present and we remain vigilant in our efforts to seize those opportunities that become available. On the positive side, as Dinos mentioned, recent actions by a few large participants in the marketplace may help to usher in a more disciplined environment in the casualty area in the near future.

P&C rates are declining in the mid- to low single digit range, but there are pockets of rate strengthening. Our challenge is to be confident at current rate level or sufficient on an absolute basis.

On the other hand, in mortgage insurance, which I will refer to as MI from here on, rates remain very healthy despite indications that they appear to be declining in light of the new rate cards filed by some of our competitors. Despite the headlines, we believe that on a risk-adjusted basis, the aggregate effective rate levels of MI providers are actually higher due to a shift in the quality of the risk assumed.

Staying with our MI segment, which as you may recall, includes primary operations in the U.S. and mortgage reinsurance globally as well as a GSE risk-sharing transactions portfolio. We estimate that the markets MI new insurance written, or NIW, was down about 10% in the first quarter of 2016 versus the fourth quarter of 2015. In spite of this, Arch continues to increase its presence in this sector. Overall, our Arch MI segment grew its gross written premium this quarter by 21% over the fourth quarter of 2015 and 84% over the same quarter last year. The growth came primarily from new GSE risk-sharing transactions as well as from a reinsurance contract with one of the major Australian lenders that we discussed last quarter.

Our U.S. MI unit continues to increase its share of the market. Excluding the GSE transactions, we estimate that we continue to gain market share at a base of approximately 2 percentage points per year since our acquisition of the U.S. MI platform.

At March 31, 2016, our total MI segment risk in force was $12.8 billion, which includes $7.2 billion from our U.S. MI operations, $4 billion from worldwide reinsurance operations and approximately $1.6 billion from the GSE risk-sharing transactions we wrote.

Our primary U.S. MI operation increased its NIW $2.9 billion during the first quarter of 2016, of which approximately 69% came through the bank channel and 31% via our credit union clients. Seasonally, the first quarter 2016 for credit union production typically runs lower than the other 3 calendar quarters. The amount of NIW from credit union this quarter is consistent with what we've recorded in the first quarter of 2015.

Our bank channel business continues to pick up steam and is becoming a larger contributor to our production and RateStar is a primary driver of this growth. We introduced RateStar less than 5 months ago, and today, we have rate filings approved in all but 3 states. Through March 31, 2016, 1,142 customers have elected to use RateStar. Over 50% of our commitment in the first quarter were obtained through RateStar. We have seen many positive signs since its launch. The increase in our application volume is very encouraging and points to our clients seeing value in our differentiated pricing framework. RateStar is proving to be an effective tool in the differentiating Arch relative to its competition, while maintaining or exceeding our targeted average return of 15% ROE. We believe that our combination of high ratings, superior customer service and product innovation will allow us to continue growing.

I will turn out to our primary P&C insurance operations in the United States, which currently represents approximately 80% of our global insurance operation. We saw a more stable rate level change at 10 basis points effective rate increase this quarter versus the 140 basis points decrease last quarter, excluding the effective ceded reinsurance. However, that 10 bps increase is somewhat misleading since it is skewed by 1 large professional liability program that renewed at a plus 7% rate increase in the quarter. Without the benefit of this program, our overall rate change would be a rate decrease of 80 bps. We believe that we were able to recapture some of that rate erosion once we consider the purchase of our reinsurance coverages.

Our insurance operations in the U.K., which represents around 17% of the insurance segment, is still pressured from a rate perspective. Rate decreases across all our product lines were 4.6% this quarter. We continue to actively manage this portfolio towards the more attractively priced lines.

On a groupwide basis, our insurance units premium written increased 4% in the 2016 first quarter versus 2015 on a gross basis, while the increase 1% on a net basis. We continue to adjust our mix of business and are generally able to buy reinsurance on more favorable terms.

Ceded premium increased 11% in our insurance group this quarter over the same period last year. Mark Lyons will provide more perspective on this in his commentary.

Areas of opportunity for growth in the insurance sector in the first quarter were in our, as Dinos mentioned, construction, national accounts, travel and alterative market lines. The vast majority of our growth came as a result of our ability to take advantage of the current dislocation in those areas, where some major players are being challenged. In contrast, our executive assurance property and programs businesses are areas where rate levels lead us to a more defensive strategy.

Finally, let's turn to our reinsurance group. Our teams are being reactive and selective consistent with our long-stated strategy of cycle management. Most lines of business, especially the ones with good results, continue to see rate decreases in the 5% to 10% range. There are, however, several lines that are experiencing some level of rate increases. A recurring question our team faces when looking at such areas is whether that positive rate changes enough to allow us to achieve an adequate return. As an example of this, we continue to struggle with large U.S. casualty placements. There is increased demand by buyers in the market for quota shares, but we have been unable to write a significant new transaction at an appropriate return.

Our reinsurance gross premium written declined by 1% for the first quarter of 2016 versus '15, while on the net basis, we were down 8%. Our property cat gross written premium for the 2016 first quarter was down over 10% as we continue to exercise underwriting discipline and benefit from improved terms on retrocessional treaty. Most of our efforts in the underwriting areas are currently directed to U.K. motor specialty liability products and niche areas, such as professional lines, excess motor and facultative. With that, I'll hand this over to Mark to cover the detailed financial results. Mark?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Thank you, Marc, and good morning to all. As was true on previous calls, my comments that follow will be on a fewer Arch basis, which excludes the other segment that being Watford Re, and I'll continue to use the term core to denote results without Watford Re and consolidated when referring to results, including Watford Re.

This quarter, our core business mix based on net written premium changed as follows and relative to the first quarter 2015: Insurance segment reduced from 58% to 56% of the total; the reinsurance segment shrunk from 37% to 33%; and the mortgage segment grew from 5% to 11% of the total. This shift in mix continues to reflect our view of the market and the relative return expectation each segment provides.

As from a longer-term view of our mix changes, I would point out that 4 years ago, in the first quarter of 2012, within the reinsurance segment, the property cat line represented 26% of net earned premiums, whereas this quarter it is down to only 6.9% of earned premiums. And this was accomplished through 71% reduction in net earned premiums over the 4-year period. Yes, 71%.

The insurance segment similarly has reduced it's property in marine net earned premiums by 38% over that same time period. Both actions reflect our view of severe margin compression in the property cat space.

Okay. Moving on to this quarter's financial results. The core combined ratio for the quarter was 87.1%, with 0.5 a point of current accident year cat-related events compared to last quarter in 2015 of an 87.5% combined ratio, which reflected 0.6 of a point cat-related events.

Losses recorded in the first quarter in 2016 from cat events totals only $4.2 million, stemming mostly from within our reinsurance operation. The 2016 first quarter core combined ratio reflected 6.4 points of prior year net favorable developments, which is net of reinsurance and related acquisition expenses compared to 7.8 points of prior period favorable development on the same basis in the 2015 first quarter. This results in a 93% even current core accident quarter combined ratio excluding cats for the first quarter of 2016 compared to 94.7% in the comparable quarter last year.

In the insurance segment, the 2016 accident quarter combined ratio, excluding cats, was 95% even essentially unchanged from the accident quarter combined ratio of 95.1% a year ago. The reinsurance segment 2016 accident quarter ex cat was 94.3%, similarly comparable to the 94% even ratio in the 2015 first quarter.

Moving over to mortgage. There, accident quarter combined ratio was 71.9% in the quarter compared to 94.1% in the first quarter of last year. As I've said in the prior calls, it's important to remember though that the concept of accident year is more of a P&C concept and not a mortgage insurance concept due to their accounting conventions.

Now as previously stated, the ACGL core accident quarter combined ratio dropped 170 basis points quarter-over-quarter. Yet, insurance and reinsurance segments ratios were virtually flat with last year's respective quarter. This is driven by the mortgage segment as its inherent strong level of profitability is becoming a higher proportion contributor to our overall results.

The insurance segment accounted for roughly 11% of total net favorable development in the quarter, net of associated acquisition expenses. And this was primarily driven by shorter tailed lines from the 2012 to 2014 accident years and longer tailed lines from the 2003, '04, '08 and 2012 accident years.

The reinsurance segment accounted for 84% of the total net favorable development in the quarter, with approximately 3 quarters of that due to net favorable development of short-tailed lines concentrated in the more recent underwriting years. And the remaining portion due to net favorable development on longer-tailed lines, primarily from the 2003 through 2011 underwriting years.

The mortgage segment accounted for approximately 5% of the favorable development, which translates to a 4.4% beneficial impact on the loss ratio this quarter, resulting primarily from continued lower claim rates from the CMG business we acquired in 2014 and from the PMI quota share we assumed within that transaction covering the 2009 to 2011 book years.

As was the case last quarter, some of this favorable development benefit is offset by the contingent consideration earn-out mechanism negotiated within the purchase agreement. And as a reminder, this contingent consideration impact is reflected in realized gains and losses and not within underwriting income.

The core 34% even expense ratio for the first quarter of this year was 50 basis points lower than last year's comparative quarter of 34.5%. Overall, the expense ratio though was aided this quarter by roughly 75 basis points of at least -- of an overestimated year-end 2015 bonus accruals.

The insurance segment expense ratio has improved 90 basis points for the first quarter of 2015, reflecting both a lower net acquisition and operating expense ratio. When one adjusts, however, for the aforementioned bonus accrual benefit, the expense ratio would be nearly 50 bps higher; however, still an improvement over last year's comparative quarter.

We, as managers, continue to focus on the total expense ratio though as mentioned previously, since the flooding of costs and benefits within net acquisition and operating expense ratios can be somewhat artificial. And ceding commissions are recorded in the net acquisition line and not allocated to every operating expense category that they represent.

The reinsurance segment expense ratio increased to 120 basis points this quarter, primarily reflecting a 6.6% lower net earned premium base. I will note though that the reinsurance segment expense ratio this quarter was 100 basis points lower than sequentially in the fourth quarter of 2015. The ratio of net premiums to gross premium for our core operations in the quarter was 72 -- 70.2%, which is a decline from 71.8% a year ago. The insurance segment had a lower 68.8% ratio compared to 70.7% a year ago, driven mostly as was the case last quarter by increased sessions on a larger alternative markets, both increased sessions on capacity-driven product lines as Dinos mentioned and a reduction in our P&C program business, which had been kept overwhelmingly net and still is kept overwhelmingly net.

The associated average cede commission ratio on quota share treaties improved another 200 basis points in the U.S. In fact, quota share treaties cede commissions have improved from 2012 to now by over 500 basis points in total, and the improvement ranges from plus 600 to plus 1,000 basis points for some product lines.

Some of this net acquisition improvement, however, is masked by the growth of businesses using captive reinsurance arrangements. Many of these carry no or marginal front-end commissions, so the associated ceding commissions are lower since they're generally no front-end commissions to be reimbursed.

Moving to the reinsurance segment. The net to gross ratio was 66.6% in the quarter compared to approximately 72% a year ago, primarily reflecting sessions to Watford Re and other third-party retrocessions.

The mortgage segment, in addition to premium growth that Marc mentioned earlier, had approximately $4 million of other underwriting income in the quarter from risk-sharing transactions receiving derivative accounting treatment and $7 million of underwriting profits associated with risk-sharing transactions receiving insurance accounting treatment. Over time, it is expected that more income will continue to emanate from transactions receiving insurance accounting treatment.

The total return on our investment portfolio on a local currency basis was a reported positive 148 bps in the quarter, reflecting positive returns in fixed income investments, both investment and noninvestment grade, partially offset by negative returns in the equity and alterative investment portfolios.

On U.S. dollar basis, total return was a positive 182 bps in the quarter. Over 80% of the portfolio was comprised of fixed income investments. The embedded pretax book yield before expenses was 2.07% as of the end of the quarter and duration remains fairly consistent at 3.56 years versus 3.35 years at the end of 2015 first quarter.

Dinos already mentioned reported investment income per share, so I won't go into that. Other than as a reminder that we evaluate investment performance on a total return basis and not merely by the geography of net investment income.

Core cash flow from operations was $257 million in the quarter versus approximately $16 million in the first quarter of 2015. Last quarter, as you may recall, had cash flow from operations being affected by a reduction in gross premiums collected, timing shifts of reinsurance premiums session and paid and deductible recoveries.

Core interest expense for the quarter was $12.6 million, which is consistent with our longer-term run rate. Our effective tax rate on pretax operating income available to Arch shareholders for the first quarter was an expense of 6.6% compared to an expense of 3.9% in the first quarter of 2015. This quarter's 6.6% effective tax rate is approximately -- has approximately 100 basis points of a nonrecurrent discrete item out of our European operations. Fluctuations in the effective tax rate can result from variability in the relative mix of income or loss reported by jurisdiction.

Our total capital was $7.3 billion at the end of this quarter, up 2.9% relative to December 31, 2015. Our debt to capital ratio this quarter remains low at 12.2% and debt plus hybrids represents only 16.7% of our total capital, which continues to give a significant financial flexibility.
We also continue to estimate having capital in the excess of our targeted position. Book value per share was $49.87, which is 4% increase over year-end and 4.3% relative to 1 year ago. This change in book value per share primarily reflects the company's continued strong underwriting performance from all segments and improved investment returns. With these introductory comments, we are now pleased to take your questions.

Question and Answer

Operator

[Operator Instructions] Our first question comes from the name of Vinay Misquith with Sterne Agee.

Vinay Gerard Misquith
Sterne Agee & Leach Inc., Research Division

The first question is on the new opportunities because of market dislocation if you could discuss that, that would be helpful.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, Mark talked about some unusual transactions or that we see on the reinsurance side, doesn't mean we're going to do any, but we see more requests. So that means there is clients out there that they have special needs.

On the insurance side, we continue to focus on small medium-size accounts. I believe, we have build the infrastructure around the country. We recently -- in our finding [indiscernible] business, we also open another new office in Scottsdale, Arizona. So we're putting a lot of focus in trying to find these profitable segments for us. But let me reemphasize, we always look for bottom line results first and we look at premium growth second. At the end of the day, you can't focus just on premium growth. Of course, that's not the case with our mortgage business. That business, we like a lot and we try to grow it as fast as we can. So Mark, you want to add to it?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

On the insurance side, I believe that we've seen an increase in submissions over the last quarter or so because some of our competitors decided to exit some lines of business. There have been some mergers and acquisitions. So we are seeing some movement. It is not widespread, but it is certainly starting to occur, and we're seizing the opportunity whenever we can and whenever we think it's appropriate.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Yes, one area we're not participating and I want to -- it seems that the flavor of the months now or the year is broker line slips here and there so they can have control of the pen, et cetera. That doesn't fit well with us. We have not participated in any of these. Because at the end of the day, you can't have the title underwriter and give it to somebody else. Either you're going to underwrite or you're not. And without groups, I want us to have the ability to underwrite ourselves.

Vinay Gerard Misquith
Sterne Agee & Leach Inc., Research Division

Okay, that's great. That's helpful. The second question on mortgage insurance. You could give us some metrics about how well RateStar is doing. I think you said, 50% of the submissions were coming through RateStar, but do you think it's actually driving more submissions to Arch because of that and any anecdotal evidence would be great?

Constantine P. Iordanou
Chairman and Chief Executive Officer

It's on -- if you look at it from a submission point of view, let me give you -- first quarter, it was 50-50. If I look at April, it is up to 68-32. So -- and it's been trending like this. So RateStar is only being out there for 5 months. So I don't know where it's going to go, but it's more significant when I look at our submission activity from the bank channel. The bank channel is predominantly -- RateStar now may be 8 out of 10 submissions in April coming from that. On the credit union channel, it still in the 50-50 range. So that's where the trajectory is going. The NIW, it was 44%, 45%, I think, in the first quarter out of RateStar price business, but it was -- in April, was 61%. So that tells you that it's -- more and more of that business is moving to the place that we wanted to move because we have a lot of faith in the way we price the business. Marc?

Marc Grandisson
President and Chief Operating Officer

Yes, Vinay, on the -- essentially, there is a huge increase in submission. We believe it's in the order of 50%, 60% through the last quarter of '15 versus this first quarter. And the vast majority of that pick up was through the bank channel. So just to give you an overall sense in the quarter.

Vinay Gerard Misquith
Sterne Agee & Leach Inc., Research Division

That's helpful. And Marc, if you could also clarify about rates? I mean, I think you mentioned that the risk-adjusted rates are actually higher now for this rather than lower?

Marc Grandisson
President and Chief Operating Officer

Yes. Because...

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, the return -- the expected ROE on the business is higher than our rate card.

Vinay Gerard Misquith
Sterne Agee & Leach Inc., Research Division

Okay. And even from a competitive standpoint you've not seen competitors sort of step in and do something similar?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Right now, we -- the rate card seems to have stabilized in some -- there are rumors. The only thing I can comment you, Vinay, is our rumors that some people will be extending the rate card or doing the risk based pricing approach that we have, but we have no way of knowing what's going to happen right now, But right now, it seems that the rate card has been stabilized where it is right now.

Marc Grandisson
President and Chief Operating Officer

But, our future, Vinay, is going to be RateStar. We like risk-based approach to looking at many characteristics of a particular mortgage and trying to get the right price for the exposure that you have. And we continue to refine our approach with that. I have a lot of resources committed to that effort, which is no different than what we do on the P&C side to begin with.

Operator

Our next question comes from Amit Kumar with Macquarie.

Amit Kumar
Macquarie Research

Two quick questions on MI and thanks for being patient with us and explaining the finer nuances of the MI market. The first question probably ties back to the next question on the broader space. Recently, the National Association of Realtors wrote a letter to FHA asking them to cut their premiums. If FHA cuts their premiums, does that change the entire sort of the private MI market? Or is that a different kind of -- it's obviously a different risk, so it doesn't impact you that much?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, it depends what sectors -- you're correct. A lot of what they write is the private MI companies do not. They write the low credits for high LTV type of business. So depending what they do, it might or might not effect the broader market. It's tough when you have the government competing with you, but entirely totally different capital requirements. None of us or our competitors in this space would be allowed to operate with a capital ratios that they have. So I don't know. It depends on what they do. And then we'll see the effects that it will have on the marketplace. And by the way, thank you for the compliment of being patient. My guys here they say otherwise so.

Amit Kumar
Macquarie Research

The other question I have was in regards to the excess capital, which you mentioned. There has been chatter in the marketplace obviously regarding the dissolution of a large MI asset [indiscernible] of one of the largest company. At this stage of the cycle, Dinos, how do you look at growing organically? And I'm talking about the MI piece versus looking at this obviously very large and game changing property out there.

Constantine P. Iordanou
Chairman and Chief Executive Officer

We -- all I can say is, we will look at all avenues. Right now, our focus has been to grow organically. But given other opportunities, we will evaluate them. If they get presented to us, we'll evaluate them. At the end of the day, it will get paid to put capital to work at an effective returns and that's where our entire team is focused on. And it's no secret that we do -- that we do want to grow the exposure we have in the MI business.

Operator

Our next question comes from Jay Gelb with Barclays.

Jay H. Gelb
Barclays PLC, Research Division

On the core reinsurance segment, I was somewhat surprised to see that the gross written premiums were essentially flat. You mentioned some specialty opportunities. I was hoping to get a better perspective on whether you think that overall business might be flat from a premium volume perspective or maybe even grow this year.

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

I don't know about the rest of the year, it depends what we're going to offered with, but in the first quarter certainly seize opportunity in the few larger transactions that Dinos alluded to at the beginning. And also, couple of opportunities, which I highlighted in my comments, which are the U.K. motor and some specialty liability, although not being very big, but it is more niche, more specialty in nature. I'd just say it's a reflection U.K. motor for instance. If you do a large quota share, you will have a lot more throughput in the quarter. So that's a great example as to what premium would actually be stable year-on-year.

Jay H. Gelb
Barclays PLC, Research Division

That makes sense, Mark. The other point I want to touch base on -- in reinsurances, the high level of persistent reserve releases. Can you give us some perspective on what continues to drive that favorable result?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, let me give it on a 10 and then I'll give it. I've been surrounded by actuaries here. Mark and Marc, they are both actuaries, but we have a methodology. We haven't changed our methodology for the 14 years. To simplify it, we try to pack the accident year based on what we believe we price the business at. And then, the other thing we do is on long-tail lines. If we see unfavorable -- we recognize that early on any unusual event where we ignore favorable at least for 3 or 4 years. So that's been our methodology, recognize bad news early, don't celebrate too early on your wins, and we follow the data. So whatever the data tells us quarter after quarter is that's what we report. Now that's was a guy who doesn't have an actuarial degree. So I'll turn it over to Marc or Mark, Mark Lyons, to give you the more scientific answer.

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Good. My scientific answer as a reformed actuary is, I had nothing more to add.

Jay H. Gelb
Barclays PLC, Research Division

The final question I have was on mortgage reinsurance. The -- clearly, there was a big benefit in 1Q from the Australian deal. I'm trying to think about on organic -- I guess, organic is not the right word, but on a normalized basis, what do you think the growth rate could be in mortgage insurance? And could this be a $500 million gross written premium business within the year or so?

Marc Grandisson
President and Chief Operating Officer

Well, we don't know. Australia is a market that dominated by 2 or 3 players or 4 banks. So we have a major relationship with one of the top 4. It's kind of hard to see where, if any, if we're able to grow relationships in other banks. But currently, right now, we have a stable, very strong relationship there. And what you're seeing right now is a production. Even though we call it the reinsurance is really a flow business that we assume on a 100% basis. So it's really like insurance, if you will. For the rest of the world, we're exploring all other geographical areas. Dinos and I are spending a lot of time to figure out what we could do in Europe, what we could do -- I mean, we already are in Europe, Canada and other countries. And this is sort of an ongoing try, grow and use and take advantage of our expertise and then strong knowledge and deep knowledge in the MI space to do more of it. It's really hard to see what it would be in 2, 3 years time. But for the Australian business, I think you get pretty much a good picture of a quarterly production.

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Hey Jay, it's Mark Lyons. Let me just add the difference between binding the business and expanding it versus the accounting recognition on it. The Australian market is a single premium market. So it's -- you really got to contrast that with the U.S., which is dominantly monthly. So it builds up and it recognize slowly. And by single, it's not like -- it's a single program writing a big bullet single. It's not the case. The underlying business, the business that is reinsuring is a series of every homeowner having a single premium as they put at the place. So the recognition will be accelerated relative to the U.S. So you can't extrapolate that into something that may appear ultimately to be larger.

Operator

Our next question comes from Michael Nannizzi with Goldman Sachs.

Michael Steven Nannizzi

Goldman Sachs Group Inc., Research Division

Just a couple here. I think most of might have been answered, but the ceded level that we saw on the first quarter that lifted from the first quarter last year. I mean, just -- you guys expect it to be ceding back to Watford or whoever in that sort of 30% range from here? Was there anything unusual in the quarter?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Okay. You're saying the 30% because of the 70% net to growth?

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Yes.

Marc Grandisson
President and Chief Operating Officer

Well, remember, those sessions are dominated by the insurance group ceding overwhelmingly to third party -- unrelated third party. You have increase retrocession on the property in marine that the reinsurance group will do. You have minor bits in the mortgage sector really the function of the deal that was cut on -- originally on the transaction. So the movement, yes, there is Watford sessions, but the level of Watford session is fairly consistent over the last couple of quarters. The biggest lever is what the insurance group does. And, as Dinos pointed out, they were just shy of 70% this quarter, but the growth in low volatility businesses that kept overwhelmingly net and the high capacity business that Dinos talked about -- the high capacity, we mean $25 million limit, things like that. Those are going to be reinsured more because we can get more favorable term. So we cut the aggregate net volatility of the total book as a result. But just keep in mind, Michael, it's the insurance group that drives that ratio.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Okay, got it. And then, other income in -- primarily in the insurance, I guess, a little bit in insurance as well that step down in the quarter. Was -- did that -- those dollars just move to different line item may be some versus geography or was there a change in the...?

Marc Grandisson
President and Chief Operating Officer

No, no. It's a great question. On the -- think of it this way. Quarter-to-quarter that other underwriting income in reinsurance was virtually flat. It's coming from the GSE transactions mostly. Last year, that was what we call catch-up premium on the difference between when the capital markets piece went out that's done earlier. And then that the insurance -- reinsurance segment was done later and if you catch up because of the time gap between them. So that was roughly $3.5 million of catch up.

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

That's the first thing. The second thing would be occasionally, we call it periodically. We reevaluate that Ethniki loss portfolio transfer. And in that year's quarter, there was an adjustment, whereas this year's quarter, there was not.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Okay. So -- but now, they were all caught up, then we should be reverting back to the pattern that we were experiencing previously, is that?

Marc Grandisson
President and Chief Operating Officer

For the derivative-oriented transactions for the GSEs in the reinsurance -- in the mortgage, the answer would be yes. [indiscernible], it depends when we -- team change is needed.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Derivative accounting for those transactions would be deescalating and going to 0 over 7 years, right. So every quarter slightly a little less, a little less until it gets extinguished 7 years out or so.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Got it. But main point being that other than this timing change you mentioned in the first quarter, nothing has really changed as far as that's concerned?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

No. No. That is correct. Yes.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

All right. And then in reinsurance, so the expense dollars and other operating expense declined in the quarter, like sequentially, I was just curious if the transaction or the item you mentioned in insurance was relevant in reinsurance as well, Mark, or is it -- was there something else there?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

I'm sorry, was that an operating question, an expense question or acquisition expense question?

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Operating.

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Oh operating.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

So other operating -- yes?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

I think the quarter and then the segments as well as in total was kind of affected by the bonus accrual -- takedown that I mentioned. So I would expect the run rate to be a little -- marginally higher on a ratio basis.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Okay. So is it the order of magnitude similar to what you mentioned on the insurance side in terms of the...

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Within staying distance, yes, which is as good as I get.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

As a reformed actuary?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Yes. Thank you.

Operator

Our next question comes from Kai Pan with Morgan Stanley.

Kai Pan
Morgan Stanley, Research Division

First -- do you see any potential impact for the second quarter cats?

Marc Grandisson
President and Chief Operating Officer

The second quarter cats, yes, I mean, we have some reported losses. I don't know how the big impact is going to be. Mark, you have more of a feel for that..

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Right. As you know, a lot of this stuff is pretty fresh. It just happened. And there's a series of that, it's a not single event. So you can appreciate that we're still accumulating some of that. I think from a 10,000 foot view down, it's more likely that there is insurance exposure than reinsurance exposure out of our U.K. operations, I would think. But our view at this point, Kai, is that across all of those aggregated together, it will still be contained within cat load. So we don't view anything unusual in that regard emanating from it.

Kai Pan
Morgan Stanley, Research Division

Okay. And what's your sort of cat load assumptions?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Our cat load will be just shy of 40.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Yes, at 40 a quarter. $40 million in a quarter.

Kai Pan
Morgan Stanley, Research Division

Okay, that's great. And then -- so stepping back on the mortgage insurance, a couple of years ago, Dinos, you mentioned that this could become the third leg of the stool, but looking back at the premium, it's only less than 10% of your overall premium. But if you look at the underwriting results, it's more than 20% now. So it's very meaningful. I just wonder why the growth in this market faster than your other 2 segments were even sort of like exaggerated or basically your -- both your underlying margin as well as ROE will be growing faster than it has been?

Constantine P. Iordanou
Chairman and Chief Executive Officer

You got to look at it from a lot of different perspectives. Premium is not the right measure for mortgage insurance because it's -- the accounting model is totally different. The way the business comes in is totally different, right? I write a mortgage today and I'm going to be receiving premium over the duration of that mortgage was usually 7 years or so or -- so you got to look it from capital consumption and you got to also look at it from the return point of view. And yes, I think we're on pace based on what we wanted to create a third revenue stream for the company and a third earning stream for us. And I wouldn't be surprised that depending what happens on the P&C insurance -- reinsurance that from an earnings point of view, there might be even more than 1/3. They might go to 40%, 45%. On the other hand, P&C concerning a couple of years and it will be -- we don't -- we do look at it from a risk management point of view as to how much exposure we have in each one of the sectors, and do we feel comfortable with that vis-à-vis our balance sheet? Or do we need to buy a reinsurance behind it or bring other capital providers into it? We know we're close to any of those decisions. We believe that we still have a lot of room to grow on the mortgage business. Marc, you want to add something?

Marc Grandisson
President and Chief Operating Officer

The only thing I would say in terms of creating a third leg in the sense of a very sustainable and profitable on a return basis. I think we have accomplished that and we're really looking forward to more of that in the future from that perspective. We're not really getting into the discussions as to how much it could be, would be. In the end, we're writing and looking at what we see every day and we're very pleased right now, and I think we have achieved at least establishing, has taken a ground in creating that third-floor diversifying flow, I would add, to our core P&C reinsurance and insurance. So we're pleased with that.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Yes. And look, I thing Marc went on to how little cap we write today versus what we wrote 4 or 5 years ago. Things might change, but we always have that -- sometimes we shrink in areas that I don't like to shrink, but if there is no return, why be in it. Other times, you got a limit what you write because you're exceeding your tolerance from a risk management point of few. I can tell you right now I'm way on the leverage on the cap business. I wish the market was better for us to write a lot more in the cafeteria, and maybe one day it will be again and it will be up utilizing quite a bit of capacity in that area. But that's the kind of think in that goes through ahead. First, if it's profitable, let's write more until we got a guy called chief risk officer, he's another actuary, François, who rings the bell sometimes and he says -- yes, he's nowhere ringing any bells yet because our risk tolerance is in every sector, is well within what we like to have.

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

And Kai, I would just like tie together the -- that commentary with -- on managing the cycle and exposure with the fact that we had $4 million of cats in the first quarter. If we hadn't reduced our volumes, 71% since 2012, we probably would not be able to report $4 million. So it's got income statement aspects, price return aspects and balance sheet risk management.

Kai Pan
Morgan Stanley, Research Division

Just to follow up on the risk management. This might be a high-class problem for you guys. If the mortgage become a meaningful portion of your overall profit pool because a different accounting unlike a trade basically you cannot smooth it out, for example, booking reserves, do you worry about the sort of volatility to the earnings?

Constantine P. Iordanou
Chairman and Chief Executive Officer

No, listen, there is 2 things that bring volatility to any book of business, including mortgage. One is what I would call micro decisions, that's the underwriting decision. That we control is within our hands. So we --

and then the other volatility is macroeconomic changes, very high unemployment, which we monitor and see which direction. I would assign 2/3 on the micro and 1/3 on the macro. And at the end of the day, we -- in our quarterly risk management evaluations on everything we do, we'll look at those parameters to make sure that our compass is pointing us in the right direction.

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

And Kai, lastly, because I want to make sure, even though you've raised the question, the accounting model as much as we criticize it, has nothing to do with our risk management evaluation. We project that's the ultimate like we do our PC lines, so we [indiscernible] assumptions, claims emanating from possible future delinquencies that are performing loans now and so forth. So just because it's the accounting model is flawed doesn't mean we follow that in our risk management evaluation.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Yes. And we have a stress test model that we run, assuming certain economic conditions, where the housing market might go, where unemployment might go, et cetera, and where interest rates are going to go. And then based on that, we see where we are with our book and where our book is growing.

Kai Pan
Morgan Stanley, Research Division

That's great. Lastly, if I may, on the buybacks. They are now trading at -- you bought it back around 1.3x for the first quarter of book value, and now trading at more than 1.4x. Is that out of your comfort zone?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, I mean, if you ask me, if I'm trading well, which is your assumption? No, I still think that -- I'm cheap, but that's the CEO talking to his own account. But having said that, we're very disciplined into when we put capital to work and depending if we're going to buy our own shares or we're going to buy something else, it's got to be within that 3 years or so of [indiscernible] that we got to recover, anything we pay above book value. And that's what's been guiding us both in -- we tried to invest in third parties or we're trying to invest on our own stock. So in the -- that's basically what we are.

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

And Kai, I applaud your 5-part question.

Operator

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

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Just a couple of questions. The first is, Mark, maybe just to make our lives a little bit easier, the reversal of these bonus accruals, can you actually give us the dollar number and where the location is?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

It was roughly 6 and change, distributed all over, actually.

Constantine P. Iordanou
Chairman and Chief Executive Officer

It was all 3 units and corporate, but it was -- call it, $7 million.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Okay. Next question. I guess, I'm looking for a little bit of guidance or help here. There are some line items within the...

Constantine P. Iordanou
Chairman and Chief Executive Officer

We don't give guidance.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Well, I'll call it help then, not guidance.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Okay. All right.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

For a nonactuary, not even reformed -- how's that -- certain line items within mortgage insurance will jump around pretty dramatically quarter-to-quarter and your looking specifically at the acquisition expense ratio. It's ranged from 33% to 13% just in the last 6 quarters. Any sort of range that you can put that in that we should be thinking about?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, on the traditional mortgage insurance, what we do in Arch MI Walnut Creek Re is steady. If you sell for, as every quarter, et cetera, what those numbers fluctuate on reinsurance transactions and on the risk sharings transactions. The cost with risk sharing is it's very, very small because we have a small unit, a couple of people that they -- we view those transactions in the home office and then they -- and Mark and I when we -- and Andrew Rippert, who got to approval those, we don't allocate our stuff into it. It's at a corporate level.

Marc Grandisson
President and Chief Operating Officer

And Jay, the only business we had in mortgage were largely mortgage reinsurance contracts and transactions and we migrated towards more of a mortgage insurance profile. And that explains the ceding commission on reinsurance treaties right now on the mortgage space are in the 28% to 35% range. And we're not doing many of those or any, at least nothing new as we speak, right?

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Got it. So in quarters, where you have a big reinsurance transaction, the acquisition expense ratio will look a little lower?

Constantine P. Iordanou
Chairman and Chief Executive Officer

No, you go the other way.

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

This is assumed, not ceded.

Marc Grandisson
President and Chief Operating Officer

Right. This is correct.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Because I'm looking at like this quarter, the acquisition expense ratio within mortgage insurance -- within the mortgage segment was quite low when you did a large deal. Maybe I'll take it offline with Don after.

Constantine P. Iordanou
Chairman and Chief Executive Officer

No, no. We did another big reinsurance deal.

Marc Grandisson
President and Chief Operating Officer

Exactly, Jay, I'm not sure, which deal you're talking about?

Jay Adam Cohen
BofA Merrill Lynch, Research Division

I saw you guys did a sizeable deal in Australia on the -- for the mortgage reinsurance?

Marc Grandisson
President and Chief Operating Officer

So that's not a reinsurance transaction. As Mark said, it's really -- a reinsurance in the legal sense of a term, but we're doing a 100% of really flow business. And as Mark alluded to, that premium is earned over a very long period of time and the other premium is actually very small, as we speak. Even though the acquisition there would be high, it doesn't really flow through the balance sheet or the income statement as we speak, it will take time to get there.

Operator

Our next question comes from Charles Sebaski with BMO Capital Markets.

Charles Joseph Sebaski
BMO Capital Markets Equity Research

I guess, one follow-up on that Austrian transaction. You say it's going to earn in over a long period of time. So despite the $43 million, we shouldn't see much affect on earned premium from that, going forward, for the next 4 or 5, 6 quarters?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Yes, it's exactly right. I mean, just picture, just to make things simplistic. Picture every month, being a million-dollar single and then no single each of those million dollars has to be earned over 6, 7 years. So it -- the written recognition is going to be a lot faster than the earned recognition.

Charles Joseph Sebaski
BMO Capital Markets Equity Research

Okay. Also on mortgage, has there been any activity on GSE-risk sharing over the quarters? Has there a pipeline or anything? Or is it kind of stagnant until something pops? Just curious what the outlook looks like for that?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, no, there is activity and there's a list of transactions that are coming down the pipe. Marc, you have the detail on that or...

Marc Grandisson
President and Chief Operating Officer

[indiscernible] right here in the quarter, there were, I believe, 3 transactions. I believe -- there were 3 transactions in the quarter. And there's actually a calendar, Charles, that they're going to -- there is a projection for the year that the GSE has shared with us. I'm not sure, we are supposed to say anything, but you could track that. They're on a pace to do from our perspective on a 2 to 3 a quarter for the next -- for the remainder of the year. So we've done 3 this first quarter and are working on some of the details as well.

Charles Joseph Sebaski
BMO Capital Markets Equity Research

Excellent. And that finally, on reinsurance, would appreciate your guys' take -- some commentary in the market that the changing landscape in reinsurers means that smaller panels of reinsurers mean you have to stay at the table, maintain business. You guys have been contracting here. Do you believe that there's risk that, over time, you need to maintain some particular level of profile with cedings? Or can you keep contracting and it still get back in opportunistically? I guess I'm trying to understand the...

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, it's -- listen. This is the -- it's a great question. At the end of the day, we have good ratings, good paper [ph], we can be good partners, but I'm not there to do it on a just relationship basis and not have a return. My responsibility is that I return from my shareholders. I'm not going to put that capital to work at a disadvantage on the hope that some future I'm going to make some money. If the deals make sense for us and our cedings will do them. If they don't, we don't, and we look for something else. This is a big market and we still writing over $1 billion worth of reinsurance. Maybe not all of it is what I would call the traditional quota shares for large clients, et cetera, but we find little things here and there, niche things here and there and we do it. Our people -- believe me, they're working harder today than in a good market and -- because to find these small little nuggets that they got to process a lot of war. So they're shoveling a lot. At the end of the day, that's our approach. We don't believe that we had to give up in a way through just purely -- we ought to be making relationship on the decision. Yes, relationship is very important. We try to be as service oriented as anybody else with our clients, give them our perspective about the market and of pricing we do, underwriting audits, et cetera, we share all of information, but we got to do a transaction that it has adequate return for us, otherwise, we won't do it.

Charles Joseph Sebaski
BMO Capital Markets Equity Research

I appreciate the answer.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Marc, I mean, you're on the reinsurance. I shouldn't be speaking on your behalf.

Marc Grandisson
President and Chief Operating Officer

The one thing I will about our reinsurance portfolio is that it's not really the same as Mark alluded to, the same portfolio that we had when we started. I think there is a lot of what we're been able to create an arrangement side, which sort of narrows what has been done on the insurance side is as we try to get as the not controllable, but as somewhat protected or that our line business that has a little bit of stickiness to it, more stickiness to it because it needs more knowledge or more expertise. Property facultative is a great example of that. Within that segment, I think we are very -- still very active, finding ways to grow and actually do more and be more relevant for our clients. So we're not be holding to the large placements as Dinos mentioned, which is a good place to be.

Operator

Our next question comes from Meyer Shields with KBW.

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

Really quickly, the mortgage insurance operating expense number went up sequentially. I wasn't expecting that. Everything else was phenomenal, but is that new -- is that the new run rate?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

I don't know. I -- as Dinos mentioned, it's a segment. The segment's made up of pretty disparate operating expense contributors. Clearly, until we hit scale on the U.S. MI acquired piece, that's putting pressure on it. But the mixture of that with a GSEs, where the OpEx is marginal at best, and the reinsurance, again, depending on the structure of it. It really comes down to mix. So I would not read in anything to an incremental change quarter-over-quarter.

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

Okay. Are you discussing the dollar amount or the percentage?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Well, effectively both, but mostly the ratio.

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

Okay. And then on the insurance segment, I guess, you talked a lot about a shift towards smaller account low volatility. Is that going to have an observable impact on either the acquisition expense ratio or the loss ratio of that mix shift?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, I don't -- I mean, this shift has been happening now for 5, 6 years. We didn't pivot to that. The largest initially we have which is about $160 million worth of business is a binding authority business. And that has a little higher expense component. It comes from the binding authority wholesale agents. And in essence, they do a lot of the work. It's all electronic. They use our systems. They price -- a pricing algorithms, et cetera, but they do that all the input and the issue the policies, our system is so good that you can bind and issue a policy within 24 hours in the agent's office. So it has a little bit of a higher expense.

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Yes, I would also say, you actually have seen some marginal improvements. Just in the past quarter, that's 30 bps down on the net acquisition ratio. Just -- remember, premium taxes are in there too. And when you go from a harder to a software market, it tends to become more admitted than not admitted, you get a little bump there, on everything else being constant. But the biggest thing is that you keep in your mind that as we move to lower and have moved to lower volatility businesses, they come with a higher acquisition costs and a lower loss ratio. So the fact that we have a higher proportion of higher commission-oriented businesses, yet the net act is continuing to go down, shows you've got leverage, power of our reinsurance session with increase ceding commissions. It's offsetting and sometimes more than offsetting that shift -- mix shift towards higher act [ph] businesses. Makes sense?

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

Okay. But lower -- I'm sorry?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Does that make sense?

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

It does, only I'm not contesting it. I'm just -- interesting, a lot of competitors have talked about lower volatility business having higher loss ratio.

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Well, whatever, we're after volatility containment. You can cede a lot depending -- what's left. There's still -- especially with the quota share, it's still highly volatile on its own. You're getting ceding commission overrides and you're putting gain in the income statement right away. But what you still have left is volatile. We've move more towards, as Dinos said, smaller accounts and small policy limits associated with those, but we keep 100% net.

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

Okay. Now that helps. Are the ceding commissions that you're seeing in reinsurance the same as you're benefiting from on the insurance side?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Yes. The answer is yes.

Marc Grandisson
President and Chief Operating Officer

Yes, there's pain on one side and there is gain on the other side.

Marc Grandisson
President and Chief Operating Officer

The market's phenomenon.

Operator

Our next question comes from Ian Gutterman with Balyasny.

Ian Gutterman
Balyasny Asset Management L.P.

I guess, first, Marc, you talked earlier about the growth in U.K. motor, and I think a [indiscernible] was about talked about that. Can you just talk a little bit more about sort of what kind of -- what exactly that business is? And what's appealing about it, I guess, I have ancient bad memories of that causing trouble from time to time?

Marc Grandisson
President and Chief Operating Officer

Oh yes, and you're quite right. It's very interesting and very volatile if you're not careful, but we have a good relationship with one big originator in the U.K. and has been a partner of ours for a little while and we've been able to maneuver through the cycle with them alongside with them. And we are seeing rate increases over the last 3 or 4 quarters, I would say, and we were able to seize on the opportunity and give them what we think are appropriate reinsurance term to be partners with them on a going-forward basis. In addition to this, the excess of loss in the U.K. has also gone through a tough time in terms of a lot of changes in the rate level, and we were also able to take advantage of that. So it's really is a reaction, to echo what you just mentioned, to the fact that rates have been increasing and improving. And as I said in my comments, and they have increased enough to that we have believed that returns are there for now for us to take advantage of it.

Ian Gutterman
Balyasny Asset Management L.P.

Got it. And so you're doing well [ph] then?

Marc Grandisson
President and Chief Operating Officer

We're doing [indiscernible].

Ian Gutterman
Balyasny Asset Management L.P.

Got it. Got it. And are there a lot of caps on those to protect you? Or is it just you can...

Marc Grandisson
President and Chief Operating Officer

They're using terms that...

Constantine P. Iordanou
Chairman and Chief Executive Officer

[indiscernible] that you're asking me and I'm not sure I'm comfortable sharing that with you.

Ian Gutterman
Balyasny Asset Management L.P.

That's fair. Okay. I guess, maybe I was getting at is -- I always see that being a long-tail business and just -- are there ways that you see it deteriorating? Is it just you won't renew it the next year? Or are there other things that you can do to protect yourself if 5 years down the road it goes bad?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Are you talking about the [indiscernible] of this or the extra loss?

Ian Gutterman
Balyasny Asset Management L.P.

I guess that's probably more on the quota, right? But I mean, I guess it could be either.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, I mean, no, the quota share you can adjust, very quickly by -- based on your underwriting audits and how you're monitoring rates. Don't forget. We do a lot of underwriting audits and we continue to watch the pricing on a quarterly basis. Now the biggest bet [ph] is the excess of loss bet [ph] because you get that wrong and it's not as easy to correct. You can get out later on, but sometimes it might take you a couple of years or 3 years before you recognize that you didn't get the pricing right. That's more, but that's not from a premium revenue point of view, it's not as big as the quota share. So we would [indiscernible], believe me.

Ian Gutterman
Balyasny Asset Management L.P.

Okay, understood. I was just curious because I've seen a lot of people adding to it. On a the MI, the -- I guess, a couple of things on rates. One is, now that everyone has lowered their rate cards for your non-RateStar business? Or is this from rate card? I think in certain cells looks off market. Do you feel you need to address your rate card to sort of match everybody? Or for those customers who want to keep that business?

Constantine P. Iordanou
Chairman and Chief Executive Officer

We actually just -- Ian, we just issued our new rate card on April 7, about 3 weeks ago. Not matching everyone so there is no plan right now to do anything else.

Ian Gutterman
Balyasny Asset Management L.P.

Got it. Got it. Okay I missed that. Okay. And then on the RateStar business, my sense is -- and the guy -- I still don't know exactly what your rates are, but it feels like conceptually a lot of what the competitors did to change the rate cards felt like it was trying to get closer to where you and UGC [ph] are. Is that fair that maybe the advantage of RateStar is a little bit diminished?

Constantine P. Iordanou
Chairman and Chief Executive Officer

I don't know what drove the actions, because your mixing apples and oranges, right? At the end of the day, if you have a pool of risks that on average gives you a good return, ROE, and now through a selection process, maybe 1 or 2 competitors, they might be taking out of the pool certain mortgages for a slightly less price, but a much better risk characteristics. That means the remaining part of the pool needs to be priced a little higher than the past not a little lower. So adjusting the rate cards and not going to look at exactly what adjustments they make, you might be getting into adverse selection, so to speak. At the end of the day, the problem with the rate card is as simplistic way to price. Just credit score and LTV alone is not the only thing that is going to tell you as to how that mortgage is going to behave. There is other parameters around, and I think that's where our advantages. Our advantage is we introduce other factors to allow us to more appropriately price that business.

Marc Grandisson
President and Chief Operating Officer

But clearly, Ian, to your question, a bit more directly, I believe that going to a more refined rate card is sort of a one step for most of them to get to that direction. If there's recognition to Dinos' point that the rate card was -- has been historically too genetic in nature.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Right. And it might die within a year or 2 and we might get into more -- as to what we do in all of our other business, on the P&C, I think. I don't care if he's Zorro or a homeowner or lawyers and accountancy and all, et cetera. We don't have 1 or 2 rating parameters, we have multiples. And then you look at it from many different perspectives to put a price. So I think the mortgage insurance business is moving in the right direction in our view.

Ian Gutterman
Balyasny Asset Management L.P.

For sure. For sure. And then just last on that topic is, if you were to look at a sizeable acquisition in that space that would take you over the 1/3 mix, can you just talk about sort of how you evaluate metrics, meaning I was sort of looking at EPS accretion, but is it sort of -- what are the different things you look at in addition to just EPS? And is it ROE? Is it your PE? I mean, I think one of the concerns some people might have is those companies share a lower multiples or if it becomes too big a part of your mix it might hurt your valuation. Just how do you think about sort of the combination of accretion versus valuation versus returns?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, listen, I don't -- you know that old saying, it says, in the short term, the equity markets is a beauty contest. And in the long-term, it's a weighing machine. That's Buffett's analogy. As long as I'm producing good profits and I keep adding, I don't worry about what the street valuations might be because how do you explain one competitor we have who's trading at 1.7x book, right, in the MI space versus another competitor we have who is trading at 1.1, right? Well, maybe the -- one has legacy business and the other one doesn't, et cetera. So I'm not worried about that because the mortgage insurance business produces very good ROEs to demand a higher multiple than the P&C world right now. And we only have 1 marker out of the 7 who has the purity [ph] in only having postcrisis business and the market is rewarding them with 1.7 multiples. So I don't know, I -- our actions is not as to about the market multiples. Our actions is, I would produce in a good return for the capital that we're committing to a particular sector and is the ROE acceptable. That's what drives us. That's the key driver in what we do.

Ian Gutterman
Balyasny Asset Management L.P.

And the reason I asked...

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Ian, for an insightful guy like you and the others, it would wind up being that ACGL would bring up the mortgage multiple, writing the mortgage multiple bring down ACGL.

Ian Gutterman
Balyasny Asset Management L.P.

Well, it's the reason I asked because if it's something big, I assume you have to use some stocks so that was sort of context I was thinking about. Maybe a better way to say this is what things do you -- historically, you haven't done anything as required and issue it as a stock. So sort of what are the things you evaluate and decide whether stock makes sense in a merger?

Marc Grandisson
President and Chief Operating Officer

Well, let me just start on that one. I mean, we talked about this before on our tangible book value kit. That's not new as to how when we repurchased our shares in respect, what's the recovery period. That is still an in-force principle that we will look at. That is one of the criteria and not the only criteria, but that's certainly one of them. But don't lose sight of the prior discussion, which is on the risk management side. So EPS is a no-brainer, really. That's not tactical. We don't want to impair the balance sheet, number one, so what's the recovery of it and the risk management aspect. We wouldn't go into it if there weren't higher ROEs to begin with, but defensively we don't want to put any dents in the balance sheet.

Operator

Our next question comes from Douglas Mewhirter of RBC Capital Markets.

Douglas Robert Mewhirter
RBC Capital Markets, LLC, Research Division

Just one follow-up question, something that was discussed on the Australian mortgage transaction that just kind of confused me. Is this a recurring revenue transaction, which is to say, we'll see another one of

$40 million or whatever the number will be next quarter and then continuing thereafter? Or is this a one-off, one-shot deal?

Constantine P. Iordanou
Chairman and Chief Executive Officer

No. This is, like I said -- and we're sorry for you -- I just want to make sure it's clear to everyone. This is really like business that was produced in that quarter. That relationship is still existing. It's been around since last year. So yes, I would expect, depending on the level of production that our partner will do in Australia, we could be around that same level if we continue producing the same level.

Marc Grandisson
President and Chief Operating Officer

If they originate the same level of mortgages, they will flow through with us and continues. And it will continue as such until the cancel us or there is a termination by either party on the relationship.

Douglas Robert Mewhirter
RBC Capital Markets, LLC, Research Division

So this puts in place, really, a fairly -- I'm going to use the word permanent or at least, hopefully, long term kind of floor flow of premiums that should last for at least on an earned basis for quite a long time?

Constantine P. Iordanou
Chairman and Chief Executive Officer

Yes, that is correct.

Operator

Our next question comes from Michael Nannizzi with Goldman Sachs.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Sorry, I have a follow-up. Just one last one here. Back to the MI and, Mark, maybe your comments on the expenses. I mean, I'm looking at premiums doubled year-over-year? Acquisition ratio is in half, dollars are down notionally, other operating expense to ratio is flat. I mean, and I understand there was a reinsurance transaction that may be obscuring some of that trend, but I would generally think that the ratio of dollars, it would seem to be more fixed in nature of the operating expenses. That ratio would improve and if the acquisitions ratio would remain relatively flat again, absence some adjustments, I'm just trying to get some understanding what that -- and I understand there are like 3 different businesses, they all operate differently, the stackers, expenses are low and things like that, but I mean, with the line that's growing this quickly, I feel like I'm just missing the mark on how to think about. And should we be looking at expense dollars relative to written premium dollars as opposed to earned during this growth phase? Just any guidance or help -- not guidance, but any help on how to think about it would be great?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

Well, I think written is the better word for the statutory view, but it's -- I still -- makes more sense. When we talked about hitting critical mass and steady state at some point, but also Michael, think about how market share is measured. It's measured on NIW, which is effectively new premium. But that's new exposure, the premium is -- comes in at a slow filled-up rate over time. So if we get to a reasonably larger market share in 2, 3 years, that doesn't mean that overnight, the whole in-force book is where it needs to be. That means the marginal amount in 2017 that we hit, market share of x, is additive to the portfolio. In PC world, we have new business and renewal business. Here, you don't have a renewal business. You have new business and in-force. So all you're doing is adding on to the heap with the NIW that you're getting. So this is a long-winded answer to say you got to be patient. The OpEx dollars are really not going to grow as much. You got to wait for the revenue to catch up with that and it well.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Okay. So OpEx doesn't grow as much. And then in the acquisition expense, I'm guessing that was impacted somewhat by this Australia transaction and the lack of delivery insurance transaction you mentioned that you have in the prior year. But is it sort of teens level of acquisition expense, I mean, is that, given the mix of business you have, is there anything in there that we need to peel out in order to think about the forward?

Mark D. Lyons
Chief Financial Officer, Executive Vice President and Treasurer

No, I think it is the mix. And this will change by quarter. It -- by the way, changes in the reinsurance segment, changes in the insurance segment by mix, the changes, the reported acquisition expense. OpEx is -- those -- the questions you asked are applicable to any of our business segments, but acquisition can fluctuate as a function of the business we write. So I'd say, no, it's mix thing quarter-by-quarter.

Operator

I'm showing no further questions. I'd like to turn the call back to Mr. Dinos Iordanou for closing remarks.

Constantine P. Iordanou
Chairman and Chief Executive Officer

Well, thank you all. A little late lunch today, but I'm going to enjoy the [indiscernible] along with the team. We're looking forward to seeing you next quarter.

Operator
Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program and you may all disconnect. Everyone, have a great day.