S&P Global
Market Intelligence

Old Republic International Corporation NYSE:ORI

FQ4 2007 Earnings Call Transcripts

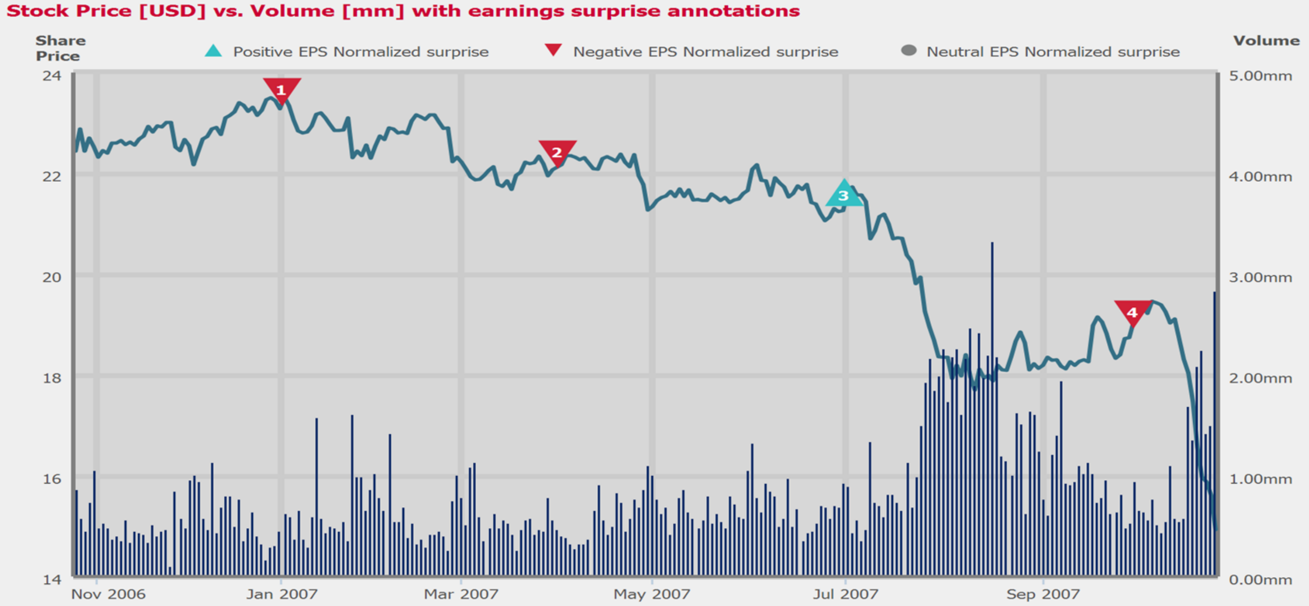
Thursday, January 24, 2008 8:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2007-			-FQ1 2008-	-FY 2007-	
	CONSENSUS	**ACTUAL**	**SURPRISE**	**CONSENSUS**	**CONSENSUS**	**ACTUAL**
EPS Normalized	0.09	0.09	▲0.00	0.12	1.12	1.17
Revenue	-	-	▲7.90	-	-	-
Revenue (mm)	977.70	1054.90	-	960.10	3965.93	4091.00

Currency: USD
Consensus as of Jan-24-2008 5:35 PM GMT

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



- EPS NORMALIZED -			
	CONSENSUS	**ACTUAL**	**SURPRISE**
FQ4 2006	0.49	0.45	▼1 (8.16 %)
FQ1 2007	0.48	0.45	▼2 (6.25 %)
FQ2 2007	0.45	0.49	▲3 8.89 %
FQ3 2007	0.39	0.11	▼4 (71.79 %)

Table of Contents

Call Participants

EXECUTIVES

Aldo C. Zucaro

Christopher S. Nard

Leslie Loyet

ANALYSTS

Beth Malone
KeyBanc

Bill Clark
KBW

Bill Laemmel
Divine Capital Markets

Brian Hagler
Kennedy Capital

Dan Johnson
Citadel Investment Group

Kevin Preloger
Perkins Wolf

Kevin Shields
Deephaven

Unidentified Analyst

Presentation

Operator

Good afternoon, ladies and gentlemen. Thank you for standing by. Welcome to the Old Republic International Fourth Quarter 2007 Earnings Conference Call. Today's call is being recorded. At this time, all participants are in a listen-only mode. Following the presentation, we will conduct a question-and-answer session. Instructions will be provided at that time for you to queue up for questions.

I would like to remind everyone that this conference is being recorded, and would now like to turn the conference over to Leslie Loyet of the Financial Relations Board. Please go ahead.

Leslie Loyet

Thank you. Good afternoon, and thank you all for joining us today for Old Republic's conference call to discuss fourth quarter and year end 2007 results. This morning, we distributed a copy of the press release and hopefully you’ve all had a chance to review the results. If there is anyone online who did not receive a copy, you may access it at Old Republic's website at www.oldrepublic.com.

Before I turn the call over to Al Zucaro, Old Republic's Chairman and Chief Executive Officer, please be advice that this call may involve forward-looking statements as discussed on the Add 6 page of the press release. Risks associated with these statements can be found in the company's latest SEC filings.

With that, I'd like to turn the call over to Al for his opening remarks. Please go ahead.

Aldo C. Zucaro

Thank you, Leslie. And as she just said, you've all seen the release this morning. So we'll just spend a few minutes embroidering on a few points and then again open the call to any questions that may be out there. While we've... as we always say in the single business of insurance, we do manage it through three major segments. As you know… as you may know we also have the small Life and Health operation, which does not amount to very much and that is why we limit ourselves to a discussion of three segments. Those three segments as you can see in the release, two of them went south on us, while the largest part of our business, namely our General Insurance business, produced operating profits that were up moderately year-over-year. Leaving aside the degree of over and/or underperformance, these developments of our business in these three segments, as I say, were very much along the lines we had anticipated early in 2007.

So going from the bottom up in terms of our capital allocation model and therefore focusing on our title business first, it performed somewhat more poorly in the final quarter of the year than it did in the first three quarters of 2007. And part of the performance lapse as you can see stems… or as you should know… I should say it does stem from the natural seasonality of this line since, as you know, housing transactions begin to slow down in the fall and generally do not pick up steam until late winter or early spring. On the other hand, some of it was due to some very pronounced cyclical downturn issues that we are currently experiencing in the housing and the related mortgage lending industries. And finally, some of it was due, particularly in the fourth quarter, to a special charge as you see in the release of about $6 million that we incurred in the process of further rightsizing our direct production facilities in the western states in particular and also most particularly in this case in the Southern California market where we've had the greatest difficulty in turning a profit, both in good times as well as in poor times.

As is generally known, our title businesses is very much of a transaction driven business and the reduced level of home sales and re-sales in these recent times is obviously the root cause of the bottom line problems we are encountering. And in light of the extra $6 million of costs, as I said, that we've just taken out of the business, we currently feel we've got limited opportunities to reduce expenses further to or to any significant extend. So our posture now is to basically hold the fort, if you will, and weather the storm. And in this context, I have to say we are expecting some more hard times for the next 12 months to 15 months, at the least.

Percentage-wise, we don't believe that our title bottom line should drop much further than has been the case in the past few quarters, and most of the downdraft to that bottom line will continue to reflect again the somewhat skewed relationship of our production and maintenance costs on the one hand and of course, the premium and fee revenues line on the other hand, which again as I say is really driven by the extent of housing sales and re-sales. We would get a small or slight uptick in loss costs. As you see throughout, it’s slightly above 7% for the first time in many years. But its effect again should pale compared to the effect caused by the expense feature of the income statement. If there is a defining and good quality in the downturn to the title business is that it does like… unlike most other insurance overages we write, it does have the ability to turn on the dime when new and resale activity turns up. And while there is no single cure out there as you know to right the current, poor state of the housing sector, the recent changes that are taking place on the interest rate front could shorten the waiting period for a turnaround by obviously loosening the lending strings to qualified borrowers and perhaps encouraging once again a greater level of refinance activity, which would be beneficial to the title business.

Let's see, turning to our second largest segment of mortgage guaranty insurance, again we think that this morning's press release touches on all the hot buttons that are affecting the business currently and as we suspect for the foreseeable future. Topline wise, we're beginning to benefit from a resurrection of the traditional primary business as the mainstay of this operation for some time to come, and more importantly the level of persistency that we're experiencing in the high 70s as you see in the release augers well going forward and in combination with new production should propel that topline for some time to come. The type of production we're putting on the books today is marked, I would say, by much more stringent underwriting standards which includes more stringent evaluation of borrower's income and their ability to pay. It's also marked by somewhat lower loan to value ratio loans and I would say by a much greater percentage of product that meets the more stringent requirements of our two big customers… ultimate customers in the presence of Fannie Mae and Freddie Mac.

There is also a modicum of improved terms of trade, as we like to say in the business, or said in other way, there is some premium rate adjustments. Admittedly, it's on the margin and I would not use premium rate increases as the major reason for the better prospects we have at the topline. But nonetheless, it's there and every little bit helps. For… I have to say that for reasons that I am sure everyone who reads the papers or watches the business TV knows, insurance of subprime loans, which in any event have not been a material portion of our total mortgage guarantee business, and production of the so-called bulk insurance, which is typically attached to securitizations, both of those seem to be a thing of the past and should not come back hopefully for several years. And if they do and when they do, hopefully they will come in at a… on a… in a different configuration than has been the case heretofore.

So from a production standpoint, we are now writing more and better underwritten and priced business. We think that we should be able to continue doing this for at least the next couple of three years or so. And as we see it now, our ability and capacity from a capital standpoint to put this new production on the books will be an important counterweight…. or counterweight is as good a word as any, to the higher lost costs we currently expect to incur.

Speaking of loss costs, those have turned out to be the critical determinant of our much downgraded fortunes of late in the mortgage guarantee business. The loss costs we registered for 2007, as you see in the... as portrayed by the loss ratio for the fourth quarter and the full year that’s shown in the press release, those loss costs are of course driven mostly by the reserves we've posted. We didn't put this in… or I guess you can see them in the press release, but if you don't mind writing them down, let me give you a couple of big picture numerical relationships that make this point about the impact… the significant impact that loss reserves are having on the loss costs we are posting.

Between 2006 and 2007, our paid claims went from $155.2 million to $220.5 million last year, and that's up about 42.5%. On the other hand, the year-end reserves we posted went from $249.5 million at year-end '06 to almost $645 million at year-end '07, and that's up a 158%. The year-end '07 delinquency count, i.e. the number of loans that have been reported to us through December 31 as being delinquent for 60 days or more, went from about 25,008 in '06 to 40,900 in '07, and that's 58% higher. And finally, on net risk in force, which is really our calculation of the maximum exposure we've out there for the total book of insurance in force, that was up 24% year-over-year. All of that say that we've looked at our MI book of business from many angles, and at year-end '07 we've again looked at the claims picture with, I'd say, a very critical degree of skepticism.

We think that the judgments we've made relative to such critical variables as cure rates, claim frequency assumptions, and loss severity assumptions are on the conservative side. And we think as a result they should prove reasonable as the delinquencies reported to us at year-end 2007 evolve into paid claims over the next 18 months or so.

But having said that, we still think that it is prudent… even though our loss ratio was less than this number, we still think that it is prudent for us to manage our business in anticipation of generating an average loss ratio of something on the order of 150% during the next couple of years. This compares as you see to about 118%, 119% that we posted in '07. The magic if you will of the two years is that it provides obviously for about a 30-month period of fix-up time starting at mid-year 2007, which is when loss reports really began to accelerate for us as well as from what we can tell the rest of the MI industry. And as we indicated in the fall… in last fall, fall of 2007, in the business review that we usefully do around that time, we are using the last significant cyclical dislocations that was experienced by the MI industry in the second half of the 1980s as a proxy for the general length and the shape and perhaps even the severity of the current downturn. And again as I believe we've indicated before, for that '85 to '89 period the MI industry loss ratio per the MICA, MICA is the mortgage guarantee industry trade association, that the loss ratio averaged about 134% for that five-year period. And for the two worst years of 1986 and 1987, the average was 166%.

Now, it's true enough that the economic circumstances and the product risk configurations then and now are not exactly the same, but we think that experience for those years represents as good a basis for aligning our current expectations or at least as good as the multiplicity of statistics and educated and non-educated guesses that are being bandied about in today's business press.

So with this in mind, our expectations are that for the next 24 months or so the MI business will deliver some pretty choppy results. The models we use show that our committed capital should be able to withstand very nicely the kind of stress that is implied by loss ratios at those levels, particularly in the context of the continuing business. And I would say that the kind of underwriting results that would be produced by loss ratios in the 150% range on an average would obviously serve to raise the risk-to-capital ratio at which we can operate safely, but still remain well below the regulatory constraint of a 25:1 ratio, which has existed for several decades with respect to the mortgage guarantee industry.

Again, if we look back to the high stress years of 1984 to 1989, the risk-to-capital ratios that prevailed for most companies in the industry were in the 21:1 area. They... at least those ratios were not uncommon then, and the MI industry managed itself out of that period very successfully as it was able to bank on better priced and better underwritten business to offset the damage of the prior underperforming book. So the long and the short of what I am trying to say here is that we think that we currently have sufficient capital allocated to our mortgage guarantee line to weather the storm and to enjoy better days from that point forward.

I'll make one other point on mortgage insurance. Those of you that follow Old Republic remember that since our third quarter call we reported a significant investment through open market purchases of the stock of the PMI Group and the MGIC Investment Corporation. The stakes we reported originally in October, November amounted to about 15% for PMI and about 11% for MGIC. Yesterday, we reported an addition to the MGIC investment bringing the total interest in that company to 15%, it’s a little less than 15%. So in the aggregate, our combined investment in those two companies as we speak is about $473 million, almost $475 million, and that's about nearly equally divided among the two investments. Both investments were funded with available monies in our property and liability as well as title insurance companies, and both investments are well within the regulatory allowances for investments in a single investee by each of our insurance companies that constitute those two groups. For obvious enterprise risk management reasons, we did not make any of the investments in MGIC and PMI via the invested asset base of our mortgage guarantee companies.

As we see it, the thinking process is that these investments are part of our overall equity portfolio, which as you see in the summary balance sheet amounted to about $840 million at year-end '07. And as we have indicated in the necessary SEC filings that we are obligated to make, our intent is to hold these equity positions for the long-term viewing them as a passive interest in the North American and far-end MI business of those two largest companies in our industry. One of the ways among several that we've reasoned our decision to make these investments is to view them in the context of our existing U.S. market position, specifically I mean that we now manage directly roughly 11% of the U.S. MI market business through our republic mortgage insurance company and its sister companies with a capital allocation of about $1.25 billion. And now through these two investments, we have an additional albeit passive interest of about 6.5% as an investor in PMI and MGIC combined at a cost of about, as I said before, $473 million.

So we think that the mix of the active and passive aspects of our interest in the MI business make a lot of sense at this stage of the game in light of the fact that we view the industry as being extremely viable and important to the American economy and that it will survive very well and come through this period of dislocation that we are experiencing.

Touching briefly on our largest segment, general insurance, the business ended the year at the lower end of the range of 92% to 94% composite underwriting ratio that we had anticipated early in 2007 when we finalized our budgets for last year. Earned premiums came in as expected, as we indicate… as we've been indicating in our press releases for each of the quarters of '07. Most of the growth that you see there in the teams came from that new book of business that we acquired late in 2006 such that the ongoing non-new business produced about 2% of their balance growth rate.

Most of the coverages we write, and again for us our coverages are mostly in the liability insurance category as opposed to the property side of the business, most of those coverages performed very well from a underwriting standpoint. As I recall, we indicated in our third quarter earnings call, the coverages that we categorize in the so-called financial indemnity line and these include our directors and officers liability, our fidelity and surety, our consumer credit indemnity and a relatively new and growing book of guaranteed asset protection coverage, which are relatively small amount policies that are sold through our automobile warranty channel, that in their totality these coverages did not perform as well. In total, all of them amount to about 14% of our overall general insurance earned premiums. To give you a flavor of the numbers that we will be posting in the 10-K this year for that aggregation of coverages, the loss ratio for them went from 41% in '06 to 70% in '07, whereas as you can see the overall loss ratio for the segment went from about 66% in '06 to about 67.5% in '07. But otherwise, the general insurance business performed very well, again from both an underwriting standpoint and with the growth in investment income and as much as cash flow was very positive and the invested capital base for that business grew some more last year.

Consolidated-wise, as you see in the summary balance sheet provided this morning, our financial condition remains very sturdy and our capital base, which has very little debt in it, we think affords us a great deal of firepower and flexibility and certainly enables us to manage the totality of our business in all of its segments without requiring any additional capital. Tax rates wise, again not much of a change there. As I say, cash flow remains positive all around. We had a little bit of negative cash flow in the title business as you can well imagine with the kinds of results we posted, but again the negativity of it was not very significant.

Having said that, we will once again open this meeting to questions and as we did with the third quarter conference call, I've Chris Nard who is our CEO of our Mortgage Guaranty Insurance companies to join me here in the Q&A section of the call, so that if there are technical questions that I am not on top of then certainly Chris knows his stuff, and so on top of all the details he should be able to answer them very well. So, we will open it up to questions.
Question and Answer

Question and Answer

Operator

Thank you. [Operator Instruction]. We will take our first question from Ron Bobman [ph] with Capital Returns.

Unidentified Analyst

Hi.

Aldo C. Zucaro

Yes, sir.

Unidentified Analyst

I had a couple of MI question, guess it is not a surprise. And I appreciate the loss ratio information that you provided sort of where you think you're going to be booking it in the ballpark in the next couple of years and how you are using the late ‘80s as a bit of a guidepost. And I’m curious if you could with respect to the prime book of business that you ensured in the MI operation, where you see whether it’d be '06 vintage or the beginning of '07, if you could you give relative to risk-in-force for that book, what the loss ratio you think will get to, whether that corresponds to where you are going to be booking it and maybe in stress case where you think that might get… where it could conceivably get to in a stress case?

Aldo C. Zucaro

All right. Let me start, and then I am going to ask Chris to add to the comment to the response to your question. On the big picture basis you are focused… and I can understand why you would be on the 2007 book and what kind of expectations we have for it, but as you know, unfortunately that is the book relative to which we have the least knowledge right now so that what we and all other insurance companies deal with when you are dealing with a new book of business is that you try to apply historical data to the current book and try to make judgments about how that new book might differ to come up to a set of expectations as to, let’s say, what loss ratios will look like. What we do obviously on our book of business is to look at the totality of all the policy used since those are in effect from all intents and purposes, continuous policy use in that we tend to do business with the same assureds and all that happens from one year to the next is that we change underwriting standards and what have you, and as I indicated before sometimes there is some price changes, etcetera. Having said that, I will ask Chris to add a little more color to that.

Christopher S. Nard

Yes. The first thing I would do is echo what Al said, which is the '07 book, which is a large book today is only on an average of about seven months old. It's very difficult to project a book that is on average six months old at this point. On the other side of that, clearly the market is worried about largely the last quarter of the business written in '05, '06, and from our standpoint largely the first three quarters in '07 we felt like the book started to… the market itself started to improve there in the third quarter of '07. So clearly, thus two books represent a large portion of the risk enforced for any of the MI companies, and likely Al gave you that 150% loss ratio number, we still feel pretty good about that number given the size in the early development out of the '06 and '07 books.

Unidentified Analyst

Can you provide a loss figure relative to risk enforced for the prime component of your book, whether it be for the '06 academic year or the portion of the '07… I am trying to sort of--?

Christopher S. Nard

I'd be uncomfortable projecting out that number today. Again, one it is so new, and two as you know the prime book is obviously effected what else goes on in the real state markets. And if you look at the rate decrease in where rates are today, there a lot of change in could come in the next 12 months with that '07 book. I would give you a number that didn't have any certainty around it.

Unidentified Analyst

All right. Well, even your 150% loss ratio doesn’t have any certainty about it, but I’ll move on. I believe that you’ve entered into captive reinsurance agreements. I am curious to know whether those are for the annual calendar year relationships and whether if they are they have sort of been re-negotiated with the terms materially different? I would think there would be cause to do so, but I haven't heard on anything in the marketplace.

Christopher S. Nard

Those are calendar year agreements, and on the main there has been meaningful re-negotiation of those terms.

Aldo C. Zucaro

I mean they are no difference than other re-insurance contracts that we have with other reinsures in the property and liability area or what have you. Those contracts run on the year-to-year. They are typically renewed or not renewed as mutually agreed by the parties. But once the term is all set for a particular calendar year book of business or a policy year book of business, the contracts are typically [inaudible] and therefore the terms are not changed.

Christopher S. Nard

And those are excessive loss agreements.

Unidentified Analyst

Yes, I just would have thought with this sort of the world of pain that the origin years have sort of grained down upon you and us, albeit… you are blind to it, but there has been a world of pain being rained down up you, that the terms of trade, the pricing of the relationship would be, and the structures would be… would want a change, but I guess not.

Aldo C. Zucaro

That has not happened so far. Most of contracts, correct me if I am wrong, Chris, have stayed in place at their original terms. We may have one or two less than the number of the fingers of hand, right, that may have asked us about potentially canceling on a go-forward basis, but certainly not changing the terms retroactively.

Christopher S. Nard

Correct.

Aldo C. Zucaro

Is that all right?

Christopher S. Nard

Yes.

Unidentified Analyst

Okay. And my last question… thanks for your patience. With respect to the MGIC and PMI investments, could you talk a little bit about the ingredients or analysis or thought making as far as making those investments with capital… company capital as opposed to increasing the allocation of buyback of your own stock? Thanks, and that's it from me, and best of luck.

Aldo C. Zucaro

Thank you. I'll address the second point of your question first. Buying back our own stock always involves de-capitalizing the company, reducing its capital. And… whereas making an investment with available investable funds, potentially at least that's what we believe increases the capital of your company if those investments turn out to be good. That's point number one. Point number two, if we were to take the $473 million of investments that we have in our, as I say, P&C companies and title companies, and move that to the... a mortgage guarantee company, we could not on an actively managed basis pick up anywhere close to the 6% of their balanced market share that on a see-through basis we gained through the investments in PMI and MGIC. We obliviously are showing quiet a bit of faith in their management of the business. We think they know what they are doing. We have a pretty good feel since we compete with those companies and the others on a daily basis. We have a good feel. We think about the nature of their book of business. And obviously, just like us we think that they are survivors and are going to do well when this market turns. So those were two of the issues that we focused on when we made those investments.

Unidentified Analyst

Thanks again. And again best of luck.

Aldo C. Zucaro

Yes sir.

Operator

Thank you. We'll take our next question from Beth Malone with KeyBanc.

Beth Malone
KeyBanc

Hi, Good afternoon.

Aldo C. Zucaro

Hi.

Beth Malone
KeyBanc

Just a couple of questions, when you were talking the time at the beginning of your presentation, you talked about the fact that the insuring bulk and subprime markets are no longer out there. I just want to make sure I understand, are you suggesting that you're not... won't be providing mortgage insurance to subprime loans or did I misunderstand?

Aldo C. Zucaro

Well, let me have Chris tell you and everybody else what it is that we're doing today and what it is that we think is out in the market that can or cannot be done from an underwriting standpoint.

Christopher S. Nard

Sure. When we talk about the bulk subprime business, that was largely the business. I'm written to Wall Street firms that then got securitized in the public markets. We largely scaled out of that business in 2000... late 2006, and it has never been a big portion of what we do. And so we haven't written that in a while, and it is the big part of the liquidity that disappeared from the market in '07. So, I think it is suffice it to say that that's not been a very active part of the origination market as a whole, same for the other portion of the bulk insurance business which was the reduced stock business. It again was also a big chunk of the liquidity that disappeared in '07 and I think very little that business is taking place today in the market.

Beth Malone
KeyBanc

Okay. Could…. another clarification, so that business that has been phased out, was that a relatively new phenomenon with this recent run-up in mortgage demand for mortgage insurance that wasn't part of the business, if you go back a few years or certainly when the markets had their other problems earlier that you were referencing?

Christopher S. Nard

Yeah, I would tell you the bulk businesses probably started to develop in '02 maybe, a lot later '01, but then certainly gained its footing in '03, '04, '05, peaked in at late '05, early '06, and then tapered down from there.

Beth Malone
KeyBanc

Okay. And then in terms of where you are seeing the most delinquencies, is it somewhat concentrated on the West Coast or are there certain markets that you are seeing more problems than others?

Christopher S. Nard

Well, I think if you look to what you hear largely in the press, it affects us all the same way. I think we all refer to it a little differently. But most people are concerned about the deterioration in Florida and California. Those were sort of the more recent trouble spots and then the ongoing troubles that everybody has had in the upper Midwest, particularly Ohio and Michigan. So, if you look at the recent increases and losses the industry suffered, it's really from the onset of a slow market in Florida, California, and then a little slowness in the other half markets obviously, Nevada and Arizona.

Beth Malone
KeyBanc

Okay. All right. Thanks.

Christopher S. Nard

Sure. Thank you.

Operator

Thank you. And we will take our next question from Dan Johnson from Citadel Investment Group.

Dan Johnson
Citadel Investment Group

Great. Thank you very much for taking my call.

Aldo C. Zucaro

Hi, Dan?

Dan Johnson
Citadel Investment Group

Good afternoon, sir. Question about the outlook when you think about the next two years and how the roll of captives may play in your reported loss ratios? I mean I guess I have my own set of assumptions, but I would be very interested to hear, if you think that those captives will be called upon in '08 and '09, and if that has any impact in '08, the '08 loss ratio on a reported basis will look relative to '09, even if on a gross basis they are sharing similar levels?

Aldo C. Zucaro

All right. Let me just say first of all, before I ask Chris to embroider on that. When we throw out that 150% shorthand loss ratio Dan, that's a net loss ratio. So inherently, it is inclusive of any NOL recoveries that we may get from the captives. In terms of the numbers as they will come through the income statement, I will ask Chris to give us a idea of what our current thinking is as to the timing of those recoveries from the captives.

Christopher S. Nard

Sure. What we would anticipate is those captives will begin to support us in a more meaningful way, late in 2008, later this year and then really come online, it's a claim paying benefit in 2009. It's a little… it can be a little bit tricky to forecast exactly when you will pierce these layers, because each book with each large lender has a little different flavor to it, be it geographically concentrated based on where the lender originated most of their products or the various types of products that lenders do, but again we think they will start to provide more benefit later this year and then come online more meaningfully in '09.

Dan Johnson
Citadel Investment Group

And is there much time lag… I guess this is a liquidity question between when you need to make the payment on a gross basis and when you can draw on the cash.

Christopher S. Nard

No.

Aldo C. Zucaro

You mean, from the captives you're talking about.

Dan Johnson
Citadel Investment Group

Yes

Aldo C. Zucaro

Yeah, yeah, Chris said no.

Dan Johnson
Citadel Investment Group

And then finally, when you look at the performance of the delinquencies within the quarter, can you talk about what you're seeing from the monthly performance, say in December relative to what we were seeing maybe overall on average, other words, are we seeing us exit 2007 on sort of an accelerating basis?

Christopher S. Nard

You mean an absolute number of delinquents?

Dan Johnson
Citadel Investment Group

I guess, however you want to put it into. I guess I'd think more in ratios base just to normalize for any growth although maybe that's not that big as a deal on the quarter, but I guess, however you would want to think about answering the question.

Christopher S. Nard

Delinquencies, I mean the easy way to answer that is delinquencies have increased throughout the quarter and I will reference back to Beth's question which was the meaningful part of those increases have come out of the deterioration in Florida and California and then again some continued softness in the upper Midwest. So, why we wouldn't forecast when any of those economies will turn around, certainly they will continue to be weak through the bulk of '08.

Dan Johnson

Citadel Investment Group

And then finally with the outlook that you have, I know there's a lot of sensitivity of this business around unemployment. Can you talk a little bit about what sort of unemployment environment you're using when you think about the loss outlook that you've given to us? Thank you very much for the question.

Christopher S. Nard

Yeah, I would tell you that forecast, that it is built on a… not built on a lot of job growth. In fact it's basically in the short run a flat to slightly down job environment that backups those numbers.

Dan Johnson
Citadel Investment Group

Thank you.

Operator

Thank you and we will take our next question from [inaudible] with Raymond James.

Unidentified Analyst

Hi. I just wanted to have a little bit more color on the mortgage insurance, the net premiums on growth, yet a double-digit growth in '07. Do you think it is going to be like that in '08 as well?

Aldo C. Zucaro

Chris, you want to take it?

Christopher S. Nard

Sure. The market for private mortgage insurance, I think has benefited strongly by this dislocation in the mortgage market, I think it's shown the value of the primary mortgage insurance market to originators and investors around the world, and that has gone a long way towards increasing the MI penetration rate, which is the amount of loans done in the marketplace that have mortgage insurance on it. Two, closed to record highs, I think it’s the lowest point about 6% of the market had primary insurance on it, and maybe mid-to-late '05 and I think we are running in the mid-to-upper teens today.

Aldo C. Zucaro

Wasn't it around sixteen point something at the end of September 1st.

Christopher S. Nard

Yes, it sounds all right. So, we would expect now whether it stays at those record high levels or not is yet to be seen, but we would expect continued good penetration rate in the market because our largest competitor which had been the piggyback business, where the borrower gets a first and second mortgage to avoid mortgage insurance is largely a structure that's not out there in the marketplace any longer.

Unidentified Analyst

Okay. And then on to general… the insurance business, do you any combined ratio goals for this year?

Aldo C. Zucaro

We think that as you saw... as you see there for the fourth quarter a little bit of an inching up. We think that most of our coverages are going to show some loss ratio growth for the simple reason that we've had in the last 2.5 years compounded, perhaps we've lost maybe 7%, 8% of the premium rate through rate cuts of one sort or another. So that of itself is going to... should show an increase in the loss ratio for 2008. We don't have our budgets finished yet for '08, but the... I'll stick my neck out and suggest that whereas at the beginning of '07 we were suggesting a 92% to 94% combined ratio, and we came in slightly before... below that 92%, as you can see. That I would... I would say that a 93% to 96% is probably a better range for 2008.

Unidentified Analyst

Okay. That's helpful. All right. Thank you.

Operator

Thank you. [Operator Instructions] And we will take our next question from Kevin Preloger with Perkins Wolf.

Kevin Preloger
Perkins Wolf

Hi, all. How are you?

Aldo C. Zucaro

Hi, Kevin. Good, yourself?

Kevin Preloger
Perkins Wolf

I am doing all right.

Aldo C. Zucaro

Good.

Kevin Preloger
Perkins Wolf

Well, a few questions and I will ask at a different way, just on the buyback and then I guess, looking at the magic in PMI stakes, and both have losses and I think the scenario that you're paying out for the next 24 months or so looks to be pretty ugly. And you see the losses mounting there at those two firms and the capital raises probably seem inevitable, and you just wonder what the dilution is going to be there. In addition, book value is going down. Now, look at Old Republic stock and see that you guys have been growing book value through this and buying back stock now, that's 30% discount. The book would seem to be like a pretty good investment at these prices, wouldn't you agree?

Aldo C. Zucaro

Well, as I said before Kevin, when you buy back your own stock you are de-capitalizing the company, and we don't think that this is a time to de-capitalize Old Republic. I mean, as I indicated before we think that given that scenario that we've painted for the mortgage guaranty business of let's say, we've used a shorthand of 150% loss ratio, this is going to be... this is going to have a negative effect on its capital and we may need to do some capital reallocations within the system. Currently, we think based on our understanding of what our customers, rating agencies and so forth, are looking for in the mortgage guaranty area, we think we are going to be allowed to run those businesses at a higher risk to capital ratio, but the question is going to be, how high is high? As you know, as I believe I may have said, from a regulatory standpoint, the bogie is 25 to 1. However, we think that the ratios at which we were operating back in the ‘80s, the last significant stress period of 21 to 1 is probably a max. And if that bears to thought should we achieve them, we are going to need capital. So again, this is not the time when you part with capital. You saw us, in the 3Q buyback small amount of our stock, but then when we saw the developments, they were going, we said to ourselves, we keep our powder dry right now.

Kevin Preloger
Perkins Wolf

But I guess dry powder in investment portfolio given what those two companies have done, I mean I guess I look at it as a Old Republic shareholder where, to make my bed in the mortgage insurance space, I put that capital on you guys because I think that you are going to survive because you have the stronger balance sheet and are better underwriters versus those other two because I haven't invested my money with the others because I don't think you know what book value is and I don't think you know if conceivably if they are around if they're going, it's really tough over the last 24 months?

Aldo C. Zucaro

Yeah, well again I think we could have pretty good argument as to what they are going to do and not do and I don't know any more than you do about that, but the assumption we are going on now Kevin is that we're all going to be allowed at least the rating agencies are not making noises about cutting back on ratings that we are going to be allowed to write more business at a higher risk-to-capital ratio. And the very fact that we have made what we... for us are significant investments in those companies should tell you that at least we believe that they are going to be survivors and that if they do issue more capital of one sort or another that we don't think it's going to dilute us below the cost at which we acquired those stocks.

Kevin Preloger
Perkins Wolf

Well I guess just one final point now. I'll leave it alone, but I think that clearly there is... there has been and continues to be some crisis of confidence here and in the mortgage insurance space and I think it does send a pretty good signal. I know you do have a balance sheet better than the rest of the industry, but that buying back stock would send a good signal that you're committed to your business as well and feel pretty good about your book of business while maintaining I think significant capital, you will be able to write new business, when it comes on the pipe.

Aldo C. Zucaro

Right. Well I'll just add one point Kevin and you've been around Old Republic as you say for a long time now. And I think you understand how we think. If it came back to getting rid of capital, you know that we have strong feelings that that capital should be given back to all the shareholders not just a few which is what happens when you buyback your own stock because again you de-capitalize the company and you are just making it easier for others to exit the stock. If we have money burning a hole in our pocket, we say okay, we will give it to all the shareholders as we did back in when was it? 2003 and we did again in 2005. But at this point in time, we think that the combination of potentially or fully increasing our dividend steadily, the regular dividend steadily and keeping some of our powder dry is the right thing to do in terms of the long-term interests of our shareholders.

Kevin Preloger
Perkins Wolf

Great, thanks Al.

Aldo C. Zucaro

Yes sir.

Operator

Thank you. And we are going to take our next question from Bill Laemmel with Divine Capital Markets.

Aldo C. Zucaro

Hello. Bill Laemmel.

Bill Laemmel
Divine Capital Markets

Hello. How are you Chris?

Christopher S. Nard

Hey, Bill.

Bill Laemmel
Divine Capital Markets

Good to hear your voices. Well, what you are telling me is that your market share is going to go up, is that going to be your assumption in MI?

Aldo C. Zucaro

Well, this is what we try to do all the time provided we can grow it in the right spaces in areas where we think we can make a buck.

Bill Laemmel
Divine Capital Markets

Okay. So that's a possibility here. Also, ultimately, can you just quickly trace the 178 claims ratio in the MI, how it affects prices going forward?

Aldo C. Zucaro

The 178, I am not sure.

Christopher S. Nard

Yeah, what do you mean by affects prices, Bill? Affects insurance prices?

Bill Laemmel
Divine Capital Markets

Yes, [inaudible] prices.

Christopher S. Nard

Yeah, well, I think as Al mentioned earlier, we really are attacking the terms of trade on several dimensions, one obviously being guidelines. So, first off, take out of the mix, the products that are affecting us negatively that we don't see alike, you could really price at any level, and as we mentioned, what you see being chased as a marketplace today is a lot of the subprime, a lot of the reduced stock and the very high LTVs. Then the next dimension we would tackle at on is price. Now one thing I think about is we file rates with the various states and they have to be approved, you have to justify the rate increases on the bulk of the business. So, the rate increases that we have put in place are largely on the higher risk products that still remain in the marketplace. On the lower LTVs, higher credit products where the performance is still pretty stable those are largely still priced down as they were last year.

Bill Laemmel
Divine Capital Markets

All right. Thank you. And are your inflation assumptions in your loss reserves over general insurance business, are they going up or down?

Aldo C. Zucaro

They have been pretty stable the last few years, Bill, including the medical portion because inflation, general inflation, as you know, has been under maps [ph], and we have not seen the effect of inflation to a much more significant degree than we did let's say back in the 1990s and even the early part of the 2000s.

Bill Laemmel
Divine Capital Markets

And thank you very much. And Chris, one last question. Now you get a claim and then you reserve it in MI, and then you are paying a loss course, is there a general time lag between that event?

Christopher S. Nard

Yeah, it takes about eight… I'll put it to you the whole time line. It takes about generally 18 months or so between the notification of delinquency to us and the ultimate payment of the claim.

Bill Laemmel
Divine Capital Markets

Okay.

Aldo C. Zucaro

Of all the claims.

Bill Laemmel
Divine Capital Markets

Yes, and thank you very much. I appreciate it.

Aldo C. Zucaro

All right.

Christopher S. Nard

Thanks, Bill.

Operator

Thank you, and we will take our next question from Stephen Mead with Anchor Capital Advisors.

Aldo C. Zucaro

Hi, Stephen. Hello? Stephen.

Operator

Mr. Mead, your line is open, please check your mute function. Thank you, and we will take our next question from Brian Hagler with Kennedy Capital.

Brian Hagler
Kennedy Capital

Good afternoon.

Aldo C. Zucaro

Yes, sir.

Brian Hagler
Kennedy Capital

Maybe to switch gears a little bit to the title business, I guess looking at your direct orders open, they were down 25% year-over-year. Can you just kind of talk about what you have seen kind of in January was it a drop in the ten-year or maybe what you would expect to see if the ten-year stays in 350, 360 range?

Aldo C. Zucaro

As I think, I tried to say briefly in my opening comments, there's no question that as these lower interest rates take hold and you that you start seeing the primary come down etcetera, etcetera, that you should have a greater opening for refunding its activity and hopefully even greater activity ultimately in the extension of mortgage loans, which certainly make the mortgages, the cost of the more affordable to more people. Have we seen that yet? There is indications here and there that some people are getting a little more excited and after moving down the road with commitments, but no, nothing hard yet. But I mean the... let's put at this way, the lowering of interest rates is a positive thing ultimately for the Title Insurance business at an earlier date than it is for the mortgage guaranty business.

Brian Hagler
Kennedy Capital

Sure. Okay thanks. I appreciate it.

Operator

Thank you. And we will take our next question from Bill Clark at KBW.

Bill Clark
KBW

Good afternoon.

Aldo C. Zucaro

Hi Bill.

Bill Clark
KBW

Speaking with the Title business, I know you mentioned in your opening comments about sector-limited opportunities to reduce expenses going forward. Can you give any perspective for the expenses in the fourth quarter, the kind of breakout what’s variable and what's the fixed cost? Is there anything you can kind of give us any indication there?

Aldo C. Zucaro

I don't have those numbers in front of me Bill, but basically as you know we've got roughly still about 65%... excuse me of our Title business written through independent agents, so the lion share of the cost, the tendon to that is variable. The rest of it is where, we have the issues with cost cutting and so forth. But as I say, I'll have to get back to you with an indication of what percentage of our total cost is variable versus fixed.

Bill Clark
KBW

Okay, thank you.

Aldo C. Zucaro

Yes.

Operator: Thank you. And we'll take our next question a follow-up from Beth Malone of KeyBanc.

Beth Malone
KeyBanc

Okay, thank you. Yeah, just a follow-up question on the Title. There was an uptick in the loss ratio on the Title, would you anticipate as we work through this that that’s going to be the case going forward in 2008 that we can anticipate that will continue to have that higher loss ratio?

Aldo C. Zucaro

Beth, if you go back to our numbers quarter-to-quarter or even year-to-year over the last five years, you will see that the loss ratio ended up around 3.5%, 4%, couple or three years ago. And at that time we said that lower loss ratio could not be sustained and that we expected loss ratios to uptick in the 5% to 6% range over time and we did that in effect between '05 and '06, and between '06 and '07, it has gone even further up as you have noticed to what was it 7.2% I think for the latest period. My gut for it's worth tells me that it might enchant [ph] a little bit more than that, let's say 7.5%, I would be very surprised if it goes to 8%. And that will be a reflection of the markets we were in where when they were claims, when there are problems with the loan, people start looking around to see if there is a scapegoat around and title companies will get growing. And so I think some of it... some of that is what's driving up the loss ratio currently and maybe for the current year 2008, but I think it should revert back to 6% of thereabout area.

Beth Malone
KeyBanc

Okay. Does that suggest then that this kick-up in the loss ratio in not so much an underwriting issue as it is a change in claims or claim severity?

Aldo C. Zucaro

I think it's a change in the economic circumstances, which is what I was trying to say before when the housing etcetera hits the skids, it tends to be a little more claims, and other thing that happened to a significant degree in Title Insurance, and I have to say in mortgage guaranty as well is that when… we went through a period of high refinance activity, and a lot of problems that may have been there with loans or with the Titles, it got swap by the continual refinancing of some of the product. And when the music stops, then the people have got to own up to some of the problems that maybe genetically imbued into and some of these loans. So I think that's what we are seeing now. We've had the same experience in prior downturns whether it is as a result of frauds or now fees and so one sort or another, and it will blow over. The other thing we've had going for us in the Title business for many years has been the fact that we re-priced and re-reserved that business back in the late '80s and benefited from that throughout the 1990s. And of course we're not getting as much of a benefit from that because now the business has leveled out... leveled off sort to speak and so the experience is leveling off as well from a loss ratio standpoint.

Beth Malone
KeyBanc

Okay. Thank you.

Aldo C. Zucaro

Yeah.

Operator

Thank you. And we'll take our next question from Kevin Shields from Deephaven.

Kevin Shields
Deephaven

Thank you. I had two quick questions. My first question was, what percentage of risk in-force in delinquencies now come from California, Arizona, Nevada, and Florida in aggregate?

Aldo C. Zucaro

Do you have those numbers broken down, Chris or--?

Christopher S. Nard

Yeah, I have got the third quarter 10-Q in front of me, if you looked at our primary traditional, primary risk in-force, which is the bulk of our risk in-force, Florida, third quarter '07 was about little less than nine, California was about 3.5 and then the other states don't hit our top ten risk in-force states.

Aldo C. Zucaro

And those are nine theory numbers, but we don't expect those to change significantly.

Christopher S. Nard

No, those risk in-force moves are more glacially where as new insurance written can move pretty well quarter-to-quarter.

Kevin Shields
Deephaven

And in the delinquency category for those states would they equal or be still under the market share?

Christopher S. Nard

Again we've reported for that same period third quarter '07 total delinquents for the top ten states, Florida is in a 5% range, little over 5% and California is about 5%.

Kevin Shields
Deephaven

Okay.

Christopher S. Nard

Again those are the ones don't rate in the top ten states.

Kevin Shields
Deephaven

My second question real quickly if the GSE conforming loan limits was increased to something like 600,000 and assuming that it was temporary in nature, would you guys participate and follow Fannie and Freddie, it seems to me that temporary nature that's been proposed would be problematic?

Christopher S. Nard

Well, we don't have, I am not exactly sure in this question, we don't a loan limit per se that follows the GSE limits. So, we ensure what we call conforming loans under the GSE limit and we also ensure jumbo loans although it's a small percentage of the book. An increase in the GSE loan limits will certainly bring more liquidity back into the marketplace and we would support that either temporarily or on a long-term basis.

Kevin Shields
Deephaven

Thank you.

Operator

Thank you. And we will take a follow-up question from [inaudible] from Raymond James.

Unidentified Analyst

Hi, I just have a quick investment question. Looking at the investment section, you have maybe slightly over a billion of munibonds, what percentage of that is insured, and what's the underlying credit qualities?

Aldo C. Zucaro

Yeah, I don't have the answer to your first question, although I have to say that, maybe I can be corrected on this that most of the munibonds that we buy nowadays tend to have some sort of insurance on them from MBIA in particular. As to the quality of the portfolio, that's shown in one of the tables in either on annual review or the fall -- analysts review that's posted on our website. And that call the mix of securities whether it'd be munis or corporate has not changed dramatically for us for many years. It's still AA average rated portfolio.

Unidentified Analyst

Okay, thank you.

Operator

Thank you, and we will take our final question from Rob Bobman [ph] at Capital Returns.

Unidentified Analyst

Hi, thanks a lot. What's the, I am sorry if I missed it, the average cost on the PMI and magic investments?

Aldo C. Zucaro

We didn't give the cost on each, we gave the cost on both of them combined and that was $473 million I believe I said and that we further indicated that it was about evenly split among the companies, and both companies as I say we have 15% or something shy of that.

Unidentified Analyst

Is there any sort of or you… I mean are you sort of effectively at a limit here as far as how much appetite you have and capital you have to buy more any sort of practical constraint that's been a sort of--

Aldo C. Zucaro

On those two companies?

Unidentified Analyst

Yeah, on those two.

Aldo C. Zucaro

Well, we are very respectful of the fact that there is a shareholders right plan in place in both companies at the 15% level. And therefore we would be... we would not being inclined to exceed that percentage.

Unidentified Analyst

Solely for that reason?

Aldo C. Zucaro

Yes, sir. They would be immediately dilutive to us, and I would say... kind of counterproductive.

Unidentified Analyst

Right, right, right.

Aldo C. Zucaro

Again we are happy with the amount of money, I mean $400 million, almost $500 million for us, even though we have got a very good balance sheet and a great investment portfolio, there is still a lot of money. And therefore... we're happy with what we've got there.

Unidentified Analyst

Okay. Thanks a lot.

Aldo C. Zucaro

Okay.

Operator

Thank you. And that concludes today's question-and-answer session. I would like to turn the conference back over to Mr. Al Zucaro for any additional or closing remarks.

Aldo C. Zucaro

Well, thank you. I don't have any more comments to make. I again appreciate Chris' input as always in this and certainly appreciate yours inviting... being coming to visit with us on this fourth quarter call as you have in the past. And with that I will say good afternoon to you all.

Operator
That concludes today's conference. Thank you for your participation. You may now disconnect.