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WRB - Q1 2016 W. R. Berkley Corp Earnings Call

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PRESENTATION

Operator

Good day and welcome to the W.R. Berkley Corporation's first-quarter 2016 earnings conference call. Today's conference is being recorded. The speakers' remarks may contain forward-looking statements.

Some of the forward-looking statements can be identified by the use of forward-looking words, including, without limitation, believes, expects or estimates. We caution you that such forward-looking statements should not be regarded as a representation by us that the future plans, estimates or expectations contemplated by us will in fact be achieved. Please refer to our annual report on form 10-K for the year ended December 31, 2015 and our other filings made with the SEC for a description of the business environment in which we operate and the important factors that may materially affect our results.

W.R. Berkley Corporation is not under any obligation, and expressly disclaims any such obligation, to update or alter its forward-looking statements whether as a result of new information, future events or otherwise. I would now like to turn the call over to Mr. Robert Berkley, President and Chief Executive Officer. Please go ahead, sir.

Robert Berkley - W. R. Berkley Corporation - President & CEO

Okay, thank you, Bridget, and good afternoon everyone, and again welcome to our first-quarter call. So on this end of the phone I am joined by our executive Chairman Bill Berkley, as well as our Executive Vice President and Chief Financial Officer Gene Ballard. The game plan for the call today is - I'm going to start off by offering a few comments on the marketplace, a couple of sound bites on how I see we see the quarter.

Then Gene's going to be running through the numbers with you all, and then the three of us will be available to address any questions that you may have. So with regards to the market, by and large the natural continuation of what we saw in the second half of last year. The insurance marketplace continues to become incrementally more competitive while the reinsurance marketplace seems to be coming gradually a little less intensely competitive, though that is a very incremental change.

Having said this, while it may seem as somewhat business as usual, there are a couple of events that are worth noting, that from our perspective could impact the marketplace and not in an immaterial way. First of all, I think at this stage everyone is reasonably familiar with the recent cat activity that not only went on during the first quarter that was certainly setting up the second quarter for a material series of cat losses, as well for the industry. Second of all, something we touched on last quarter, there is a fair amount of dislocation in the marketplace that is stemming from the degree of reorganization as well as M&A activity, and I think we've been talking about this again for a couple of quarters at this stage, and we are starting to see it really materialize in a distraction for some and an opportunity for others.



And then finally, we are seeing a bit of a change in the reinsurance marketplace, and if there was ever a part of the industry that deserved a break, it was probably the reinsurance market these days. And that is, a few years ago we started to see a change in buying habits of some of the largest purchasers of reinsurance. Ultimately they ended up increasing their intentions and reduced the amount of reinsurance they bought in a pretty dramatic way.

Loss activity has come through, and as a result of that it would seem as though they are yet again changing their habits and they are reentering the marketplace as customers. So again, I don't think that that is a silver bullet for the reinsurance market, but may be helpful in the balance between a supply and demand. One other comment in the broad sense about the marketplace, and again something I mentioned last quarter, and it has to do with the balance of the relationship or perhaps the tension at this stage between distribution and carriers.

Something that we've been paying attention to and have been actually taking notice of for some time - there seems to be a growing level of tension between carriers and distribution. And ultimately we are concerned that this is actually going to become more and more pressurized as the insurance marketplace becomes more competitive and pricing potentially gradually erodes.

Moving on, to the Company and its performance during the quarter and I'm going to keep my comments brief, otherwise my colleague Gene gets quite cross with me. So from our perspective, pretty solid quarter, good way to start out the year. The growth coming in at about six points, of that about one point was associated with rates.

Certainly growth is something we pay a lot of attention to, we want to make sure we understand it, we want to make sure that is well-controlled. And I'll share with you a couple of high level metrics that we look at to make sure we have our head around the situation. So for starters, we have a look at our renewal-retention ratio which has consistently been around 80%, and it remains at that level.

And another metric that we look at is - we try and make sure we understand the pricing or the rate that we're charging for new business and we compare that rate for our new business to what we would be getting on a renewal business. And to make a long story short, we are charging an incremental premium above -- or an incremental additional premium for new business when compared to the renewal business. Giving us a degree of comfort that the integrity of the book is remaining intact, and we are not buying business or burning our way into the market in any way, shape or form.

I know we've talked a bit about how the market is becoming more challenging. From our perspective, there are still a number of opportunities out there and we think our structure lends itself for us to be able to be a bit more nimble - to use a bit of a scalpel or a laser as opposed to a cleaver. So what Gene is going to be talking about where we've grown, but having -- and he may speak to it in somewhat of a broad sense, but I would recommend or remind you that the growth is really in a very granular level, where its operating unit by operating unit in particular divisions.

And for that matter, there are some parts of our business that have grown dramatically and there's certainly plenty of parts of our business that actually are shrinking. With regard to the loss ratio, 60:4, in line with our expectations. Certainly, we did have some storm activity, but again, not anything extraordinary or beyond what we would have expected for the time of the year.

Cat activity certainly can exist in the first quarter, and has historically for us, but its not an overwhelming number. Part of it goes to perhaps a little bit of luck, but I think by and large, us not having a larger or more outsized loss stemming from cat activity in the first quarter has more to do with our strategy around how we manage cat and how we think about volatility and make sure that we are getting paid appropriately for it.

Expense ratio to 33:1 may on the surface appear to some as though we took a bit of a step backwards compared to the first quarter of 2015. Having said that, if you normalize that number again -- Gene will be sharing some numbers with you shortly. I think it's actually very much in line and it is certainly an improvement from what was on the second half of 2015.

The reserves continue to develop to the positive, yet I think we are up to something along the lines of quarter number 37 of net-positive development at this stage. Having said that, it's really just a reflection of the approach that we take to setting reserves. Our view is that we want to err, if we are going to err, on the side of caution with the initial pick and as those reserves season out and we have more information we will tighten up those picks.

Couple other comments on the investment front - certainly kudos to our colleagues that are managing the investment portfolio. Our yield at the end of the quarter, compared to the end of the -- rather, I'm sorry, our duration at the end of the quarter compared to the end of the year had shortened up a bit from 3.3 to 3.1 while they were able to maintain the same level of yield, as well as the same quality. And then finally, a couple of comments, and you may have picked this up and our K, that we filed recently, we started in six new operations during 2015 and we've announced one new operation, that perhaps for some, was particularly noteworthy this year, and that is organizing and planning to enter a particular niche within the personal line space.

When we first made the announcement, we got a few questions around - why would you be going into the personal line space? Ultimately our view is that this piece of the personal line space is no different than, quite frankly, much of our overall strategic plan. And that is to focus on specialty products, specialty lines, where ultimately its knowledge and expertise which is how one differentiates themselves and ultimately focusing on a customer base and a distribution where they are willing to pay for the service and expertise.

So I'm going to pause there and I'm going to hand it over to Gene and again, our Chairman and myself will be available to join Gene for any Q&A once he's done. Thank you.

Gene Ballard - *W. R. Berkley Corporation - EVP & CFO*

Thank you, Rob. Well, as Rob said, we started the year with another solid quarter with operating income up 8% to \$115 million and operating income per share up over 11% to \$0.89. The improvement over a year ago was attributable to a 12% increase in underwriting profit, a 5% increase in investment income, and a 3% decrease in the average number of shares outstanding.

Before I go through the numbers, I want to mention you'll see on page 5 of the earnings release that we have combined the domestic and international businesses into one financial reporting segment. Background of that is that when we established those segments a few years ago, the domestic segment wrote essentially all of its business in the US and the international segment wrote nearly all of the business outside of the US. But since then our profile is very different. It's very different today.

Now our largest international company, which is our Lloyd's syndicate, for them the majority of their risks are actually located in the US, and for 11 of our US profit centers, that are now insuring risk outside the US, in 2016 - and we expect that to grow significantly in future years - so that the distinction between the two segments was becoming less meaningful and we decided to put them together. We've posted a schedule on our website that presents the five-year historical underwriting results for the new insurance segment.

Okay, going back to the release then, overall our net premiums written increased by 5.6% to almost \$1.7 billion. For the insurance segment, premiums increased 4.5% to almost \$1.5 billion. The growth was led by a 21% increase in workers' compensation business, with significant increases from both our mono-line work comp company as well as our specialty businesses.

Professional liability lines were up 8.5%, and property and other short tail lines were up 1.5%. On the other hand, commercial auto -- for commercial auto, premiums were down 7% as we continued to emphasize higher rates, and other liability business was down 5%. For the reinsurance segment, the premiums increased 16% to \$175 million with strong growth in the US [tree] business, and that's primarily due to growth in structured property reinsurance.

I mentioned these before - these are structured businesses that has very limited cat exposure and carries a lower than average loss ratio that is partially offset by higher profit commissions. Our overall underwriting profits increased 12% to \$100 million and a combined ratio improved by four tenths of a point to 93.5. Our current accident year loss ratio before cat activity, was 60.2%, down almost one point from a year ago.

Catastrophe related losses were \$16 million. That represents one loss ratio point and is right in line with cat loss ratios for the first -- for both first quarters of both 2014 and 2015. Loss reserves developed favorably by \$12 million, with nearly all the improvement in the insurance segment, and as Rob said, that's now our 37th consecutive quarter with positive development.



That gives us a calendar year loss ratio of 60.4, down 8 tenths of a point from a year ago. Our overall expense ratio for the first quarter was 33.1, compared to 32.7 in the first quarter of 2015. The insurance segment expense ratio was 32.5, that's up a 10th of a point from the first quarter 2015 but slightly below the run rate for the last three quarters of 2015.

And 2016 first quarter expense ratio includes 3 tenths of a point that are directly related to the six business initiatives that Rob referred to. So if you normalize the expense ratio for those investments, the ratio for the first quarter actually declined compared to the prior year by 2 tenths of a point. The reinsurance segment expense ratio increased almost 2.5 percentage points to 32 -- 38.2 - that increase was due primarily to the growth in the structured property business that I mentioned earlier, as well as to slightly lower overall earned premium volume for the segment.

Investment income was up \$6 million or 5%, to \$130 million, three main components to that first income from fixed-income securities was up \$1 million to \$109 million with an annualized yield of 3.3%, which is unchanged from the first quarter and the full year of 2015. Earnings from investment funds were up \$10 million to \$17 million, due primarily to improved results for energy funds. That gave the investment funds an annualized yield of five point -- 5.5% for the quarter, which is in line with our target for investment funds.

The third item, income from all other investments declined by \$6 million, due to above-average returns for the merger arbitrage account in the first quarter of 2015. At March 31, 2016, unrelated investment gains were \$258 million - that's up \$77 million from the beginning of the year. The average rating was unchanged at a double A-, and as Rob mentioned, we shortened the portfolio from 3.3 years in December 2015 to 3.1 years at March 31, 2016.

The overall tax rate was 31.1 which is unchanged from the overall tax rate for the full year of 2015. That gives us net income of \$115 million and overall return on equity of 10.4% and for comparison purposes, a pretax return on equity of 15.2%. Also during the quarter, we repurchased 734,000 shares of our own common stock for \$37 million, and for the first three months of the year, our book value per share increased \$1.44, which is an increase of 15.4% on an annualized basis. Thank you.

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

Thank you, Gene. Okay, Bridget, if we could open it up for questions.

QUESTIONS AND ANSWERS

Operator

Michael Nannizzi, Goldman Sachs

Michael Nannizzi - *Goldman Sachs - Analyst*

Thank you. Rob, one question on the reinsurance business, what drove the lift in premium there? First time we've seen double digit increases in reinsurance for some time now, so I'm just curious is that something that you expect will continue and is reflective of opportunities you see in the market?

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

I think that it's unclear as to what exactly tomorrow will bring, Mike, as far as the growth, or the spike that you saw in the quarter as far as the reinsurance, that really came from a couple of unique opportunities, as Gene had suggested earlier, on the property front where we entered some structured deals that we think are particularly attractive. But ultimately, it's unclear as to what the opportunity will be from the reinsurance marketplace, as I had suggested earlier, as we'll have to see what the impact is of some of these historically very large buyers having exited in the past and they are entering so no I don't think you should necessarily assume this is the new run rate.

We are an opportunistic participant if we think that we can make a reasonable return we are prepared to participate, but this was, I think, somewhat of a one-off unique opportunity.

Michael Nannizzi - *Goldman Sachs - Analyst*

Okay. And then can you give us - thanks for that - a little bit more on the merger, Gene, trying to square everything up here. Can you tell us what you earn there?

Gene Ballard - *W. R. Berkley Corporation - EVP & CFO*

Yes, it was positive earnings, it was about \$3 million for the quarter.

Michael Nannizzi - *Goldman Sachs - Analyst*

About \$3 million for the quarter. Okay. Got it. And then any impact from market movements in the -- now you -- you are current quarter marks on your private equity, is that right? So your -- (multiple speakers)

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

Our private equity is carried in two ways. There's some private equity investments where we are the vast majority owner. We own the vast majority of it, we carried any equity basis for accounting therefore, the only increase we show is our proportionate share of the earnings of the enterprise.

Those private equity investments, which is very small, where we're just an investor, we mark to market.

Michael Nannizzi - *Goldman Sachs - Analyst*

I see. Got it, okay and then just last one -- (multiple speakers)

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

Health equity would be an example where we don't mark to market either way - we carry it in cost which is sort of give or take \$25 million and whatever our program share of the earnings are is what we gain from it

Michael Nannizzi - *Goldman Sachs - Analyst*

I see, okay thank you. So when you called out that statement upfront, where you talked about \$100 million or more of annual gains? So in that, are you sort of including some proportion or some piece of the health equity unrealized gains or unaccounted for gains?

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

I'm not - I'm not -- Michael, we own a large amount of invest -- real estate for investment purposes.

Michael Nannizzi - *Goldman Sachs - Analyst*

Okay.

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

You know we own health equity as well as a number of other private equity investments, and I tried to give - because analysts like to have models - I've tried to give them a number that they could plug-in. I didn't rely upon any one thing or another. What I said is if you put in \$25 million a quarter or \$100 million for the year, that would be sort of a reasonable number to assume and while both our lawyers and accountants weren't happy, we'd be giving a number, I felt, to give some idea about it.

So it isn't based on health equity, it isn't based on selling a building or whatever, it's based on in the ordinary course that's what I think will happen. It could easily be significantly more. Obviously, and in some event it might not happen as we expect, although for a while we've been able to do that.

Michael Nannizzi - *Goldman Sachs - Analyst*

Okay great, thank you so much.

Operator

Kai Pan, Morgan Stanley.

Kai Pan - *Morgan Stanley - Analyst*

Thank you, and good afternoon. Just to follow on Mike's question on the \$100 million year about the realized gains, I just wonder how much is that your current value, market value versus [secure] value? I just wonder how long could that \$100 million a year last?

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

A long time.

Kai Pan - *Morgan Stanley - Analyst*

Okay. All right. That's good. And then on the hiring, of the new team, I just wonder what do you see -- do you see more opportunity in that front, basically hiring more team?

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

Which new team? We did six last year and we've done one this year so which one were you referring to and --

Kai Pan - *Morgan Stanley - Analyst*

Not specific, I just wonder are there more other opportunities out there I just wonder --

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

I think the answer is in some ways the period that we are going through now, is somewhat reminiscent of 2008, 2009, 2010 for different reasons. And that is there is a lot of dislocation in the market, there are a lot of people -- large organizations that for one reason or another are very inwardly



focused. And that creates opportunity for organizations like ours to try and continue to find opportunities and to build and enhance the value of our franchise for our shareholders, both organically through expanding our existing businesses as well as starting new operations.

I think ultimately we are optimistic that we will be able to find other opportunities, but I think you'll probably hear about them, if and when we find them and start them when we do press releases about them.

Kai Pan - *Morgan Stanley - Analyst*

Okay thanks. So would that have sort of any near-term impact, meaningful impact, on your expense ratio?

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

I think that certainly it will have some impact, but do I think it's going to be Earth shattering? No, I don't. As Gene suggested earlier, at this stage, the expense ratio that we reported in the quarter was impacted to the tune of 20 basis points I think it was in the quarter.

So some of the things that we are looking at, some of the things we've announced, you can get up and running very quickly and the earned premium will start showing up relatively quickly. There are other things that it takes time to build and it takes time for the earned premium to show up. So will there be an impact? Yes.

Will it be overwhelming, no, I think we're quite confident that it's manageable.

Kai Pan - *Morgan Stanley - Analyst*

So the expense ratio will stay or going down from the second half 2015 levels or probably stay to the same in near future?

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

I think since we don't know for sure what the opportunities will be tomorrow, or what the opportunities are that, quite frankly, or even some of the things that we're working on that we can't talk about, it would be wrong for us to try and nail things down to basis points for you. Obviously we are conscious of our expense ratio.

We are conscious of being efficient, at the same time our goal is to create long-term value for our shareholders and if there's an opportunity for us to invest in short-term, we take a step back with expense ratio but we think we will deliver long-term value for the shareholders. We are prepared to do that in a controlled way.

Kai Pan - *Morgan Stanley - Analyst*

Okay. In terms of lines where you see big growth, say Workers' Compensation more than 20% year-over-year, and on the other lines like commercial art or where people have seen some price increase probably not still -- do you find these probably too unattractive? The contractor business.

Could you talk about these two lines? In particular why you see opportunity in one versus the other?

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

I think it's very important that one not paint with two broad of a brush. So let's use Workers' Compensation as an example. It varies very much by account size, and it varies very much by region.



So there are parts of the Workers' Compensation space that we find exceptionally attractive and we would like to take full advantage of those opportunities as long as they present themselves. There are parts of the auto space that have gotten meaningful rate increase and in spite of that, we do not think the rates are adequate. From our perspective, the marketplace overall, as far as commercial auto, offers niche opportunities where you can make a reasonable return and that is what we are focusing on.

So the fact of the matter is, when Gene talked about how that book has shrunk for us overall, and he talked a little bit. If you look at the meaningful rate we were getting there any put those two things together, from an exposure perspective, we are shrinking even more than it looks like because of the rate increases that we are getting. So that's sort of how we see it.

As far as getting more granular with you, as to specifically where we see the micro niche opportunities and where we are trying to grow, I think that something that we'll probably stop short of, as far as getting into that level of detail. Because we are not looking to increase the crowd around the watering hole any quicker than will happen naturally.

Kai Pan - *Morgan Stanley - Analyst*

Okay that's fair. Last question - big picture, Rob, you alluded to as growing tension between distribution and carrier? Could you expand on that? Thank you so much.

Gene Ballard - *W. R. Berkley Corporation - EVP & CFO*

Yes, I'll make a couple of comments and then I'm going to yield to my boss here who always is - well he's a little less filtered than me, so it seems to have an entertaining component to it. But our general observation is this -- that the companies are trying to maintain, or perhaps grow their margins, the distribution is trying to do the same thing. At the same time, if you look at the insurance marketplace, rates are plateaued, and in all likelihood are gradually going to decrease, and that creates tension and pressure.

And ultimately, it would seem as though everyone is so focused on how they maintain their margins and how they keep the world happy every 90 days, that is getting in the way of distribution and carriers finding ways to work together to bring more value to the customer. Because ultimately, as technology evolves and customer behavior evolves over time, the master that we both have to please, whose needs we both need to address, is ultimately the insured. So that was the censored version and now you're going to get the uncensored version.

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

So. He told me he was going to do that, I didn't think he really would. The long and the short of the situation is - the big picture is technology is moving to dis-intermediate the current distribution system to some extent. The fact is that that's a long-term problem, and at the same time as we're moving in that direction, the existing distribution system, instead of working with companies to try and find ways to deliver value to the customer, is more focused on how to improve their margins.

And at the same time, insurance companies are faced with the need for more underwriting margin because their investment margins are declining. So you have a natural crisis. Everyone wants a bigger piece of a shrinking pie.

And it's unfortunate that much of the distribution of, at least the very largest agencies, have decided to not just make a continuing non-reduction in their commission rates, but have tried to find ways to generate additional marginal commissions. Which come, frankly, directly at the expense of the final customers. They make it as though it seems to be an additional amount paid by the insurer.

But if the insurer can afford to pay that additional amount, the amount really should go to the benefit of reduced cost to the insured. Somehow that seems to have escaped those large brokers. So ultimately, we failed to serve the customer in an open and transparent way, this intermediation accelerates.

Kai Pan - Morgan Stanley - Analyst

Where you find a way -- I've just fallen back to where you find alternative distribution yourself?

Robert Berkley - W. R. Berkley Corporation - President & CEO

I don't think that's what we're suggesting. We are just suggesting in the big picture, there's a challenge going forward and we all have to get on the same team to deliver value to the customer now. We're not -- we believe in the human participation and distribution to the customer. We continue to do that and we don't see any change in that method, obviously just as in automobile insurance, there are various methods for getting direct and I'm sure for some small policies, that will evolve but we're not rushing in that direction. We think everyone will ultimately be sensible and know we have to serve the best interest of the customer.

Kai Pan - Morgan Stanley - Analyst

Thank you so much for all the answers.

Operator

Vinay Misquith, Sterne Agee.

Vinay Misquith - Sterne, Agee & Leach - Analyst

Hi, good evening. The first question is on growth, and you seem to be pretty excited about the opportunities you have. And then I look at the numbers ended up about 4% in the primary insurance operations, most of the growth is coming from workers' comp, could you help me understand -- are you pulling back on some lines and that's what's so negatively impacting the overall growth of the Company?

Robert Berkley - W. R. Berkley Corporation - President & CEO

Look, there are parts of the business that are growing, as I suggested earlier, and there are parts of the business that are shrinking. I think as we've shared with you in the past, and others, we are in business to make money -- not necessarily just to issue insurance policies for the sake of an issuing insurance policies. We are in the market every day trying to provide product and provide continuity to the marketplace in our offering.

Having said that, ultimately if there are parts of the market that move away from our pricing then we are prepared to shrink. So yes, the answer is there are parts of our business that are shrinking right now - auto would be an example of that - again, that's just the reality of operating in a cyclical business when you're focused on profitability and return.

Vinay Misquith - Sterne, Agee & Leach - Analyst

Sure, fair enough. Then on the expense side, this quarter underwriting expenses were about \$505 million in total for the Company. Is that the run rate we should be looking at for the future? Or do you think that's going to creep up if you make some new hires.

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

I think that the expense ratio where it sits in the low 30s is not a bad expectation for people to have going forward. I don't think it would make sense for me to try and nail it down to the last dollar. Certainly we see, we saw meaningful opportunity to expand our business last year with the six new operations that we referenced.

It takes time for those businesses to get up and running and it even takes a little bit longer for that earned premium to show up and for them to get to scale. That's why Gene made the comment about the impact on the expense ratio for businesses that are two years old or less. Again, in addition to that, we expected a meaningful investment that we will be making in the high net worth personal line space that does require infrastructure, it does require investment and we think that is a worthwhile investment for the shareholders that will yield meaningful returns over time.

As far as other investment opportunities that will present themselves or that we are currently examining, it's hard to know for sure how that will play out but we think it is likely that it will be additional opportunities for us to expand our franchise and develop more value for shareholders. So do I think the expense ratio, long story short, can pick up between now and the end of the year? Yes, I think it's possible it will, as we're investing in new opportunities.

And ultimately, if we weren't pursuing some of these new opportunities, I think that we would be doing the shareholders at a disservice in the long run.

Vinay Misquith - *Sterne, Agee & Leach - Analyst*

Okay that's helpful. In the last point was on the realized gains, so it seems that you got about \$25 million pretax of realized gains, is that correct? And then was it offset in part by some OTTI? So here's about the source of the \$25 million of gains, and also the \$18 million of OTTI?

Gene Ballard - *W. R. Berkley Corporation - EVP & CFO*

So the gains were primarily in the fixed income arena.

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

Non domestic fixed-income.

Gene Ballard - *W. R. Berkley Corporation - EVP & CFO*

That's right.

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

OTTI was a common stock that had been underwater for more than a year and we market down. Those are the rules.

Vinay Misquith - *Sterne, Agee & Leach - Analyst*

Sure, thank you.

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

One of the problems with OTTI is, you get to mark them down but not mark them up. So if they're down for 12 months, you mark them down. When they go up the next day, doesn't matter.

Vinay Misquith - *Sterne, Agee & Leach - Analyst*

So for the \$25 million of realized gains, that's from the sale of fixed income securities, right? That wasn't part --

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

It's really more complicated than that. But it's not -- selling a core part of our portfolio. It is not selling a core part of our portfolio.

Vinay Misquith - *Sterne, Agee & Leach - Analyst*

So its not part of the \$100 million that you said before? Okay.

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

No, no.

Vinay Misquith - *Sterne, Agee & Leach - Analyst*

Okay thank you

Operator

Jay Cohen, Banc of America Merrill Lynch.

Jay Cohen - *BofA Merrill Lynch - Analyst*

Hey there, just one follow-up from an earlier question first. On the issue of the tension between carriers and intermediaries - their view is, while they are searching for higher revenue, and higher-margin, they would suggest that they are providing value as services for those revenue. I suspect you wouldn't fully agree with that but I wouldn't mind your comment on it?

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

I don't think we're necessarily commenting on the value that they bring. Were not questioning the value that they bring to their clients. We're merely suggesting that ultimately, when the day's all done, there is a bit of tension there.

And in what seems to be looking like a softening insurance market, it is likely that tension may increase over time. And as my father reminds me, and reminds others, that ultimately it's a partnership. There are moments in time when the carriers are the senior partner and there are moments in time when the distribution is the senior partner, but ultimately in the long run for us all to survive one needs to be conscious of the obligation to their partnership and their need to survive as well.

Jay Cohen - BofA Merrill Lynch - Analyst

Got it. Second question, on the personal lines business, and I was certainly one of the people that took note of that investment - it sounds like you got the person to run that business. And clearly, it's a good business to be in, as proven by legacy [chub] over many years, but it's also kind of sticky.

And I would suspect this is going to take really quite a while for you to get enough scale for this to meaningfully impact your earnings? Or even positively impact your earnings? Can we get a sense of the time, Rob, that you're thinking about with this venture?

Robert Berkley - W. R. Berkley Corporation - President & CEO

Well, at this stage Jay, we expect that the business will be operational sometime next year. Again back to the point earlier, it does require time to set up the infrastructure, amid a product that takes time as well to get the filings, etc. And what is it -- when is it that we will get to breakeven and to profitability?

Clearly our expectation that it will be measured in years but we think that it is a manageable period of time, and again we believe deeply in the opportunity, we believe deeply in the people's ability to create the opportunity and to a reality accrued value for the shareholders. So my sense is that I'm not answering your question with the precision that you'd like, and quite frankly, that's by design.

Jay Cohen - BofA Merrill Lynch - Analyst

I get it, all right, thank you for that. I appreciate the comments anyway.

Operator

(Operator Instructions)

Ian Gutterman, Balyasny

Ian Gutterman - Balyasny Asset Management - Analyst

Actually I had a follow-up as well on the high net worth, Rob. To me I think the challenge of that business is being able to compete on the cost side. Meaning, to be able to build up a sufficient claims operation and distribution for structure and especially given the high demands of a lot of those clients -- could you just talk about how - without being [a vouch], you have the same scale of some the bigger players?

You think you could be competitive on a cost side of that?

Robert Berkley - W. R. Berkley Corporation - President & CEO

I think it's going to take some time for us to get the critical mass where we are able to be as efficient as some others. Having said that, we think over a reasonable period of time we will be able to get enough scale that we are able to make a reasonable return. Again that will take some time.

As far as the details and the minutia of how we will be structured and how we will try and be efficient yet strike the balance between that and also provide the customer service. I think you're asking me to go a little bit deeper into the strategy of the business plan and I think wouldn't really make sense for us to do on this call.

Ian Gutterman - *Balyasny Asset Management - Analyst*

That's fair. If I could maybe try one other the way of asking this a little bit broader. Is there some kind of technology play that you think you have? By being new, that you don't have a lot of legacy costs that other people would have?

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

I think, clearly, any time someone is starting a new business, in a mature space, and will be competing primarily against mature players that have a legacy, there are pluses and minuses. The fact of the matter is, we are in the process of putting together a team of people that are very knowledgeable about the subject matter, but are very bright and open-minded as to - is there a better way to do what has been done in the past?

So we are confident, again, that this will prove to be a very worthwhile venture for the shareholders. We think the team of people that will be managing the capital on behalf of the shareholders in this space are very seasoned and thoughtful, and we are thoroughly convinced that this is a great opportunity for value to be created for the shareholders and increasing the franchise.

Gene Ballard - *W. R. Berkley Corporation - EVP & CFO*

In our history we've started 45 Companies. 44 of them are still running, and are either profitable or right on the edge of profitability. We have had a pretty good record of being able to assess what it takes to do this.

And the person whose led most of that is Rob, and I can assure you that he's not the only one who's confident. So is everybody else who's been involved.

Ian Gutterman - *Balyasny Asset Management - Analyst*

Sounds very promising, actually. I was hoping to learn more. The other I wanted to ask about was - I think in the last year or two, you've grown your Florida homeowners' reinsurance a good amount? Is your cat exposure in your reinsurance book?

Gene Ballard - *W. R. Berkley Corporation - EVP & CFO*

Hold on one second, with that. We need a little bit of a distinction there. First of all, yes we have grown our Florida homeowners book, and this is through our reinsurance.

Having said that, there are meaningful event taps and significant exclusions, as far as coverage when it comes to natural catastrophes. So I think that while there is a modest amount of cat exposure that comes with it, I would encourage you to think of that less as a cat play. It shows up in the Yellow Books and in other filings where it could be misinterpreted, so hopefully we been able to rectify the understanding.

Ian Gutterman - *Balyasny Asset Management - Analyst*

No that's great. What I was going to ask is something a little bit in between, which is I believe a lot of his quota share. Which also limits some of the exposure but I was wondering, as Florida seems there's an issue has come about the last year or so, this assignment of benefits that causing trouble for a lot of the primaries?

I was wondering if that's something that you would have some risk for as a quota share to them? Not as big as a cat obviously, but is that something you're concerned about?



Gene Ballard - *W. R. Berkley Corporation - EVP & CFO*

Certainly not something we're particularly preoccupied with.

Ian Gutterman - *Balyasny Asset Management - Analyst*

Okay, great and --

Gene Ballard - *W. R. Berkley Corporation - EVP & CFO*

We are familiar with the situation, but we don't think it's an overwhelming concern for us, hence our willingness to continue.

Ian Gutterman - *Balyasny Asset Management - Analyst*

Just one numbers question for Gene - do you have the pay-loss ratio?

Gene Ballard - *W. R. Berkley Corporation - EVP & CFO*

Yes, I do. Just a second. 52% compared to 51% a year ago - very favorable.

Ian Gutterman - *Balyasny Asset Management - Analyst*

Got it, great, thank you.

Operator

I'm not showing any further questions at this time. I'll now turn the call back over to Mr. Berkley for closing remarks.

Robert Berkley - *W. R. Berkley Corporation - President & CEO*

Okay, thank you, Bridget, and thank you all for calling and joining us for the discussion today. From our perspective as I've referenced earlier, this is a bit of a unique moment for our organization, and perhaps others, to take advantage of some of the dislocation that I think we're all acutely aware of that exists in the marketplace today. It's somewhat of a unique moment in some ways for different reasons.

We've gotten to this place where there's massive dislocation, not dissimilar to 2008, 2009 and we have been able to take advantage of that. In addition to that, I think our approach to risk-adjusted return and how we think about volatility and getting paid appropriately in part was demonstrated in our cat results in the quarter, and hopefully that does not go unnoticed.

So as we look out for the balance of 2016, while perhaps there are parts of the market that are challenging, and more challenging today than they were yesterday, we still see meaningful opportunity to grow our business in a sensible way and continue to enhance value for shareholders. So again, thank you very much for tuning in and we will talk to you in 90 days. Bye.

Operator

Ladies and gentlemen, this does conclude the program and you may all disconnect. Everyone have a great day.



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