S&P Global
Market Intelligence

Everest Re Group, Ltd. NYSE:RE

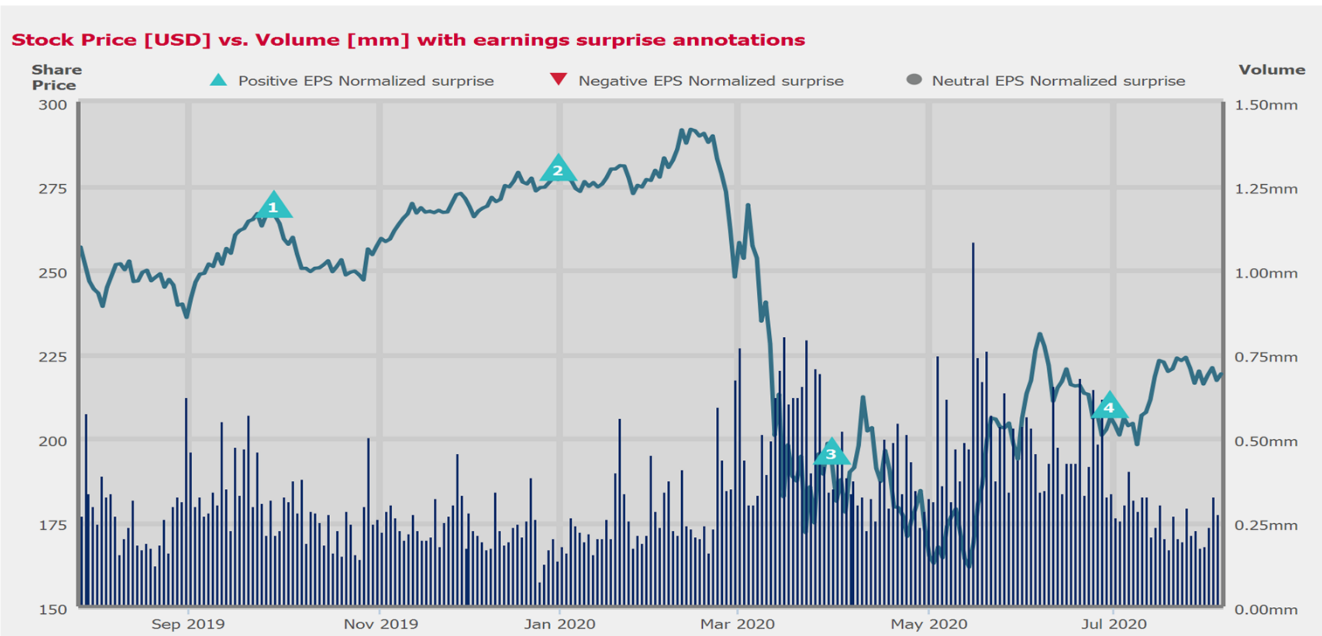
FQ2 2020 Earnings Call Transcripts

Thursday, August 06, 2020 2:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ2 2020-			-FQ3 2020-	-FY 2020-	-FY 2021-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.65	2.07	▲25.45	2.34	13.39	23.70
Revenue (mm)	1968.67	2017.48	▲2.48	2197.49	8620.24	9226.74

Currency: USD
Consensus as of Aug-06-2020 11:01 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ3 2019	2.22	3.39	▲1 52.70 %
FQ4 2019	2.58	3.20	▲2 24.03 %
FQ1 2020	3.63	4.03	▲3 11.02 %
FQ2 2020	1.65	2.07	▲4 25.45 %

Table of Contents

Call Participants 3
Presentation 4
Question and Answer 10

Call Participants

EXECUTIVES

Craig William Howie
Executive VP, CFO & Treasurer

John Paul Doucette
Executive VP, President & CEO of the Reinsurance Division

Jon Levenson
Head of Investor Relations

Juan Carlos Andrade
President, CEO & Director

Michael Karmilowicz
President & CEO of the Everest Insurance® Division

ANALYSTS

Brian Robert Meredith
UBS Investment Bank, Research Division

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Joshua David Shanker
BofA Merrill Lynch, Research Division

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

Michael David Zaremski
Crédit Suisse AG, Research Division

Philip Michael Stefano
Deutsche Bank AG, Research Division

Ryan James Tunis
Autonomous Research LLP

Yaron Joseph Kinar
Goldman Sachs Group, Inc., Research Division

Presentation

Operator

Good day, and welcome to the Everest Re Group Second Quarter 2020 Earnings Conference Call. Today's conference is being recorded.

And now at this time, I'd like to turn the conference over to Mr. Jon Levenson. Please go ahead, sir.

Jon Levenson
Head of Investor Relations

Thank you, Cody, and welcome to the Everest Re Group Limited 2020 Second Quarter Earnings Conference Call. The Everest executives leading today's call are Juan Andrade, President and Chief Executive Officer; Craig Howie, EVP and Chief Financial Officer; John Doucette, EVP and President and CEO of the Reinsurance Division. We're also joined by other members of the Everest management team.

Before we begin, I will preface the comments on today's call by noting that Everest SEC filings include extensive disclosures with respect to forward-looking statements. Management comments regarding estimates, projections and similar are subject to the risks, uncertainties and assumptions as noted in these filings. Management may also refer to certain non-GAAP financial measures. These items are reconciled in our earnings release and financial supplements.

With that, I turn the call over to Juan Andrade.

Juan Carlos Andrade
President, CEO & Director

Thank you, Jon. Good morning, everyone, and thank you for joining the call. The world is struggling with the greatest public health threat in the last century, which has resulted in economic and great personal suffering. At the same time, individuals are rightly calling for positive social change and seeking an end to racism and inequality. At Everest, we stand together with our colleagues around the world against racism and discrimination. We have an unwavering commitment to supporting diversity, equity and inclusion in our workplace.

In the context of this public health, economic and social environment, Everest is serving our customers and providing the strength and stability that they have come to rely on for almost 5 decades. Our business is running smoothly. We are performing well, and our people continue to demonstrate the passion and resilience that differentiates Everest. The health and safety of our employees and our customers are paramount.

I am very proud of our team and very thankful for their hard work and perseverance in delivering the solid results we're reporting today for the second quarter and for the first half of 2020. Our ability to leverage our capital position, our global platform and our success in executing against our objectives, even under adverse conditions, positions us very well for continued profitable growth. We have strong and broad-based forward momentum across both our Reinsurance and Insurance divisions.

Our growth stems from a combination of new business opportunities, resulting from our strong financial ratings, deep distribution and diverse portfolio as well as increased rate levels and high retention rates. We sequentially improved our underwriting profitability in the second quarter, and we continue to demonstrate strong structural expense management discipline. Our industry-leading expense ratio continues to give us operating flexibility. We also reported significantly improved net income compared to the first quarter as we benefited from the upswing in the capital markets during the second quarter. And our shareholders' equity grew to a record $9.3 billion as of June 30.

Our book value per share was $232.32, up 8% from the first quarter of 2020 and up 4% compared to year-end 2019. Our excess capital position remains a source of strength, as evidenced by A+ financial strength ratings recently affirmed with stable outlooks. Everest has the capital to play offense in this market. If we were to identify a need for additional capital, our low debt ratio gives us high degree of flexibility. Our capital position, our focus on execution, our people and our emphasis on solving problems for our customers keep us well positioned to pursue all business opportunities that meet our underwriting appetite.

Before I specifically address our second quarter results, let me share how we're driving the company forward. Our focus is on sustainably growing a balanced and diversified insurance and reinsurance portfolio by line of business and geography through the relentless execution of our strategies to deliver consistent underwriting profitability. We are nimble. We are opportunistic. We are capturing current market conditions that meet our return requirements.

On the revenue side, this is about creating greater optionality and diversification across our entire business. With a broad mix of products, customer segments, distribution and selective local presence, we're capitalizing on growth opportunities around the world and balancing the highs and lows of our industry and economic cycles. This is why having vibrant reinsurance and insurance businesses is a key element of our strategy. The growth of the Insurance division, with gross written premiums now exceeding $3 billion on a trailing 12-month basis with sustained attritional profitability, is vital to greater balance in the organization. But this growth is not at the expense of our Reinsurance division.

Today, we are a top 10 global reinsurer, a growing specialty insurer, and we are building on these positions in this market. As a group, we are playing offense to improve and further solidify our position with the best mix of talent, product and services. We are enhancing and sharpening the strategy and tightening the execution and operating rhythms. We are deploying our sizable balance sheet and diverse capital base to expand our relevance in our chosen markets. On the margin side, the focus is on underwriting profit. We are maintaining and enhancing our underwriting results with active portfolio management, strong risk governance and excellent analytics.

We are reducing exposure in areas not meeting the right risk-return profile, and we're dynamically deploying that capital to areas that do. Our strategic utilization of alternative capital will enable us to further diversify the portfolio. We are focused on claims management to deliver consistently accurate outcomes with superior service. We are maintaining our expense leadership through more efficient and scalable operating models enabled by the latest technology, including artificial intelligence and natural language processing tools. On investments, we continue to generate strong cash flows that are invested in conservative, high credit quality portfolios. We remain well diversified. All of this will deliver growth in earnings over time, resulting in book value per share growth.

Turning to the second quarter of 2020. We demonstrated continued momentum across the group with 11% growth in gross written premiums, excluding the impact of foreign exchange. The growth was broad-based across both our reinsurance and insurance businesses with gross written premium growth of 11% and 10%, respectively, also excluding the impact of foreign exchange. We continue to benefit from improved insurance and reinsurance market conditions during the quarter, which I will discuss in a moment.

Excluding catastrophes and the pandemic impacts, our IBNR loss provision and a small amount of associated credit impacts, our attritional combined ratios for the group at 88.5% and each of our segments, Reinsurance at 86.7% and Insurance at 93.7%, are reflective of the strong underwriting performance across the group and the earnings generating power of this franchise. Underwriting profitability remains at the core of everything we do. On a 6-month year-to-date basis, Everest has grown 15% and delivered an 89.1% attritional combined ratio, excluding pandemic impacts.

Our Reinsurance segment had strong growth for the quarter. We continued to successfully execute our strategies to underwrite a high-performing book of business with higher economic returns at the important April 1, June 1 and July 1 renewals. We continue to see excellent reinsurance opportunities in several areas such as facultative risk, property and in certain territories including the U.S., Canada, Latin America and Asia.

This environment gives us the opportunity to better shape our book toward deals with better terms and pricing and walk away from others that do not meet our pricing hurdles. Traditional capital from highly rated carriers like Everest has become more relevant, and supply is tight, particularly given the more limited availability of alternative capital. We see this favorable pricing environment continuing for the foreseeable future, even with pandemic-related economic headwinds.

Reinsurance profitability was also strong for the division, with a 95.3% combined ratio, including COVID impacts, and an 86.7% excluding the COVID impact. John Doucette will provide additional details on market conditions. Our Insurance segment's growth remained strong for the quarter at 10% and with improvement in underlying performance. The attritional combined ratio, excluding the pandemic impacts, improved to 93.7% for the quarter compared to a 96% in the second quarter of 2019.

We are strategically managing the insurance portfolio to build a more diversified business and steer our mix towards product lines that we expect to earn higher margins long term. The maturation of several new product lines launched over the last several years as well as our wide market footprint give us access to significant opportunities. For the quarter, the main insurance growth drivers were: strong and widespread rate momentum excluding workers' comp of plus 18%, and including workers' compensation of over plus 12%. This is the highest overall rate change we have seen in a long time.

Insurance written rate also continues to exceed loss trend across our core P&C lines of business. We also saw continued strength in the excess and surplus line space. We had strong renewal retention in both our retail and E&S businesses. But this growth is offset by pandemic-related headwinds and lines heavily impacted by lower payrolls and lower business activity.

Turning to investments. Net investment income decreased to $38 million for the second quarter. The drop was attributable to negative returns from our limited partnerships, which, as we mentioned in our first quarter call, report on a 1 quarter lag. Given the lag, this drop reflects the market turmoil, which occurred in March. The second quarter recovery in the public markets provides a basis for expecting an improvement in limited partnerships, which will be reported in the third quarter. The amount of the recovery is difficult to predict given the ongoing uncertainty caused by the pandemic.

Regarding COVID-19 impacts, as per our July 23 announcement, we have taken $160 million loss provision in the second quarter made up substantially of IBNR. The majority of this loss provision, $130 million, was for the reinsurance business. These losses relate to event cancellation or postponement, business interruption and workers' compensation. We have also increased our IBNR for allocated loss adjustment expenses based on anticipated cost to investigate and defend some portion of claims. We are taking a measured approach to our loss estimation process that is based on credible and supportable information. This is an ongoing event and very different than a natural catastrophe.

We're continuously monitoring this evolving situation and recognizing potential exposure based on the most up-to-date information available. Our second quarter estimate was based on a refreshed analysis updated with the latest information from our clients. While our analysis continues to include all aspects of our global portfolio, our estimate does not take into account legal, regulatory or legislative intervention that could retroactively mandate or expand coverage provisions.

Of the $30 million loss provision for the second quarter in our specialty insurance business, the majority was from event cancellation and postponement policies as the nature and duration of the pandemic has increased the likelihood of cancellations into early 2021. A smaller portion of the insurance loss provision was predominantly loss adjustment expenses for business interruption policies. As stated last quarter, our property policies have unambiguous policy language that requires direct physical loss for business interruption coverage to be triggered.

Additionally, the majority of the property policies in force contain a virus exclusion. Only a very small number of policies have endorsed sublimits that would offer BI coverage for a notifiable human disease. These exposures have already been recognized as part of the overall IBNR estimate. Workers' compensation represents the smallest portion of the insurance provision in the quarter. We have refreshed our analysis based on the industry profile for businesses which have now been deemed essential by many states. However, this is not a significant amount. Our portfolio has no known exposure to first responders and very minimal exposure to frontline health care workers.

With regard to the reinsurance loss provision, we have updated our analysis based on information from cedents and brokers. It is important to reiterate that as a reinsurer, our analysis will be very fact specific to each situation and each contract. We have also updated our review of our mortgage reinsurance contracts. Based on our current view of the macroeconomic situation, updated client information and our internal modeling, we remain comfortable with our exposure and with our loss reserves. We will continue evaluating this business as the economic situation unfolds.

In summary, Everest continues to gain traction and forward momentum despite the macroeconomic uncertainty and the rapidly changing external environment. We're operating smoothly with the health and safety of our employees and their families top of mind. I am optimistic about our future. We have a talented team, a global platform and a strong capital position, which allows us to capture the improving opportunities in front of us.

Lastly, I want to welcome Mike Karmilowicz to the call today. As you saw in our recent announcement, I am pleased to introduce Mike as the new CEO of our Insurance division. Mike's promotion is an acknowledgment of the key role he played in the growth of the insurance business over the past several years and provides continuity so Everest can execute on our winning strategy. He will be available to answer your questions today.

Now let me turn it over to Craig to provide additional details on the financials.

Craig William Howie
Executive VP, CFO & Treasurer

Thank you, Juan, and good morning, everyone. Everest delivered another solid quarter of financial results. For the second quarter of 2020, Everest reported net income of $191 million. This compares to net income of $17 million in the first quarter of 2020 and $333 million for the second quarter of 2019.

On a year-to-date basis, net income was $207 million compared to $687 million for the first half of 2019. Net income included $22 million of net after-tax realized capital losses compared to $100 million of capital gains in the first half of 2019. These results were driven by a strong underwriting performance across the group, stable investment income from fixed maturities and low catastrophe losses, partially offset by a COVID-19 pandemic loss estimate of $310 million and negative limited partnership investment returns.

The overall underwriting gain for the group was $51 million for the second quarter and $80 million for the first half compared to an underwriting gain of $393 million in the first half of last year. The company continues to grow premium in 2020. Year-to-date gross written premium was $4.9 billion, up $646 million or 15% compared to the first 6 months of 2019. This reflects growth in both segments, with Insurance up 20% and Reinsurance up 13% compared to last year.

In the second quarter of 2020, the company reported $15 million of catastrophe losses related to the civil unrest in the U.S. Although there were a number of loss events in the quarter, notably U.S. storm events, none of these events breached our $10 million catastrophe threshold, and as such, are included in our attritional loss estimates. On a year-to-date basis, the results reflected catastrophe losses of $45 million compared to $55 million during the first half of 2019.

The group combined ratio was 98.1% through the first 6 months compared to 95.5% for the full year of 2019. Excluding the catastrophe losses and the impact from the COVID-19 pandemic, the comparable combined ratios were 89.1% through the first 6 months of 2020 and 88.4% for the full year of 2019, mostly attributable to business mix changes that impact the attritional loss ratio. Excluding the pandemic loss estimate, the group attritional loss ratio was 16.7%, up from 16.2% for the full year 2019, primarily due to the continued change in reinsurance business mix.

For the Reinsurance segment, the attritional loss ratio, excluding the pandemic loss estimate, was 59.0%, up from 58.2% for the full year 2019. This increase was related to the continued shift toward more pro rata business, which requires a higher loss pick, but allows us to benefit directly from the firming primary market. Pro rata premium is less volatile than excess premium, and we will see the benefit earn into our results as we let the loss pick season over time.

For the Insurance segment, the attritional loss ratio, excluding the impacts from the pandemic, was 65.4%, down compared to 66.0% for the full year 2019. Our U.S. franchise, which makes up the majority of our global insurance business, continues to run an attritional combined ratio in the low 90s, excluding the pandemic loss estimate. The group commission ratio of 22.4% was down compared to the prior year due to the business mix and more ceding commission received in the Insurance segment.

Group expense ratio remains low at 5.8% in the second quarter and 6.1% for the first half of 2020, in line with our expectations. During the second quarter, we saw reduced expenses for new hires, travel, entertainment and conferences. On loss reserves, we completed several reserve studies during the quarter related to some smaller classes of business. The overall indications were not material enough to warrant any action on these studies during the second quarter.

For investments, pretax investment income was $186 million year-to-date on our $21.6 billion investment portfolio. As Juan mentioned in his remarks, investment income in the second quarter was impacted by $88 million of limited partnership losses. The fixed income portfolio remained stable and produced $272 million of investment income year-to-date compared to $253 million for the same period last year. The pretax yield to maturity on the investment portfolio was 3.4%, stable compared to 3.4% one year ago. We've been able to maintain a consistent yield to maturity without a dramatic shift in the overall investment portfolio.

We expect to maintain our asset allocation and a conservative, well diversified, high credit quality bond portfolio with conservative duration. For our investment-grade portfolio, the new money rate was 2.7% for the quarter. Other income and expense included $24 million of foreign exchange losses during the first 6 months of 2020. On income taxes, the year-to-date tax benefit of $14 million included a $31 million tax benefit related to the CARES Act that we reported in the first quarter. Excluding this benefit, the effective tax rate on operating income was 11%, in line with our expected tax rate for the full year.

Positive cash flow continues with record operating cash flow of $1.1 billion for the first half of 2020 compared to $854 million in 2019. This increase reflects our growth in premiums and a lower level of catastrophe losses in 2020 compared to 2019. Shareholders' equity for the group was $9.3 billion at the end of the second quarter, a new record for Everest, up from $9.1 billion at year-end 2019. The increase in shareholders' equity in the first half of 2020 is primarily attributable to the $207 million of net income and a significant recovery in the fair value of the investment portfolio.

A mark-to-market impact on the fixed income assets improved from an unrealized loss of $248 million in the first quarter to an unrealized gain of $545 million in the second quarter of 2020. Everest continues to maintain a very strong capital position, with industry low debt leverage and high liquidity in our investment portfolio.

Thank you. And now John Doucette will provide a review of the Reinsurance operations.

John Paul Doucette
Executive VP, President & CEO of the Reinsurance Division

Thank you, Craig. Good morning. Having now finished our June and July renewals, we are increasingly optimistic about the reinsurance market and our position as a global provider of reinsurance solutions. The flight to quality by reinsurance buyers continues. And highly rated reinsurers like Everest, with solid financial strength and global underwriting capabilities, will do well in this market.

The expanded opportunity set allowed us to improve our portfolio across virtually all geographies and classes of business. As Juan stated earlier, Everest's market positioning, combined with healthier market conditions, led to strong growth in gross written premiums for this quarter and for the first half of this year. For net written premium, the growth was even higher at 15% for the second quarter as we retain more business given our capital strength, the improved underwriting environment and the shifting economics of retrocession purchases.

Overall, we have a larger and more profitable portfolio than we did last year. By many measures of risk and return, the expected performance of writings this year is improved versus the expected performance of the last underwriting year. Our portfolio's growth has been broad-based with significant contributions from our global facultative operations, which are seeing large increases in submission activity and strong pricing trends. Encouragingly, rates are increasing strongly even in markets with sufficient capacity.

In terms of property cat, market conditions overall remained strong, particularly in peak zones and recently loss-affected areas. Cat renewals in Florida and the U.S. generally experienced double-digit rate increases with higher increases on loss-affected business, leading to higher expected margins and profits. In our Florida cat book, we wrote more premium versus last year, but with less exposed limit. As a result of our underwriting execution and rate increases, our expected dollar margin for Florida is meaningfully higher.

We also refocused our capacity on fewer core clients. Regarding our global property portfolio, we executed our plan. Expected profits grew considerably as we retained more economics due to a smaller outwards retro spend. However, we maintained hedging capacity through Mt. Logan in our catastrophe bonds. Across our peak cat exposures, our net PMLs increased midyear relative to January's net PMLs, reflecting our plan to capture this market's improved profitability. The net PML increases are predominantly further in the tale of the distribution.

Competition from ILS capacity was less pronounced during the midyear renewals due to investor frustration from multiple bad industry cat loss years, adverse development and trapped capital by several ILS managers. The retro market is favorable for sellers. And as a net seller of retro, we captured strong double-digit rate increases. And demand from recurring retro buyers remains robust. We also deployed more capacity in property pro rata business with original rate improvement and tighter occurrence caps. The well-priced cat exposure of this class contributed somewhat to the increased PML.

The casualty reinsurance markets are also improving directly from increased excess rates or indirectly as original business rates benefit pro rata deals. Excess casualty rate increases generally range from single digits to well into double digits, varying by ceding and product. Casualty ceding commissions improved slightly. While the casualty market improved, we still walked away from some large renewals priced below our return requirements. Nevertheless, we have several compelling opportunities to partner with our global clients in several classes of business, either through new deals brought to the market or increased shares on improved renewals.

In Australia and Asia, market firming continued throughout the year with earlier renewal rates increasing less than later renewal rates. For these midyear renewals, more business met our return hurdles, and we wrote more premium accordingly. Our long-term relationships in Asia cultivated over the last 30-plus years allowed us to capture better opportunities and in times like these, those situations become more pronounced. Likewise, quality underwriting opportunities presented themselves in Canada as rate increases were achieved across several different lines of business in both fac and treaty. Therefore, we have been increasing our shares on several Canadian programs.

Finally, some comments on our mortgage book. We remain comfortable with our exposure, loss picks and loss reserves on our mortgage writings. The majority of our in-force mortgage business will not be impaired by the pandemic unless housing fundamentals and post-economic recovery, unemployment deteriorate significantly. This is in part because of our generally high attachment points and our conservative underwriting and pricing of mortgage. Also, unlike the primary mortgage insurers, we, as a reinsurer, can and do book significant IBNR reserves.

In summary, disruptions facing our industry and our personal lives create uncertainty around the future of many businesses and economic sectors. As a leading provider of reinsurance solutions, we maintain a strong position to absorb volatility and diversify that uncertainty for our clients with our robust balance sheet, global presence, and capital resources, while generating solid returns for our shareholders.

Thank you. And now I will turn it back over to Juan.

Juan Carlos Andrade
President, CEO & Director

Thanks, John. I feel good about the direction of the insurance and the reinsurance market, and I am pleased with our execution and our momentum. We have grown our premium by 15% in the first 6 months of 2020. Our first priority is to profitably deploy our capital for organic business growth in this hardening market environment. We continue to find ways to put our capital to work, and we see strong opportunities ahead.

Now let me turn it over to Jon Levenson to open it up for your questions.

Jon Levenson
Head of Investor Relations
Great. Thanks, Juan. Cody, I see we have a number of participants in queue. Can you please open the Q&A?

Question and Answer

Operator

[Operator Instructions] And we'll first take our question from Mike Zaremski with Crédit Suisse.

Michael David Zaremski
Crédit Suisse AG, Research Division

First question. I appreciate all the color regarding the COVID losses that were booked. Curious, we get a lot of questions from investors about how to think about the COVID impact going forward. And I know it's complex, given a lot of your losses are coming through the Reinsurance division. But in regards to your conversations with cedents, do you -- are some of them thinking that there's likely to be more losses trickling in during the back half of the year as this very complex situation is further assessed? Or some insurers, I think, mostly primary issuers are trying to say that they think they kind of have most of their loss picks on booked, unless things get materially worse regarding COVID?

Juan Carlos Andrade
President, CEO & Director

Yes, Mike, this is Juan Andrade. Look, I think we have a very solid estimate based on what we know today. We have a good process that has underlined the estimates really from the beginning of this crisis, and we certainly talked about it in the last call. All that being said, this event is still underway, right? The crisis is still ongoing. And much of this is going to be determined by the length of this crisis, as well as by any actions that are taken by governments along the way. So I think in that sense, there is some uncertainty as to where the losses, particularly on the reinsurance side, may go as cedents are still trying to grapple with their own numbers and essentially come up to a good estimate. But again, I would say, from my perspective, we do have a solid estimate based on what we know. And that certainly has been the approach and the perspective that we have taken from the very beginning. And as we have more updated information, we will be updating that as well.

Michael David Zaremski
Crédit Suisse AG, Research Division

Okay. Great. My last follow-up question is regarding your outlier low leverage level. And I think we appreciate that you guys are playing offense. Clearly, you can see it. PMLs came up a little bit, but still kind of well below historical levels. You're seeing certain participants in the industry either raise debt, equity, new startups. So has your thought process changed in terms of the opportunity cost of holding a lot of excess capital? Is it changing or is it kind of plan A is still is just let's keep kind of trying to grow the top line in excess of our ROE, less the dividend and we'll just kind of use up our excess over the coming 3, 5 years that way?

Juan Carlos Andrade
President, CEO & Director

Yes. So let me start, and then I would ask Craig Howie to jump in as well. Mike, what I would say is our capital management philosophy hasn't changed. I start out with the fact that we have more than ample capital to deal and face off with the opportunities that are in this market today. And I think you see it from our numbers, right, that we've been very forward-leaning and being able to continue to grow in this environment. We also have a very low debt leverage, right? So as I mentioned in my remarks, to the extent that we see any opportunities that are relevant for us, that are accretive for us, at that point in time, we have the flexibility to increase our capital. But as I sit here today, look, I feel very good about our capital position. We also have over $13 billion in deployable capacity, right? When you think about our policyholder surplus plus what we hold in our bonds, what we hold in Mt. Logan, et cetera, et cetera, we have plenty of capacity to work with in this market. So from that perspective, our philosophy continues to deploy capital into this market, particularly given the favorable conditions that we're seeing right now. But Craig, is there anything you would add?

Craig William Howie
Executive VP, CFO & Treasurer

Juan, I think you covered it. I do think that, just to state the obvious, that if we did want to build our balance sheet, we have sufficient low leverage and certainly one of the lowest debt leverages in the industry to be able to do so.

Michael David Zaremski
Crédit Suisse AG, Research Division

And so would you -- if you had to put more capital to work, are you leaning more towards reinsurance in the near term or primary insurance to deploy that -- the access?

Juan Carlos Andrade
President, CEO & Director

Yes. It's a great question. Fortunately, we're in a pretty good position, right, in the sense that you don't have to choose which of your children you like most. We see opportunities on both sides, right? And so I think as I articulated and John Doucette had articulated, we're seeing some really good opportunities on the facultative risk side, some very good opportunities in property as well. All of that being said, you also heard from John that we're being very disciplined. So if things do not meet our economic return criteria, we will walk away from it just like what we did at some of the recent renewals. But we see plenty of opportunity to deploy capital there. The same thing in insurance. You saw the growth rate there. We see great opportunities in property, both wholesale and retail. We see very good opportunities in excess casualty. We see very good opportunities in D&O. So right now, because of our capital base, we are looking at where we can play offense in this market and deploying our capital that way, so we can grow and essentially take advantage of the favorable conditions.

Operator

We'll now take our next question from Josh Shanker with Bank of America.

Joshua David Shanker
BofA Merrill Lynch, Research Division

So I saw you took the PMLs up, of course, and following on what Mike was saying. Is there any change in the cat load guidance? And if we think about next year, if things go the way you want them to go, where would you ideally want to be setting your PML and your cat load guidance? What is a healthy market and a healthy PML in an attractive market for cat protection?

Juan Carlos Andrade
President, CEO & Director

Yes. So Josh, this is Juan. So for this year, there is no change in our cat load from that perspective. But let me ask John Doucette to speak to the PMLs.

John Paul Doucette
Executive VP, President & CEO of the Reinsurance Division

Yes. Thanks, Juan. Thanks, Josh, for the question. So as I mentioned in the script, we have seen opportunities. And as we put in the investor presentation, the PMLs are up now, Southeast wind is 7% of equity, up from 5.7%. And really, it's going to be a function of the -- of what we see in the market. We expect -- we like Florida, but we were disciplined. We did shed some clients and nonperforming accounts that didn't meet our return thresholds. And that was true at July 1 as well, and we expect it to be true at 1/1. So we do expect to see momentum continuing into 1/1 and beyond. We think it's a great market to be a seller of retro. We are a top 2 seller of retro among rated reinsurers. And as Juan alluded to, we have the capital across the Kilimanjaro bonds, Logan and, of course, our common equity and debt -- have the capital and flexibility to write the book that we see that's in front of us and what the market gives to us. But we do expect to see robust demand in 1/1 and going forward.

Joshua David Shanker
BofA Merrill Lynch, Research Division

Okay. And then a little education in casualty pro rata risk. If I may cede and I have a pool of risk that I'm raising prices on and I think improving margins on. When I negotiate a treaty with a reinsurer to protect me from some of that business, because maybe I need balance sheet protection or let's just say balance sheet is just not big enough. I'm going to say, look, our business is going to be more profitable next year, so we're going to raise the ceding commissions on you. To what extent, I mean, is there a ceiling on how much profitability you can receive in a rising rate environment for risk if it's sort of tempered by the ceding commissions being charged for improving profitability on that same risk?

John Paul Doucette
Executive VP, President & CEO of the Reinsurance Division

Yes. That's a great question. And I think first principles. That's why we're agnostic to the form that we take in reinsurance risk, whether that's casualty, property, specialty and mortgage. We look at it across -- we look at it as to how we want to deploy capital, and that will vary by product. And likewise, our clients will look to see whether they want to do things on a proportional basis, an excess basis, excess or loss per risk basis. And that varies. Some of them will change that over time. But that's why in my statement, in my comments, I mentioned that the casualty market we're seeing improving, but we're seeing a little bit of improvement in ceding commissions given the market that we're in. But we are seeing a lot more of the benefit coming through the original, the primary rates on the insurance operation.

So -- and then also, I think it's -- we need to remember that there are a whole lot of clients out there that write their business using different capital levels. And some have capital -- a lot of capital support that, that gives them flexibility, whether they do something potentially on a pro rata basis or an excess basis. But then a lot of our clients around the world, again, they don't have a lot of capital. And so sometimes they need to de-lever their premium. And so they do need to buy proportional treaties. And that's in the U.S., that's international, that's in Lloyd's, where it will vary, again, by line of business. And that gives us the opportunity by having the ability to dynamically allocate capital by line, by territory and by product, excess loss or pro rata, it gives us the best chance to capture what we see as the opportunity in front of us profitably.

Operator

We'll take our next question from Yaron Kinar with Goldman Sachs.

Yaron Joseph Kinar
Goldman Sachs Group, Inc., Research Division

I guess first question. I do want to go back to the capital raise question. It sounds like the environment is a very constructive one, and you see it probably with legs going into '21. So does the decision to not raise capital today -- I'm just trying to understand how that fits in to this construct. Do you not see sufficient opportunities to deploy capital that you would raise? Is the market not attractive enough? I guess at what point -- what would make you want to raise capital that you're not seeing today?

Juan Carlos Andrade
President, CEO & Director

Sure, Yaron. So thank you for the question. This is Juan. Look, so number one, I would start with the fact that for us, this is a dynamic process, right? We're always sort of assessing our capital, our needs, the environment, that sort of thing. So it's not a fixed point in time. It's a very dynamic discussion that we have within the company. We find the current opportunities to be quite attractive. And hopefully, you saw that from, frankly, the bullish nature of my comments and those of John Doucette on this call. I think you see that from the growth rates and how we're managing to execute on the opportunities that we see in this market. But our position right now is, look, I mean, where we sit with the capital that we have right now, we feel that we have more than enough to be on offense in this marketplace. Unlike others who have had to raise capital for defensive purposes, we're not in that situation, right? We're actually in a good place right now. Now I did say in my remarks that this environment is very fluid. And if we identify opportunities that we see that are accretive to our bottom line, then we certainly have the flexibility to be able to do that. Again, I would have like Craig to see if he's got any additional thoughts on that.

Craig William Howie
Executive VP, CFO & Treasurer

Yes, Juan, I agree. If you're going to raise capital, it should be accretive. And certainly, timing comes into play as well. If you're raising equity capital, certainly, earlier in the year was a good time to do it instead of waiting toward election times. But we didn't need to raise equity capital. We didn't need to build scale. We already have the scale. We're not trying to fund M&A at this point in time, and we're not trying to replace retro coverage at this point in time. So certainly, as the market changes, we still have flexibility, especially with respect to our debt leverage.

Yaron Joseph Kinar
Goldman Sachs Group, Inc., Research Division

Okay. And my second question, with regards to Reinsurance COVID losses, can you maybe explain what the difference is between being fact-specific to each situation in each contract as opposed to following the fortune? Like what's the distinction that you're making?

Juan Carlos Andrade
President, CEO & Director

Yes, Yaron, happy to talk about that. Look, every contract is going to be different, right? I think unlike a natural catastrophe, there's going to be hours clauses, there's going to be bench definitions, there's going to be different attachment points, et cetera. And so that's really when we say that, that's what we mean, is that this is not a panacea, and we're going to look at each contract by its nature, by its merits, by its own facts. And then we will make claims adjudication decisions based on that.

Yaron Joseph Kinar
Goldman Sachs Group, Inc., Research Division

And that's not the same as following the fortune?

Juan Carlos Andrade
President, CEO & Director

Well, I think following the fortunes would imply that essentially, any loss that you're seeing to report as being a COVID loss would be automatically accepted. And essentially, what I'm saying -- what we're saying as a company is it's very fact specific, and that will be put against the contractual requirements and wording in each of our contracts.

Operator

We'll then move on to our next question from Elyse Greenspan with Wells Fargo.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Sorry, I also have a question to follow-up on the capital side of things. Is there a way that you can tell us like, I know you pointed to, right, that you have your own common equity, Logan as well as Kilimanjaro, that help support increased writing, cedings into what seems like a really strong market in 2021. But can you give us a sense on your current capital base, right, assuming on more increased deleverage, which sounds like you're holding off on that for the time being? How much growth could Everest absorb on its own capital base today in 2021?

Juan Carlos Andrade
President, CEO & Director

Sure. I would ask Craig Howie to answer that.

Craig William Howie
Executive VP, CFO & Treasurer

Well, Elyse, it depends on which capital measure you're looking at. And right now, we feel as though we can grow both sides of our book, both reinsurance and insurance, with the capital base that we have today. And that even goes into looking forward to 1/1 renewals on a reinsurance basis. So that's why we feel as though given the market and given where we are today, that we have enough capital to not miss out on any opportunities in the current market conditions.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Okay. That's helpful. And then my second question, on the leverage side, obviously, you guys have pointed out, you're underlevered relative to your peers. Is there a certain internal mark that you guys are viewing to go to? And then I guess, in that answer, how high would the rating agencies let you take your leverage? And can you also provide with an updated AUM for Logan? I'm not sure if you guys provided that earlier.

Juan Carlos Andrade
President, CEO & Director

Craig?

Craig William Howie
Executive VP, CFO & Treasurer

Yes. So Elyse, with respect to our leverage, certainly, from a rating agency perspective, what they're doing currently right now is allowing people to increase their current leverage. As you know, we're closer to 6%. We could have easily grow that capital to 20% leverage without any question or concern at all. Most of our peers are in the 20% and upwards of 30% range, as you well know. So from that standpoint, we have plenty of room to grow and expand that leverage. As far as the Logan AUM question, our Logan AUM was -- we were able to grow the AUM slightly this quarter, but it is down from year-end. We're at about $800 million.

Operator

We'll now take our next question from Ryan Tunis with Autonomous Research.

Ryan James Tunis
Autonomous Research LLP

So I'm actually interested in John Doucette's perspective, because I would think, look -- John, looking at Slide 15, if that slide would be driving you nuts, because you've been here -- you've been at Everest for years. And in '15, '16, '17, '18, the PML was double digits and pricing was a lot worse. And common sense says, if you want your PMLs to be better or higher when pricing is better and now they're only at 7%. So I guess the question is like, what's the lesson here? Was it too high back again? Or are you more in the camp of I'm chomping at the bit to deploy more capital at this moment because this is when you really want to be quite a bit higher in terms of PMLs?

John Paul Doucette
Executive VP, President & CEO of the Reinsurance Division

Yes. Ryan, thanks for the question. So a couple of things. So what we've been saying for a while is that we want to -- we're not just a one-trick pony within property. And if you rewind the tape, property -- our view, the property was more attractive on a relative basis than some other lines, and you talked about being more bearish on casualty than some of our competitors. So what we've seen, a couple of things. We have seen property -- improvement in property prices. We've also seen improvement in casualty. As you know, we've been growing out our mortgage book substantially. We're seeing nice increases and opportunities in specialty lines business. And so we're deploying more capacity along the way there.

And really, I think what we're trying to do is capture what we see as the opportunity in front of us. We've also talked about on prior calls kind of an elevated risk that we've seen in a social -- when you think about social inflation and things in Florida tied to like assignment of benefits and climate change and other risks that also have caused us to make sure that we're deploying what we view as the right amount of capacity fill combination. And so that elevated the return requirements that we needed to deploy increased capacity. And again, our view as to where are we head into 1/1, we expect to see a robust January 1, particularly in peak zone cat and retro. And we'll deploy capacity accordingly. So we'll do it, but we'll also be -- we'll do it based on what the market terms and conditions are, what the clients' demands are, but we'll also be looking across all lines of business and territories to really build the best book we can.

Ryan James Tunis
Autonomous Research LLP

And then just one follow-up for Juan on the insurance side. You said in the press release that pricing is exceeding loss trend. We're seeing modest improvement of the underlying combined ratio in that business. It's probably not arithmetically what you think it would be, given the level of rate we're getting. So I guess, how would you describe, I guess, the cadence and the pace of margin improvement we're seeing in insurance relative to the amount of rate.

Juan Carlos Andrade
President, CEO & Director

Thanks, Ryan. Look, what I would say is we are definitely seeing loss trend being essentially below our written price change, right? So we're seeing a lot more rate right now ahead of trend. And that's a good thing. That being said though, we are also keeping our loss picks up and conservative given the environment in all of this, right? So while you're seeing rate ahead of loss trend, and frankly, you're seeing some frequency benefit on some lines of business, at this point in time, we think it's just prudent to maintain the loss picks where they are. And so over time, you will see that margin improvement. And so that's basically how we're looking at that.

Operator

We'll move on to our next question from Meyer Shields with KBW.

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

I want to start with Juan, I guess, basic question. I know it's way too early to have an estimate for losses from the Beirut explosion. But how should we think about that impacting various insurance and reinsurance markets?

Juan Carlos Andrade
President, CEO & Director

I'm sorry, Meyer. I didn't hear the first part of your question.

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

I'm trying to get a sense in terms of directionally. When you got something like the Beirut explosion, obviously, far too early for any estimate of losses, but should we think of this as an insurance event, a reinsurance event?

Juan Carlos Andrade
President, CEO & Director

Got it. So if we're looking at Beirut specifically, I think, as you pointed out, look, it's probably too early to tell. We are a global company, and I would expect that we will have some loss out of that. I would expect the loss, if it comes, it will be more on the reinsurance side than on the primary insurance side, at least for ours.

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

Okay. That's very helpful. I'm getting a couple of questions about the modest adverse reserve development in the Insurance segment. I was hoping that either Juan or Craig could comment on that maybe.

Juan Carlos Andrade
President, CEO & Director

Yes, sure. This is Juan, Meyer. Would be happy to talk to you about that. Number one, it's very small, right? So it's less than $5 million. And it's really an increase on a specific large loss that came through in the quarter in our international insurance operations. So it's not meaningful from that perspective. And as you know, our reserving philosophy has been that we react quickly to that news. And frankly, we felt it prudent to recognize in this quarter and we recognized the development.

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

Okay. So if this was an actual loss emergence instead of this happening. Okay. And then final question, and I know quarterly numbers again bounce around a lot, but the -- within insurance, the other specialty line was down year-over-year. Is that a more economically sensitive line than some of the other specialty lines?

Juan Carlos Andrade
President, CEO & Director

Yes. And let me ask Mike Karm to jump in and give you a little bit of color on that as well. So Mike?

Michael Karmilowicz
President & CEO of the Everest Insurance® Division

Sure. Thanks for the question. That actually is definitely an economic impact. That business usually is transactional risk, which is M&A, which is obviously impacted by the COVID and the pandemic and then other lines on the credit side. So some of those actions, we actually were deliberate in actually slowing that business down, given what's going on with the pandemic and its impact to the credit markets.

Operator

We'll move on to our next question from Brian Meredith with UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

A couple here. Juan, I just want to clarify. I think you said in your response to Ryan's question that you didn't take any frequency benefit in the quarter either on comp or short-term property lines in the Insurance segment?

Juan Carlos Andrade
President, CEO & Director

Yes. So that's correct, Brian. We are not taking any frequency benefit in the quarter for any of the lines of business where we have seen lower frequency so far this year. At this point in time, we think that's premature. And the reason for that is pretty straightforward. While you do see claims counts down in some lines of business like commercial auto and workers' comp and in GL, exposures are also down, which also result in premium refunds, right? So the impact on severity is less clear yet. And so I think you really need to look at longer-term averages because some of these frequency decreases may be temporary, and we don't know what the bounce back is going to be once the economy is fully reopen.

Brian Robert Meredith
UBS Investment Bank, Research Division

Got it. That makes sense. And I guess I'll just add on to that. I'm just curious, Juan. Could you give your perspective on kind of what social inflation kind of currently looks like? And what your outlook is here as the economy reopens? And with respect to that, is there anything that you can do right now with contract awards in your insurance space to potentially mitigate COVID-19 related claims here going forward?

Juan Carlos Andrade
President, CEO & Director

Yes. No, absolutely. This is something that, frankly, we have been all over from the very beginning of this crisis. And I give a lot of credit to our corporate underwriting teams and our chief underwriting officers on that. Look, this is consistent with what I just said about frequency. I think as the economy begins to reopen again, a lot of the trend indicators that were there prior to the pandemic that frankly gave rise to some of the rate increases that we're seeing now across the board are still going to be there, right? So that hasn't gone away.

But we have taken a number of actions, whether it's been pushing rate, tightening terms and conditions, reviewing contract wordings. We've also been putting pandemic exclusions in place across the board. We've also withdrawn capacity from certain territories, certain products, certain lines of business that, frankly, we weren't comfortable with as far as the risk assessment or the coverage that was being granted. And as you just asked on the earlier question regarding other specialty and insurance, we're also remaining cautious on certain economically sensitive lines. So we've taken a pretty deep and thoughtful approach to our underwriting from the very beginning of this pandemic in order to provide protection to the book going forward.

Operator

We'll take our next question from Phil Stefano with Deutsche Bank.

Philip Michael Stefano
Deutsche Bank AG, Research Division

Yes. I was hoping you could talk about the reserving process for the COVID charges on the insurance business. And I think, Juan, you had mentioned in your opening remarks that there are some events into 2021 that are contemplated. So maybe you could just give us a flavor for kind of the time line and how you're thinking about reserving there.

Juan Carlos Andrade
President, CEO & Director

Yes, absolutely. Look, I would tell you that the estimate that we have on the insurance side is a solid estimate, as I mentioned before. Particularly for event cancellation type policies, we are looking at early 2021 at this point in time. And this goes back to one of the questions I was asked earlier about the nature of this event. And what I mentioned, which, look, this is an ongoing event, and a lot of this will depend on the length and shape of it, frankly. But on contingency, we're definitely looking at early 2021 at this point in time.

Philip Michael Stefano
Deutsche Bank AG, Research Division

And so the reason I'm asking the follow-up then leads to the reinsurance side of that. I'm getting the impression on these calls first quarter and probably even more so second quarter that auditors are having a different feel for how far they're allowing people to look in their reserving process. I guess, on the reinsurance book, when you have conversations with students, is the horizon they're allowed to contemplate in any way complicating your ability to reserve on the reinsurance side? How are those conversations going? And is the time line you're contemplating a reinsurance really different than the insurance side of your book?

Juan Carlos Andrade
President, CEO & Director

Yes. So let me give you my thoughts on that, and then I would ask John Doucette to jump in as well. So look, I think the process has been very similar from the perspective of the detailed discussions that we've been having with our cedents, we've been having with brokers trying to understand the book of business. Obviously, the difference being that in the reinsurance side, it's a much more global book. We have some very large cedents and they're still trying to grapple in some ways, as you've seen in a lot of the calls, with their own exposure. And so from that perspective, on the reinsurance side, we do get a bit of a lag as far as the information is concerned with some of this information. But I think as far as the time horizon is concerned, our conversations with the cedents have been -- they're looking at similar time frames through the end of this year, beginning of next year. But John, I don't know if you would like to add some color to that also.

John Paul Doucette
Executive VP, President & CEO of the Reinsurance Division

Yes. Thanks, Juan. And as you said, there clearly is an information lag in terms of when the reinsurers hear things, plus everybody has to go look at the contracts in terms of how -- again, going back to contract specific, fact specific, what are the retention clauses. What were the retentions? What are the hours clauses? What are other terms and conditions, exclusions that are in the contract? And I think that just takes a while to understand. And our clients -- again, it varies by territory, what the original wording is. And so there's a lot of moving parts that really result in this as well as, as we've said, this being an ongoing event, that it makes it a lot more complicated. But we feel comfortable, based on all the information we have today, with both the process that we put in place to identify as well as what we have booked, again, given the information we have today.

Juan Carlos Andrade
President, CEO & Director

Yes. And the last thing that I would add to that is, remember, the assessments we have out there are really management's best estimate. And what the auditors will review is really the approach on how management essentially achieve those estimates.

Operator

We'll take a follow-up from Mike Zaremski with Crédit Suisse.

Michael David Zaremski
Crédit Suisse AG, Research Division

Great. Just 2 quick follow-ups. Any California wildfire subrogation benefits this quarter expected? And also, just wanted to confirm regarding the mortgage insurance book, I believe you said that losses weren't booked unless the situation deteriorates or did you say that there was some IBNR put up, but you don't expect kind of losses unless things deteriorate?

Juan Carlos Andrade

President, CEO & Director

Yes. Thanks, Mike. Let me start off with mortgage first, and then I'll ask Craig to talk about the subrogation question. We have not put up any estimates for mortgage because we don't think we need to. We think our loss estimates, and we think our reserves are fine, more than adequate at this point in time. So we have not put up anything for the mortgage book. Craig?

Craig William Howie
Executive VP, CFO & Treasurer

With respect to the California wildfire subrogation, first of all, on the reinsurance side, we'll see a lag in reporting from our cedents on that. The PG&E settlement just happened this quarter. So it will take some time before it gets reported to us. On the insurance side, we don't expect much subrogation at all since we had very few losses related to the California wildfires in our Insurance segment.

Michael David Zaremski
Crédit Suisse AG, Research Division

Okay. So from the reinsurance, can you kind of look at what the -- you can see what your losses were and just expect a certain percentage of that to potentially come back in the coming quarters?

Juan Carlos Andrade
President, CEO & Director

Go ahead, Craig.

Craig William Howie
Executive VP, CFO & Treasurer

It depends on each season, and it depends on each contract that we have with them and how much coverage we have with them. And then they will report back to us depending on what their settlement was out of the PG&E settlement.

John Paul Doucette
Executive VP, President & CEO of the Reinsurance Division

Yes. This is John. I just wanted to add. So it very much is a function of what was their gross wildfire loss and then where do their reinsurance -- what is the attachment point and the limits. So some of it, it could meaningfully impact their ceded losses. In some cases, it could have no impact on their ceded losses. So we're really in a wait and see, as Craig said, waiting to see what the settlement, if any, was and what they report as the benefit to the reinsurers. And when and if they do that, we'll book that into our numbers.

Operator

And we'll take our last question from Josh Shanker again with Bank of America.

Joshua David Shanker
BofA Merrill Lynch, Research Division

This is probably easy, and probably not. I want to say. Can you tell us anything about the insurance or reinsurance markets in Lebanon, given the news last week and how we might want to think about that?

Juan Carlos Andrade
President, CEO & Director

Good question. I'll ask maybe John Doucette to start on the reinsurance side.

John Paul Doucette
Executive VP, President & CEO of the Reinsurance Division

Yes. So I mean, again, very early days. It's a small market, and we're looking at what the -- first, we're looking at what the coverages are that are offered in the region. So far, some of the brokers have come back with some modest coverages that are there. And really, we're still -- it's too early to tell in terms of what the ripple effect is, both for the building, the specific building that was at risk, but then also the broader -- the territory, the neighborhood that was impacted around that. So frankly, we're looking at it, but it's a relatively small market.

Joshua David Shanker
BofA Merrill Lynch, Research Division

And is your exposure in line with your global market share?

John Paul Doucette
Executive VP, President & CEO of the Reinsurance Division

We're still assessing that. We don't have -- we certainly would expect it to be, but it does vary by territory, but we don't have any reason to think it wouldn't be.

Juan Carlos Andrade
President, CEO & Director

I think it would be helpful to add that indigenous exposure would be de minimis, right? I think any exposure for the company really would be out of global treaties from global cedents, that sort of thing.

John Paul Doucette
Executive VP, President & CEO of the Reinsurance Division

Correct.

Operator

And that does conclude our question-and-answer session. I would like to turn the conference back over to management for any additional or closing remarks.

Juan Carlos Andrade
President, CEO & Director

Great. Thank you, and thank you for joining us today, and we look forward to continuing the discussions next quarter. But before I let you go, just echo what I said earlier. We feel very good about where Everest stands right now. We feel very good about our traction, our momentum and our ability to execute in this market. So thank you for your support, for your questions, and I hope you stay safe.

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