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ACGL.OQ - Q3 2025 Arch Capital Group Ltd Earnings Call

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OVERVIEW:

Company Summary

CORPORATE PARTICIPANTS

Nicolas Papadopoulos Arch Capital Group Ltd - Chief Executive Officer, Director

Francois Morin Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

CONFERENCE CALL PARTICIPANTS

Elyse Greenspan Wells Fargo Securities LLC - Analyst

Andrew Kligerman Cowen and Company LLC - Analyst

Andrew Andersen Jefferies LLC - Analyst

Joshua Shanker Bofa Merrill Lynch Asset Holdings Inc - Analyst

Tracy Benguigui Wolfe Research LLC - Equity Analyst

Ryan Tunis Cantor Fitzgerald LP - Research Analyst

Michael Zaremski Bank of Montreal - Analyst

David Motemaden Evercore Inc - Analyst

Robert Cox Goldman Sachs Group Inc - Analyst

Alex Scott Barclays Services Corp - Equity Analyst

Meyer Shields Keefe Bruyette & Woods Inc - Analyst

Brian Meredith UBS AG - Analyst

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the 3Q 2025 Arch Capital earnings conference call. (Operator Instructions) As a reminder, this conference call is being recorded.

Before the company gets started with its update, management wants to first remind everyone that certain statements in yesterday's press release and discussed on this call may constitute forward-looking statements under the federal securities laws. These statements are based upon management's current assessments and assumptions and are subject to a number of risks and uncertainties. Consequently, actual results may differ materially from those expressed or implied. For more information on the risks and other factors that may affect future performance, investors should review periodic reports that are filed by the company with the SEC from time to time, including our annual report on Form 10-K for the 2024 fiscal year.

Additionally, certain statements contained in the call that are not based on historical facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The company intends the forward-looking statements in the call to be subject to the Safe Harbor created thereby. Management also will make reference to certain non-GAAP measures of financial performance. The reconciliation to GAAP for non-GAAP financial measures can be found in the company's current report on Form 8-K furnished to the SEC yesterday, which contains the company's earnings press release and is available on the company's website at www.archgroup.com and on the SEC website at www.sec.gov.

And I would like to introduce your host for today's conference, Mr. Nicolas Papadopoulos and Mr. Francois Morin. Sirs, you may begin.

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

Good morning, and welcome to Arch's third-quarter earnings call. We delivered record results in the quarter with over \$1 billion of after-tax operating income and over \$1.3 billion of net income, both up 37% year over year. After-tax operating earnings per share of \$2.77, another record, represented an 18.5% annualized operating return on average common equity. These results reinforce the strengths of our diversified platform, which enables our underwriters to pursue opportunities and deploy capital across the enterprise. Meaningful contribution for all three segments, combined with solid investment returns, push year-to-date book value per share growth to 17.3%.

Our quarterly consolidated combined ratio of 79.8% reflect excellent underwriting and low cat activity in the quarter. Big picture, our nine months combined ratio of 83.6%, which include the impact of California wildfires and severe convective storms, highlight the strong underwriting performance across our businesses.

Now some comments about market conditions. As you have heard on other calls, competition is generally increasing. As cycle managers, we lean into the strengths of our brand, including underwriting discipline and using risk-based pricing tools to generate profitable business. We deploy capital into businesses we believe will generate superior risk-adjusted returns.

However, given relatively weaker market pricing and an attractive entry point for our stock, we repurchased \$732 million of shares in the quarter. Critically, our strong balance sheet and strong capital-generating capabilities permit us to both invest in our business and return capital to investors. Our objective is clear throughout the cycle: to maximize return for our shareholders over the long term.

Importantly, I want to emphasize that we are actively looking to deploy as much capital as possible towards attractive underwriting opportunities. Our playbook remains consistent: allocate capital to attractive opportunities that meet our risk-adjusted target returns, pursue profitable growth while prioritizing renewals that meet our return thresholds, and take full advantage of our operating flexibility across Insurance, Reinsurance, and Mortgage. Over time, this playbook has been key in enabling us to deliver consistently strong returns without regard to market cycles.

I will now provide some color from our reporting segment, starting with our Property and Casualty Insurance group. Underwriting income for the quarter was \$129 million, up 8% year over year on nearly \$2 billion of net premium return. Our combined ratio was 93.4%, with a current accident share ex-cat combined ratio of 91.3%, reflecting the strong underlying margins of our Insurance portfolio.

A distinguishing strength of our Insurance segment is its breadth across specialty lines, areas where our team applied deep knowledge and experience to drive better risk selection. Successfully navigating a transitioning market demands that our underwriters employ the capabilities and experience they have developed to leverage our differentiated offerings and market leadership position as we look to drive profitable returns.

When compared to the third quarter last year, we grew net return premium in North America other liability occurrence by 17%, supported by growth in middle market and double-digit rate increase in E&S casualty. Net written premium in our North America property and short-tail book increased 15%. Growth in middle market admitted property more than offset declines in excess and surplus property. International premium volume was essentially flat.

A strategic element of our Insurance growth is our middle market business in North America, which was significantly enhanced through the MidCorp and entertainment acquisition last year. As discussed previously, the acquired business provides a significant platform from which we intend to build further scale in the middle market sectors. Importantly, it is already driving growth and yielding tangible returns.

At the outset, we set three integration priorities for the acquired business: rollover the portfolio, remediate less attractive areas, and separate from legacy systems. We have completed the portfolio rollover. Remediation and separation are on target. Even though there is still work to do, we remain excited about this opportunity, which has been well received by our distribution partners.

Next, to Reinsurance, which delivered another strong quarter with a record of \$482 million of underwriting income. The 76.1% combined ratio was a significant improvement over last year's cat-heavy third quarter and illustrates our ability to generate attractive underwriting returns.

Net premiums written were \$1.7 billion, down roughly 11% year over year, reflecting current pricing conditions in short-tail and property cat lines and increased retention by cedents. The diversity of our insurance platform means we aren't overly concentrated in any one line. For example, property cat, which has been a hot topic of recent industry conferences, represents only 14% of Reinsurance total net premium return for the trailing 12 months ended September 30.

Our diversified reinsurance platform, supported by strong partnership with our broker and ceding company across multiple lines and geographies, further enhances our ability to navigate a competitive environment. We continue to like our prospects in most lines of business, and with improving conditions in casualty lines, our agility and ability to create opportunities is an advantage for us in this market.

Moving to Mortgage, which continues to operate exceptionally well, generating \$260 million of underwriting income for the quarter. The segment remains on pace to deliver approximately \$1 billion of underwriting income for the year and is a steady diversifying contributor to Arch's earnings. While Mortgage originations remain modest due to affordability challenge, our high-quality in-force portfolio continues to outperform expectations. We are well positioned to support first-time homebuyers when the US housing market eventually expands. The broader mortgage insurance market remains healthy with disciplined underwriting and stable pricing.

Now turning to investments, where strong earnings and cash flow grew investable assets to \$46.7 billion this quarter, with net investment income of \$408 million, a quarterly record for Arch. We continue to position the portfolio to remain conservative in the current environment with an eye towards generating reliable and sustainable earnings and cash flows for the group.

To conclude my opening remarks, I want to emphasize that we manage Arch with a long-term lens. That was true in the past. It is true today, and it will be true tomorrow. Market cycles span years, not quarters. And in a transitioning environment, our focus remains on producing superior returns and profitable growth.

Our ability to remain successful is rooted in our differentiated customer experience, superior risk-based pricing, and the creativity of our underwriting teams, which are empowered and incentivized to generate profitable business aligned with shareholder value. Today, we are well positioned to outperform in an increasingly competitive market. Our strong capital position gives us the flexibility to invest in the most attractive risk-adjusted opportunities, whether in the business or by returning capital to shareholders. This transitioning market is a moment to lean into our strengths with confidence and clarity.

I now turn the call over to Francois before returning to answer your questions.

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

Thank you, Nicolas, and good morning to all. Last night, we reported our third-quarter results with after-tax operating income of \$2.77 per share and an annualized net income return on average common equity of 23.8%. Book value per share grew by 5.3% in the quarter. Similar to last quarter, our three business segments delivered excellent underlying results, with an overall ex-cat accident year combined ratio of 80.5%, down 40 basis points from last quarter.

Our underwriting income included \$103 million of favorable prior year development on a pre-tax basis in the third quarter or 2.4 points on the overall combined ratio. We recognized favorable development across all three of our segments and in many of our lines of business. The most significant improvements were, once again, seen in our short-tail lines in our P&C segments and in Mortgage due to strong cure activity.

Current year catastrophe losses were low at \$72 million net of reinsurance and reinstatement premiums in what is typically our most active quarter for catastrophes. The Insurance segment's net premiums written grew by 7.3% compared to the same quarter one year ago, mostly due to the contribution of the MidCorp and entertainment unit for a full three months this quarter compared to only two months from the same quarter one year ago.

The ex-cat accident-year loss ratio improved by 10 basis points to 57.5% compared to the same quarter one year ago. And the 220 basis point increase in the acquisition expense ratio is primarily due to the benefit we observed in the third quarter of 2024 from the write-off of deferred acquisition costs for the acquired business at closing under purchase GAAP.

Profit commissions paid for prior accident years also explain some of the increase from the same quarter one year ago by approximately 40 basis points. The Reinsurance segment produced its best quarter ever in terms of pre-tax underwriting income at \$482 million, a direct reflection of the strong underlying profitability of the business written over the last few quarters and the absence of significant catastrophe activity in the quarter.

Overall, net written premium was down by approximately 10.7% from the same quarter one year ago. Of note, approximately 75% of the overall reduction is the result of two large transactions from the third quarter in 2024 in our specialty line of business that did not renew this quarter. The absence of reinstatement premiums also negatively impacted our top line this quarter.

Our ex-cat accident year combined ratio remains very strong at 76.8%, reflecting the robust level of underwriting margins in our book of business. Once again, our Mortgage segment delivered another very strong quarter with underwriting income of \$260 million. The improvement from last quarter was primarily due to a lower level of ceded premiums as a result of the tender offers we executed in the second quarter for two Bellemead Re securities. There was also a slight benefit due to a higher level of cancellations on CRT transactions.

The delinquency rate of our USMI business increased to 2.04%, in line with our expectations due to seasonality in the business. On the investment front, we earned a combined \$542 million from net investment income and income from funds accounted using the equity method or \$1.44 per share pre-tax. Net investment income remains an important source of income for us, and with the help of strong positive cash flow from operations, \$2.2 billion in the quarter, it should continue to grow in line with the size of our investment portfolio. The allocation of our portfolio remain neutral relative to our targeted benchmark.

Income from operating affiliates was strong at \$62 million due especially to a very good quarter at Somers Re. Our operating effective tax rate on a year-to-date basis stands at 14.7% and reflects the mix of income by tax jurisdiction. It is slightly below the 16% to 18% previously guided range, mostly due to a 1.7% benefit from discrete items. As of October 1, our peak zone, natural cat, probable maximum loss for a single event, 1-in-200 year of return level, on a net basis, remained flat at \$1.9 billion and now stands at 8.4% of tangible shareholders' equity. Our PML remains well below our internal limit.

On the capital management front, we repurchased 732 million of our shares in the quarter and added \$250 million to this number so far in October. On a year-to-date basis, we have repurchased 15.1 million shares, representing 4% of the outstanding number of common shares at the start of the year. As Nicholas mentioned, our balance sheet is stronger than it's ever been, and it remains a significant asset for us as we focus on executing our playbook and leveraging the value of the Arch brand as we move forward in this dynamic market.

With these introductory comments, we are now prepared to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Elyse Greenspan, Wells Fargo.

Elyse Greenspan - Wells Fargo Securities LLC - Analyst

My first question is just on capital. The level of buyback went up in the quarter, so I guess, my question is maybe two-pronged. Just how do we think about the level of buybacks going forward, just given the strong earnings this year? And then I know, last year, you guys had gone the route of a pretty substantial special dividend, so is this year the route more of buyback versus a special in terms of capital return?

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

Yeah. The last one, I think it's -- for us, we think of those as two options, but most likely not going to do both at the same time. So in this current environment where, yes, we certainly see our earnings profile being very strong and we think there's, as we've seen, right, limited opportunities for us to grow aggressively in the business. So capital return to shareholders will remain a focus, and given the stock price, I think share buybacks will be our preferred method going forward, at least for the short term. We'll see how things play out moving forward, but that's obviously something we talk with our Board on a regular basis.

So I'd say that's kind of where we're at. And again, balance sheet remains very strong. So is there room for us to do more buybacks as we move forward? And I think the answer is definitely yes and something we'll keep evaluating as we move forward.

Elyse Greenspan - Wells Fargo Securities LLC - Analyst

And then my second question is just on the insurance premium growth. So we've annualized the MidCorp deal, but there is going to be some impact from non-renewals there and obviously, just the overall market, which is softening in spots. So how do we think -- as you guys think about pricing, the combination of the non-renewals on MidCorp, how do you guys see the premium growth outlook for your Insurance book from here?

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

Yes, good morning, Elyse. Yes, on the Insurance side, I think we're still very much bullish about the business. I think we like the market we trade in, and we would like to grow. And we talk about profitable growth. That's what we're really focusing on. And you have to divide the market in three broad categories, first one being areas where we still see some rate increase. Casualty will be the main one, and the middle market business, where we think with the rate increase, and I think we have the propensity to grow. Then the second segment, which is the one that had witnessed headwinds in the past, which is mostly professional lines, whether it's D&O or cyber. The good news there, I think, the rate decrease really moderated on the D&O, pretty flat. And on cyber, there are signs that they are moderating, so that should be less of a headwinds going forward. And third, it's really the property, whether it's the large account property and the E&S property. The good news for us is that we don't write much of the shared and layer property business, and we have a relatively small footprint on the E&S side, which is really under a lot of pressure today. So I think overall, if I look at the outlook for us and our positioning in the London market as well, if I look at the outlook, I would expect us to have the ability on the Insurance to grow better than the market we play in.

Elyse Greenspan - Wells Fargo Securities LLC - Analyst

That's helpful. And then just one last one. There's a hurricane out there right now with the potential to impact the Caribbean. I don't think there is a lot of Insurance or even Reinsurance exposure there, but do you guys just have some high-level thoughts there just on potential exposure?

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

I think it's just too early to tell. I think, for sure, it's going to be -- looks like a big event potentially for Jamaica. And whether it's big enough to have repercussion that goes affecting the Caribbean, overall, too early to tell.

Elyse Greenspan - Wells Fargo Securities LLC - Analyst

Okay, thank you.

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

Just quickly, I mean, obviously, depending where it hits, like some of the resorts might be the insured values that might be more -- that we might participate on, just not knowing at this point where -- again, where things may land. But I think that's -- in terms of where the exposures are and what could be impacted, that would be the focus area, I would say.

Elyse Greenspan - Wells Fargo Securities LLC - Analyst

Thank you.

Operator

Andrew Kligerman, TD Cowen.

Andrew Kligerman - Cowen and Company LLC - Analyst

Maybe starting with, you just touched on growth in Insurance with Elyse, maybe shifting over to Reinsurance. You kind of kicked off, I remember in the first quarter, you thought that -- I think you did adjusted net written premium growth of 6 or 7%. You kind of repeated that in Reinsurance in the second quarter. And then this quarter, you talked about the two deals and the reinstatement premium is kind of creating a bit of noise. So part A of it is, what would the normalized growth have been in the absence of those items? And the part B is, how are you thinking about growth going forward in that segment?

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

Well, I'll take the first part. I mean, maybe Nicolas can chime in on the second. I mean, the normalized growth absent, call it, these kind of one-offs are, again -- and they happen, right? We've talked about it in the past, Reinsurance can be lumpy. There's deals that happen. They don't happen. The timing of it is not always predictable.

But yeah, the fact that with a little bit of the headwinds that we're seeing, again, coming from a very high bar on the property, property cat, 7/1 renewals, I'd say our growth in the quarter might have been around, like, call it, a decrease of 3% to 4%, not the 10% that we -- that is was reported in the quarter.

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

Yeah. Thank you, Francois. And on the outlook for growth on the Reinsurance side, so I think of Reinsurance pretty much the same outlook as Insurance. I think you have rate pressure on the short-tail lines. But I think you're seeing a rate increase in dislocation on the casualty lines that could provide opportunity. So I think, I would say, similar pictures, but for -- I think a big headwind is like a lot of our ceding company like the business like we do. We like the Insurance business.

So after a few years, there's less fear in the marketplace. People feel better about their balance sheets. So what we're seeing is companies retaining more, which creates significant headwinds for the Reinsurance group. I mean, by doing so, they either retain the business or move -- very often, you move more to an excess of loss position that present additional opportunities for us. And I would say that the margin on the excess of loss is usually better than the margin on the quota share. So I think we may see a different makeup of the margin going forward.

Andrew Kligerman - Cowen and Company LLC - Analyst

I see, I see. Thank you for that. And then maybe shifting back to Insurance, as a specialty writer and especially with pressure in E&S property these days, just more from the industry perspective, and you touched on your view of how Arch is going to do, but maybe again a little bit, but how do you see E&S premium for the industry playing out over the next few years? I mean, not only have we -- we've seen such tremendous growth over the last few years, but is it possible that E&S premium as an industry starts to decline over the next few years? And so outlook and then just Arch in E&S over the near intermediate term as well.

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

So I think -- the outlook of the industry, I think, it's a tale of two stories. I think on the casualty side, I think because of what's happening in the market and because of the issues people are having with the prior years and I think my view is that the trend of more of the business moving to the excess and surplus side where you have freedom of rate and forms and where you can add the exclusion that take a much longer time to be able to do on the admitted side, that will continue.

On the short-tail line, we could see some of the shared and layer business and your cat exposed business going back to the admitted market as we've done historically. So I think -- how to predict, but I think the fundamental shift, which has been driven by casualty, that I expect to continue.

Andrew Kligerman - Cowen and Company LLC - Analyst

I see. And then Arch, how do you see yourselves? Do you see gaining share on the short tail and the casualty, respectively?

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

The short tail will be a challenge based on what we see in terms of the pricing. I think we are more optimistic on the casualty side, where we've been underweight in the difficult years. And I think we're I think our loss pick has been holding pretty well. So that gives us confidence in how we price the business forward

So I think that -- as rates continues to improve, I think that gives us an opportunity certainly to do more at a time maybe where our competitors are still kind of caught up into looking at the right things they did in the earlier years.

Andrew Andersen - Jefferies LLC - Analyst

Okay. Thank you for the insight.

Operator

Josh Shanker, Bank of America.

Joshua Shanker - Bofa Merrill Lynch Asset Holdings Inc - Analyst

Yeah. I don't want to pigeonhole you too much, but obviously, you did a lot of buybacks in 3Q. Some companies don't do buybacks in 3Q because they're worried about the outcome of the hurricane season. But then trying to gauge your appetite for 4Q and maybe 1Q, when did you start buying back and how much -- were you buying the whole quarter or really were you able to do \$732 million within about a month ending up a quarter?

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

Yeah, I mean, it was pretty consistent throughout the quarter. I think there was a little bit more in September, and that's kind of, as I mentioned, I think we've been active in October as well. I think -- again, I think I touched on it on the last call. I think no question that some years ago, we would have said we would not buy during the hurricane season. I think Arch is different today than it was back then. I think Arch is much more diversified, much stronger, less exposed on our percentage of equity from a massive or a cat PML, even at the 1 and 250 or below.

So for all these reasons, we do feel and felt a lot more comfortable buying back during the wind season. And I think -- as I said earlier, I think we're going to keep pursuing that opportunity as we move forward.

Joshua Shanker - Bofa Merrill Lynch Asset Holdings Inc - Analyst

And you're not worried, in the past, you said part of the reason to do a special dividend was because you just don't think you can return as much capital as you desire to through the buyback of the limitations as you look out into the end of this quarter and beyond? Do you think you can satisfy every bit of capital return you need through repurchases?

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

It's a daily thing we look at daily. I certainly think we can do more capital return. We don't set a target for ourselves. I think it's an ongoing process. But there's a lot of liquidity in the stock right now, and we're able to buy back stock, we think we perceive to be a very attractive price. And we'll do as much as we can, how much we think is right. And then we'll see where we're at.

Joshua Shanker - Bofa Merrill Lynch Asset Holdings Inc - Analyst

All right. Thank you very much.

Operator

Tracy Benguigui, Wolfe Research.

Tracy Benguigui - Wolfe Research LLC - Equity Analyst

This is a bit belated that it's been a while since I've been on your call. Congrats on your S&P upgrade back in June. Since capital is so topical, my question is, while it's great that you have a AA- rating as a new category, you now have to hold AAA capital. Back when you were rated A+, you only had to hold AA capital. And I realize a lot of that was just model methodology driven. But my question is, how important is it to you to stay in this new rating category when you're thinking about your ability to deploy capital?

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

I mean, is it critical? I mean, it's not, but it's certainly an advantage, and we've seen the benefits of that already in some places, particularly in Europe. So no question that the new higher rating, I think, has been well-received, and we're able to benefit from that.

But you're right. I mean, it comes at a certain cost. I'd say, though, that the S&P capital model is only one of the things we look at. We have our own internal view of capital. We have our -- I mean, there's other rating agencies that we look at as well. So all in, I think our capital position remains very strong. It was always strong. And again, we try to optimize within all those constraints from all the rating agencies and regulators that look at us.

But the AAA level of capital that you mentioned is really not something that's not really new to us because we were, I'd say, already at that level. So that's kind of -- yeah, it wasn't an additional kind of burden or initial step we had to meet.

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

Yeah. I think we don't only manage one point. I mean, usually we look at AA, AAA. And for a while, I think we were a little bit on the penalty box because of the MI. So I think -- now, I think it's more -- I think it changed completely our capital structure. And also, I think it's been helpful on some of the MI, CRT, and SRT, where the buyer are extremely sensitive to the rating of those layers. And they actually pay a differentiated price for better ratings.

And as Francois said, I think in Europe, as we lean to, especially on the Reinsurance side, but also on the Insurance side, our strength is really casualty, professional lines, and as we lean into those markets, I think having a AA- rating is an advantage.

Tracy Benguigui - Wolfe Research LLC - Equity Analyst

Okay. So do you do it just opportunistically? Or could you see a scenario where you could reduce capital and live with -- back to the A+ rating?

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

(inaudible) I mean, it is a trade-off we all -- we constantly look at, right? I mean, how much capital do we need to hold on the margin to get the incremental rating? Right now, we already have the capital. We're not -- we're in a very strong capital position. But down the road, if conditions change, the question you ask is something that we've asked ourselves many times in the past, like how much capital do we -- is it really worth it to us to hold that incremental level of capital? But right now, given our capital position and again, given the strength of our earnings, the earnings profile where we generate internally the capital on a regular basis, I think we're in a very, very good position.

Tracy Benguigui - Wolfe Research LLC - Equity Analyst

Okay. My next question is, you said you like Insurance, and you're bullish on business, and you mentioned casualty rate increases. Casualty can mean a lot of things. So once I strip out some of the casualty lines, like you mentioned professional lines, what is really left -- what you're left with in terms of attractive pricing in GL, commercial auto, and excess liability, which includes auto? So I'm wondering where you're seeing the opportunities. Is it more auto-orientated? Or if you could just let me know the different casualty lines that are attractive.

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

Yes. I think one of the opportunities on the E&S casualty side, which would be excess, excess liability, so that would include some auto, but usually, we don't focus on the auto on the E&S side. And then we have other franchise, like rate sensitive business like national accounts or construction, which are casualty-lead lines with heavy components of workers' comp, general liability, and a lesser amount of auto. So those are the places where we think we have the ability to grow.

Tracy Benguigui - Wolfe Research LLC - Equity Analyst

Thank you.

Operator

Ryan Tunis, Cantor.

Ryan Tunis - *Cantor Fitzgerald LP - Research Analyst*

I just wanted to go back. I thought it was an interesting comment that on the Reinsurance side, you're seeing cedents proactively retain more. And I guess, I'm curious, when I look at the facultative property decline of 17% this quarter, how much of that is -- I don't know, you guys proactively walking away, or decline in exposure as opposed to rate? Because I was thinking it was kind of more rate-driven, but that comment made me think it might be more volume-based.

Nicolas Papadopoulos - *Arch Capital Group Ltd - Chief Executive Officer, Director*

No, I don't think we are cutting back. I think at this stage, I think we -- on the other property, which I think we should clarify other property line of business. I think the main factors there is a couple of our clients on the E&S side of the business and on the -- retaining more of the business at this stage. So that's really -- we would like to do more.

And also, I think, let's not forget, the rates are also going down. So some of our cedents are also revising some of their ceded premium to the downside. And so those are the two components, their ability to wanting to retain more of the business, and also, they're re-forecasting their growth downwards, which impacts our Insurance volume. (multiple speakers)

Francois Morin - *Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer*

Just to confirm, it's no question that the rate environment is down in property. There's also a drop in exposure, but just to be clear, that drop in exposure is typically not our decision, right? It's the cedents' decision. There are some situations where, again, they decide to keep it net or they use a different structure. But we still like the product. We still like the line. In most of what we do, we like a lot. And any reduction in exposure that you see that we experience is generally, at this time, more because the cedents choose to do something different, not because we decide to walk away.

Ryan Tunis - *Cantor Fitzgerald LP - Research Analyst*

Got it. And then just to follow up, you guys talking about the transitioning market. I think a lot of times we just want to focus on pricing, but I'm curious if what type of lines are -- it might be in primary because there's business going back to admitted and just some of the more bad stuff stays E&S or facultative, I guess, it could be a cedent just choosing to -- I guess, just continue to cede the stuff where they feel like there's an arbitrage. But like are there pockets you'd point out that are kind of particularly challenging to underwrite in this type of market where you really got to kind of cross your T's and dot your I's?

Nicolas Papadopoulos - *Arch Capital Group Ltd - Chief Executive Officer, Director*

I think it's a competitive market. I would say a lot of the market today, you get a lot of anti-selections. We develop a lot of data analytics tools to really segment our portfolios and provide underwriters some really granular information which price for which risk, which limit for which risk. So I think underwriting the market, we are bullish because we have those tools. I think if you don't have the tools, I would be a lot less bullish about our ability to write profitable business going forward.

Ryan Tunis - *Cantor Fitzgerald LP - Research Analyst*

Thank you.

Operator

Did you have further questions, Ryan?

Ryan Tunis - *Cantor Fitzgerald LP - Research Analyst*

I'm good. Thanks, guys. Appreciate it.

Operator

Mike Zaremski, BMO.

Michael Zaremski - *Bank of Montreal - Analyst*

Pivoting to the Mortgage side of the business, I feel like when we were to quiz most people and ask them what the historical five, six, seven-year loss ratio was, most people wouldn't guess it was 0. And obviously, there were unique circumstances in the past five-ish years. But just curious -- and we know it's a feast or famine business, but curious if your views on a normalized loss ratio is different compared to the past, if we think about the current cycle and the next cycle coming.

Francois Morin - *Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer*

Well, not knowing what the next cycle will look like, I think we'd be speculating. I think we have talked about a normalized loss ratio in the 20% range across the cycle. I think we have said, and we believe strongly that home prices are the key driver of what the performance will look like for the Mortgage book. And so far, home prices have remained very strong. There's been some pockets. There's been some home price declines, some home price declines in a few areas, but across the nation, across the US, you can see that home prices remain very strong. So that, I think, explains in large part, I'd say, the outperformance of the Mortgage business relative to what we would have thought over an extended period.

Does that remain the same going forward? Again, there's a lot of macro factors that will come into play on that, but as long as -- and we do have strong beliefs that based on lack of inventory and the lack of housing in the US, I think we'll support home prices for the foreseeable future. And on that basis, we'd like to think that the performance will remain strong. Now, does it inch up a little bit over time? Maybe a little, because it feels like it's been really, really good for a long, long time. But for the time being, again, we've said it, and we still are very, very, very bullish about the Mortgage business, because it's been truly a terrific business for us.

Michael Zaremski - *Bank of Montreal - Analyst*

Got it, understood.

Nicolas Papadopoulos - *Arch Capital Group Ltd - Chief Executive Officer, Director*

And the underwriting remains excellent. I think if you look at the FICO distribution, I think they're getting better. So that will drive better outcome.

Michael Zaremski - *Bank of Montreal - Analyst*

Got it. Moving to capital management. Clearly, you signaled buybacks are high on the list. Maybe you can just give us an update. Has anything changed quarter on quarter on maybe inorganic opportunities? Is US small commercial still something that's on the -- retail small commercial still high up on the wish list? Thanks.

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

Yeah, the wish list is long. I mean, we -- but by the same token, we have a lot that we are working on and can work on. Middle market is obviously a big focus for us. We've talked about other areas that we'd like to grow in. But as you know, these M&A opportunities, they don't happen that often. They take a while to materialize. So we're not going to hold a ton of excess capital just in the -- on the potential that we might do an M&A transaction. I mean, our leverage ratio is it's maybe the lowest it's ever been. So we've got a lot of flexibility. The balance sheet is strong. We got some excess capital.

So we got a lot of flexibility in our ability to execute on that, I think, is really good. So if there's other things that we can get our hands on that would make us better, we'll be happy to do that. But in the meantime, there's a lot that we already have that are -- that is -- we can generate good earnings on as well.

Michael Zaremski - Bank of Montreal - Analyst

Got it. And maybe just taking one last one in since you guys provide excellent market commentary. And Nicolas, you provided a good view of how to think about the E&S marketplace going forward. Do you all have a view on what has also been the kind of exponential growth of the MGA marketplace and kind of how it's been impacting Arch or maybe the industry? And do you view the MGA's marketplace growth to continue to grow much faster than the rest of the market? Thanks.

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

Interesting subject. I'm personally bearish on the MGA. I think, historically, strong growth in the MGA except for a few exceptions didn't turn out to be good. I think the lack of incentive alignment, the delay in the information to the insurance carrier or the reinsurers, I'm not bullish on that model. So I think it's been the flavor of the month and the last few years, and I'm still a little bit questioning what the outcome is going to be.

Michael Zaremski - Bank of Montreal - Analyst

Thank you.

Operator

David Motemaden, Evercore ISI.

David Motemaden - Evercore Inc - Analyst

Just had a question. Obviously, still very good reserve releases. Just focusing in on Insurance and Reinsurance specifically, could you talk about the movement between long-tail and short-tail lines between those two? Any sort of things to point out on that front?

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

I'd say nothing unusual, very similar to prior quarters. There is a little bit of the adverse on casualty. I mean, nothing that stands out. It's a couple of -- could be one accident year within one business unit, the one line of business. So small adverse on casualty, which I don't think is surprising, at least to us.

But when we look at the overall picture around kind of where -- how the reserves are performing or quarterly actual versus expected, which is still showing favorable, meaning lower than expected, I think gives us a lot of comfort there. So we're reacting to the data. And in some places, there's

no question. There's trends that are showing up that we're addressing. But big picture, the short-tail stuff did extremely well as it has for quite some time, and we'll keep evaluating it every quarter.

David Motemaden - *Evercore Inc - Analyst*

Got it. Thanks for that. And then just taking a step back, the mix shift to casualty lines in both Insurance and Reinsurance, at least if I look at it on an earned basis, that definitely is up a bit year over year, hasn't really increased much, I guess, over the past few quarters. Is that having any bit of an impact at all on the underlying loss ratios in either segment? And how should we think about that going forward?

Nicolas Papadopoulos - *Arch Capital Group Ltd - Chief Executive Officer, Director*

So I mean, at some point you will, but because I think the loss pick on the casualty line is a bit higher than the loss pick on the short-tail lines. But I think the shift -- the mix hasn't really changed fundamentally at this stage, I think. So I think down the road, I think it might.

David Motemaden - *Evercore Inc - Analyst*

Great. Thank you.

Operator

Rob Cox, Goldman Sachs.

Robert Cox - *Goldman Sachs Group Inc - Analyst*

Yeah, just curious, as you start to renew the MCE book, anything interesting you're seeing either on the delegated or the non-delegated side? And how far are we through the non-renewals on the programs book?

Nicolas Papadopoulos - *Arch Capital Group Ltd - Chief Executive Officer, Director*

So I think what we've seen so far, and I think we've renewed -- the entire book has been transferred to Arch. I think we -- I'm personally very pleased with what we've seen so far, and I think the stickiness of the business, the ability to provide additional lines of business or distribution partners to be more relevant to them, the property expertise that in the admitted property business that we really didn't have, that we acquired, all those assumptions that we had made at the time of the purchase turned out to be true

So I'm actually very pleased with the strategic decision we made to go for the acquisition. On the delegated side, the MGA, I think we knew -- we didn't do the deal because of the MGA portfolio that was coming with the acquisition. So I think we started the remediation, and there, I think it's pretty much what we expected. And I think it takes more time than you think because all these MGAs have notice periods. So I think we will see the impact really in 2026 of the non-renewal -- of the notice period that we send a number of those MGAs this year.

Robert Cox - *Goldman Sachs Group Inc - Analyst*

Got it. Thank you. And then just wanted to follow up on credit. I mean, just given the Mortgage book and the investment in Coface and I think a relatively larger private credit book that you guys have, any thoughts on the credit environment and anywhere you're leaning into or out of, just given some of the noise in private credit?

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

Yeah. I think you've got to be careful, I'd say, in what we're looking at. No question that certainly maybe the headlines around subprime auto loans not performing well, I think that's a totally different type of customer than what our borrowers would be on the USMI front. So I think that -- and we're not seeing any of the same kind of results and that I guess the proof is what we reported this quarter.

So again, very specific around kind of the type of borrowers in the US, the trade credit world, no question that there's been a couple of insolvencies that have made the headlines that we -- Coface, we don't know, but may be exposed, and that's for them to work on. But there's no question that when these types of events happen, people will start to think a bit harder about dependencies in the credit and lines of credit they extend, et cetera. But that's not unusual.

So at this point, we're very, very comfortable with the exposure we have. We understand it well. And obviously, we look and monitor all the external data and the trends that are happening. But so far, there's nothing really that stands out that we think we have to adjust our thinking or strategy.

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

And more specifically on Coface, I think this is short-term credit. The game here of the underwriting is really -- as you are aware of the weaker credit, is really to over time cut your line to that particular credit name so that when the inevitable happens, your exposure is much less. I think they played that game really, really well. And I don't know about the latest insolvencies, but historically, they've been very good at that.

Robert Cox - Goldman Sachs Group Inc - Analyst

Thanks for all the color.

Operator

Alex Scott, Barclays.

Alex Scott - Barclays Services Corp - Equity Analyst

First one I had was just circling back on Rob's question on the remediation. Could you frame for us at all, like how much impact that could have on the Insurance segment. I just thinking through trying to dial in premium growth estimates and knowing how much some of us missed our Reinsurance growth this quarter from not knowing about the transaction. I just want to make sure I'm layering in enough for this lagged remediation impact.

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

Yeah. So specifically on the programs we acquired, the premium that we've identified and has been -- will be nonrenewed is roughly \$200 million. And again, Nicolas said, the notices went out, and then there's a notice period, and then MGA has three to six months to find another carrier. And some are more -- I mean, some are more successful in getting a replacement sooner. So some of that may actually start happening in the fourth quarter. I don't have the precise like projections on when it's going to hit the top line in each of the next few quarters.

But just at least give you an idea, like, call it, \$200 million part of \$1.5 billion to \$1.6 billion book is -- which was the overall MCE premium volume that's kind of the impact that we expect to see, the flip of that, though, is the middle market business that we really was attractive to us was really what we were trying to get has done very, very well. So the rate environment both on casualty and property in that business has been very good. And we just came back from a couple of industry conferences where the business partners are very supportive, and they are very happy to do business with Arch. So we'd like to think that some of that kind of headwind in terms of giving up or nonrenewing some of those programs, we can make up some of that, at least in the middle market side.

Alex Scott - Barclays Services Corp - Equity Analyst

Got it. Helpful. Second question I had is on the Reinsurance business in casualty specifically. The repricing efforts, I guess, a lot of it's on the quota share, the actual underlying primary taking rate. Can you characterize what you're seeing there? I mean, are the underlying primaries taking enough rate where it's in excess of loss cost and it's actually building improving margin in there. Is that why you're speaking more optimistically about it? Or is it still pretty obviously, high loss cost environment. So I'm just trying to get a feel of whether that's actually improving or not.

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

So I think you got it right. I think we believe in casualty in general, we're getting more rate than the last cost, and it's an elevated loss cost. So I think that's what -- if you back on the Reinsurance side, if you back the right specialty underwriters, people that manage their limits well, avoid some of the heavy auto or other difficult class of business, I think you would want to do more business with them. And I think over time, we expect to be able to write more of that business.

Alex Scott - Barclays Services Corp - Equity Analyst

Okay. Thanks.

Operator

Andrew Andersen, Jefferies.

Andrew Andersen - Jefferies LLC - Analyst

Maybe you could just expand a bit on how you're thinking about 1/1 prop cat renewals. Do you still see returns of kind of 20% here on this line? And how are you thinking about ILS impacting kind of return levels and industry capital?

Nicolas Papadopoulos - Arch Capital Group Ltd - Chief Executive Officer, Director

Yes. On the cat side, we remain bullish. The outlook is bullish. We like the margin and maybe a couple of data points. The market really peaked in July 2024. So a little bit over a year ago.

And I think in 2025, market -- the price went down between 5% and 10%. So we are into our second round of rate decrease. And depending on the region, the increase that we witnessed from 2021 to 2024, some of those rate doubled. So I think we are in a good place. It depends on the region.

But generally, we remain optimistic that the business is attractive. There's more demand. We had more demand last year. We expect more demand to come to the market in the US on an international basis. So overall, we think despite pressure -- expected pressure on the rates, we will remain -- we think the margins are still very attractive.

Andrew Andersen - Jefferies LLC - Analyst

Thanks. I'll leave it there. Thank you.

Operator

Meyer Shields, KBW.

Meyer Shields - *Keefe Bruyette & Woods Inc - Analyst*

Just in the past, you've talked about ramping up some spending associated with MidCorp. I was hoping we could get an update of timing and maybe amounts of increased spending.

Francois Morin - *Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer*

Well, increased spending, I think, was more -- the focus -- question that we got, I don't want to call it a bare bones organization, but the people that transferred back in August of 2024 was, call it primarily underwriters and claims people, right? So that was the bulk of the staff, the transferred and what we talked about at that time was that, yes, we would need to hire to reinforce our capabilities in terms of actuarial, data analytics, and a few support functions here and there. So that, we knew it would take some time. It's a competitive job market. We've been able to address some of that, too.

But I think ultimately, it's still -- I want to say on the expense ratio on the OpEx side, I mean, we're -- we can run the incremental MidCorp business at a more efficient or lower expense ratio than we had pre the acquisition, given the synergies and kind of some of the infrastructure costs that we can spread to a bigger base. So I think we still have a few, I'd say, openings that we're trying both on the underwriting side and on the kind of support functions that we're trying to fill. But we've done -- a lot of the work has been done in the last year, and it's showing, right? The business is doing well and we're able to execute on the strategy and try to grow in some specific areas. So we're -- again, a little bit of work to do, but we're in a good spot.

Meyer Shields - *Keefe Bruyette & Woods Inc - Analyst*

Okay, perfect. Thank you so much.

Operator

Brian Meredith, UBS.

Brian Meredith - *UBS AG - Analyst*

Two quick ones here. Just going back to the whole MCE MidCorp in the program business runoff, the underlying loss ratio improvement in Insurance, is that a direct result of some of the actions being taken there? Or is that something else? And therefore, as we start to see this run off, should we start to see underlying loss ratios continue to improve in Insurance?

Francois Morin - *Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer*

It's more the latter. The impact of the non-renewals has not really come into play into our -- on an earned basis. So the improvement, again, somewhat not huge on this quarter, but I think the -- hopefully, there should be some benefit as this business runs off, and we'll see some improvement or at least some stable loss ratios.

Brian Meredith - UBS AG - Analyst

Great, thanks. And then first of all, I wonder if you could talk a little bit about the substance base tax credits that Bermuda came out with, I think it was the end of September, what that impact could potentially be for you all?

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

A bit early to tell. No question, yes, the consultation paper is out. Comments have been submitted. We have had meetings with obviously the insurance community with the government expressing our views. The biggest, can I say, remaining item that we don't have clarity on is on the transition credits. I mean, at what pace will these kind of credits be allowed to be reflected starting in 2025. So that is still to be determined. There's work being done on that right now.

We expect to have clarity in the, call it, first half of December, clarity slash almost finality, because it has to be enacted before the end of the year for us to be able to reflect it in our financials. But to your question, Brian, I think it will be substantial, we hope. And when we have like the law, I mean, we'll be very quick to share that with you all and give you a bit more color on what that might mean for us.

Brian Meredith - UBS AG - Analyst

Great. Thank you.

Operator

At this time, I'm not showing any further questions. I would like to turn the conference back over to Nicolas Papadopoulos for closing remarks.

Francois Morin - Arch Capital Group Ltd - Chief Financial Officer, Executive Vice President, Treasurer

Yes. Thank you for spending time with us this morning, and we're looking forward to talking to you next quarter. Thank you.

Operator

Thank you, sir. Ladies and gentlemen, again, thank you for participating in today's conference. This concludes the program. You may all disconnect your lines.

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