Atlas Financial Holdings 2014 Third Quarter

Earnings Conference Call

Speakers: Scott Wollney, Paul Romano

Operator: Greetings, and welcome to the Atlas Financial Holdings 2014 Third Quarter Earnings Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation.

If anyone should require operator assistance during the conference, please press star zero on your telephone keypad. As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Scott Wollney, President and CEO. Thank you. You may begin.

Mr. Scott Wollney: Thank you very much, Jessie [sp], and good morning everyone. With me today is Paul Ramano, our vice president and CFO. Before we begin, I'd like to acknowledge that today is Veteran's Day. Thank you to those who serve and have served to protect our country and its freedoms.

In this morning's call I'll discuss Atlas' operating performance and what we're seeing in our niche and the commercial auto market overall. Paul will review our third quarter financial results in greater detail, and then I'll return to discuss our plans for future growth and the recent announcement of our acquisition of Global Liberty.

I'll now turn it over to Paul.

Mr. Paul Ramano: Thank you, Scott, and good morning everyone.

Yesterday after market close, Atlas issued its 2014 third quarter financial results. A copy of this press release is available at the Investor Relations section at the company's website at www.atlas-fin.com. We will be utilizing a slideshow presentation in conjunction with this call.

This presentation is available on our website's Investor Relations section, and then under the earnings release info selection. We welcome each of you to review this presentation and follow along.

On this call, Atlas may make forward-looking statements regarding the company, its subsidiaries, and businesses. Such statements are based on the current expectations of the management of each entity. The words anticipate, expect, believe, may, should, estimate, project, outlook, forecast, or similar words are used to identify such forward-looking information.

The forward-looking events and circumstances discussed in this call may not occur and could differ materially as a result of known and unknown risk factors and uncertainties affecting the companies, including the risks regarding the insurance industry, economic factors, and the equity markets generally, and the risk factors discussed in the risk factors section of it's Form 10-K for the year ended December 31, 2013.

No forward-looking statement can be guaranteed. Except as required by applicable securities laws, forward-looking statements speak only as of the day in which they're made, and the company and its subsidiaries undertake no obligation to publically update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

When discussing our business operations, we may use certain terms of art, which are not defined under U.S. GAAP. In the event of any unintentional difference between the presentation materials and our GAAP results, investors should rely on the financial information in our public filings.

All amounts discussed on this call are in U.S. dollars unless otherwise indicated. For those of you following along with our presentation, we will begin on slide 4. With that, I'd now like to turn the call back over to Scott.

Mr. Scott Wollney: Thanks, Paul.

The last three months continue the momentum that we've built in previous quarters, and we are pleased with the steady profitable growth in our core lines. We reported strong underwriting improvement, including considerable increases in gross premiums written, net premiums earned, and that income.

Throughout all of this, we've been vigilant with respect to pricing and claims management and our core taxi, livery, and paratransit lines, which to date, have been steadily improving, and trends remain favorable. Let me touch on our financial and operating results from the quarter, which are outlined on slide 5 of our presentation.

Gross written premium increased 31.1 percent in the third quarter. It's important to note that in the third quarter we renewed our New York Excess Taxi program. This is a business arrangement providing excess coverage above the levels of risk retained by the insured, and only a small number of [unintelligible] owners qualify for this program.

As a result, we do not expect the premium volume related to that program to vary significantly year-over-year. If you remove this excess taxi business, Atlas' increase in gross written premium was 53.7 percent in the third quarter. We reported significant improvements in our profitability for the period with net income of 3.5 million in the third quarter as compared to 1.7 million in the prior year same quarter.

This equates to net income of $0.29 per common share diluted. Ultimately, we define our success by long-term return on equity, growth and book value, and responsible capital management. For the quarter, we reported an annualized return on equity on 14.5 percent, an increase book value for the seventh consecutive quarter. The increasing scale of our business coupled with responsible operating cost management moved our expense ratio towards the 10 to 12 percent range that we consistently share as a near-term target.

The operating leverage in our insurance subsidiaries remains relatively low at 1.27 times net written premium to surplus. As noted in our recent call regarding the acquisition of Global Liberty, completion of the transaction will result in our operating leverage being closer to two times.

The quota share reinsurance treaty we put in place provides us with flexibility to ensure that capital is only raised at levels we deem to be attractive, and we have no debt on our balance sheet. As compared to the same quarter last year, we saw improvement in each of our financial ratios producing a combined ratio of 89.6 percent during the third quarter, and $1.6 million increase in operating income.

On slide 6, we highlight our combined ratio trends since our U.S. IPO in the first quarter of 2013. This quarter, Atlas achieved a combined ratio below 90 percent for the first time since we brought the company public, and we still feel that there's more room for continued improvement in the current market cycle.

Our loss ratio improved 120 basis points over the same quarter last year. This slight increase in our loss ratio is compared to the second quarter of this year with the outcome of our business mix in the quarter. We continue to expect this ratio to trend towards our underwriting margin targets, which are now consistently below 60 percent.

Paul will go into greater detail on the components of our combined ratio for the quarter later in the call. I think it's important to briefly explain the infrastructure we built, and how we see it driving both our growth and the ability to correctly price our products to generate expanded margins.

We operate in a niche market within the $25 billion commercial auto space in the U.S., which has historically outperformed the property and casualty industry throughout several market cycles. Last quarter we shared the fact that we estimate our light [sp] commercial auto niche to have grown to be approximately 2 billion as an addressable market, largely due to the greater number of the owner operator and small fleets that Atlas targets.

We feel that a proportionate market share of 20 percent in all geographic areas where we operate is achievable during the current market cycle, and to date, our growth is supporting that conclusion. And we're seeing rate increases in the majority of our territories due to the hyper-elasticity to the market cycle typically seen in our niche as well as in other specialty lines of insurance.

The fundamental reason we expect to achieve return on equity in excess of the P&C industry at large irrespective of market cycles is our specialized focus. The taxi, livery, and paratransit business places a great demand on service due to the high frequency of interactions between the insured agents and insurance company in the underwriting service and claims areas of the business.

Our model is designed to meet this demand with a straightforward, but a critically important value promise. We help keep our customers' business in business. We do this every day in every aspect of our operation whether it's quickly reviewing a driver against our underwriting criteria, ensuring that a customer's local insurance reporting obligations are met, or handling a claim in a way that meets the critical needs of the business' reinsurer.

We're only able to deliver on this value promise by truly understanding our clients' needs and by taking advantage of what we know from the decades of experience and the high-level of commitment our organization has to the specialty niche on which we focus. This approach increases customer engagement and allows our company to have a stronger control over risk selection, pricing, and claims management within our marketplace.

Our growth rate has been achieved by leveraging the important heritage that our subsidiary brands have earned over the years, the strong value promise we offer, and the specialized and committed independent agency network who distribute our products. These are focused agents, 75 percent of which have more than 10 years of experience selling our core products for one or more of our insurance subsidiaries.

They understand Atlas' value promise and how to sell it. We do not distribute through wholesalers, managing general agents, or other intermediaries who are disconnected from the point-of-sale. In the next two slides, we outline Atlas' current geographic footprint and increasingly diverse nature of our book of business.

As seen on Slide 7, Atlas is currently licensed in 49 states, and actively distributes products in 40 states plus Washington DC. These are shown in blue on the map in our presentation. We only write business in states where we feel that we can generate level of profitable premium that will offset upfront cost of entry within 12 to 24 months. These states must be areas where our value promise will allow higher than average pricing.

Further, each state must be a market that we deem favorable in terms of achieving underwriting profitability, that is we need to be able to properly gauge and value potential loss. As a result, we avoid states where there is a high propensity for fraud.

We review each state in which we are writing business regularly to evaluate rate efficiency, and to validate there are assumptions in the three areas I just mentioned are holding up. In the last favorable market cycle, our first two subsidiary companies, American Service and American Country, wrote over $125 million of premium in Atlas' niche market in only a handful of states.

Gateway, the third company we acquired, wrote approximately 25 million. Today we are in 40 states and still have considerable room to grow with the niche. On Slide 8, we breakout our premiums by state. You will see that New York is larger than normal during the quarter as a result of the Excess Taxi program, but overall we have an increasingly geographically diverse book of business, particularly on an earned premium basis.

As noted earlier, we believe we can achieve a 20 percent market position without having a disproportionate share of the business in our niche. We expect growth in the large number of states where we currently have less than 3 percent market share to be marginally greater among mature states, like Illinois, which currently has our largest market penetration at approximately 10 percent.

We continue to leverage brand strength in markets where our companies were traditionally strong and are also establishing a position of market leadership in states we entered over the past few years. Our strong value promise, marketing efforts, and commitment to the niche are paying off.

On Slides 9 and 10, we share some of the key leading indicators that support our view on pricing. We've seen increases in new business submissions and are writing a greater number of policies at a healthy rate of growth. But, equal importance, our renewal retention continues to remain above target levels.

We're retaining policies at the highest percentage since we came public. Every production metric is moving in the right direction year-over-year, and at the same time we continue to increase our underwriting profit targets. On Slide 12, we've included recent industry data that we feel highlights two main items.

First, that small accounts, the type that Atlas targets, are outperforming the pricing trends seen with larger accounts. Second, the commercial auto is outperforming the entirety of the market in terms of rate, and although rate increases slowed in the second quarter of 2014 as we expected incremental rate increases are coming back in the third quarter.

On Slide 13, we outlined what pricing changes in operating scale can ultimately mean to Atlas both on a combined ratio and return on equity standpoint. These loss ratios are the range typically seen from soft to hard markets. We're currently pricing below a 60 percent target in every geographic market in which we focus, and our operating leverage and scale are increasing.

Atlas' business is generally one of low severity and high frequency. The light vehicle segments in which we focus have a relatively lower limit profile than most heavy commercial auto segments. Therefore, our exposure to severity surprises is also inherently less than other higher limit lines of business.

We've built our model and decades of data, strong relationships, accurate pricing, and a value promise that is specific to the needs of our niche. We feel some of these parts allow Atlas to continue to be a margin leader in both hard and soft markets. We expect that leading the cycle will ultimately result in maximum accretion to book value and return on equity.

We're already pricing at levels below those shown in the middle box on slide 13. As our loss ratio trends towards target levels over time, and we increase operating leverage and scale, ROE will follow.

I'll once again turn the call over to Paul for a review of our financial results.

Mr. Paul Romano: Thank you, Scott.

I'll briefly go through quarterly highlights, but welcome each of you to review our press release and filings should you have any further questions. Our financial overview in the slide deck begins on page 15. Atlas' gross premium written increased 31.1 percent to $42 million during the quarter compared to 32.1 million in the three-month period ended September 30, 2013.

The improvement relative to the third quarter 2013 is attributable to our market penetration and an improving competitive landscape across the company's distribution platform. Excluding the company's Excess Taxi program, which renews in the third quarter, that is not expected to vary considerably in size year-over-year. Gross premium written on core lines increased 53.7 percent as compared to the same quarter of 2013.

Effective July 1, 2014, we entered into a quota share reinsurance contracts with Swiss Re. Our initial session is 5 percent of subject written premium, which equated to 2.1 million of ceded premium written in the third quarter 2014. Including the impact of quota share reinsurance, net premium earned increased by 42.3 percent to 25.6 million for the quarter compared to 18 million in the prior year period.

Our net premiums earned ratably over the term of our policies, which are generally 12 months in length. As a result of the growth in net premium earned, we are continuing to see the benefits associated with our operating scale. This, along with favorable year-over-year loss trends, led to a combined ratio of 89.6 percent during the period.

Let me discuss the combined ratio components in greater detail. Atlas’ loss ratio was 62.2 percent in the third quarter 2014 compared to 63.4 percent in the prior year period. As Scott mentioned earlier, we've been pricing lower than a 60 percent loss ratio, and believe we could see further improvement.

However, it's important to note that we will always wait to observe loss reporting before giving credit for rate increases. Acquisition costs represent commissions and taxes incurred on net premium earned. Through the third quarter, acquisition costs were $3.7 million, or 14.4 percent of net premium earned as compared to 15.9 percent in the prior year quarter.

While this number can vary from period to period, 14 to 15 percent remains a reasonable annualized target for this ratio. The other underwriting expense ratio, or OUE, decreased by 1.6 points to 13 percent for the current year quarter as compared to the prior year quarter. This incremental margin is primarily due to the operating scale that was achieved despite our 16 percent increase in additional staff during the first nine months of 2014.

We have hired this additional staff in anticipation of continued above average growth. We feel very comfortable with our current infrastructure, although we continue to remain vigilant in reviewing our operating needs in conjunction with our growth.

As communicated in the first quarter of 2014, the company is accruing [sp] for expected management and director incentive compensation to mitigate lumpiness quarter-to-quarter. This expense represented 1.6 percent of the OUE ratio in the three-month period ended September 30, 2014. The improvements in the combined ratio led to strong gains in our bottom line.

Net income for the quarter was $3.5 million, an increase of--over the 1.7 million reported in the third quarter of 2013. Earnings per diluted common share were $0.29, representing a $0.12 increase as compared to the third quarter of 2013 before taking the impact of the $1.8 million discount upon redemption of preferred stock that occurred in the third quarter of 2013.

On slide 16, we detail the elements impacting book value from year end 2013. As indicated, we have increased book value by $1.70 per share to $8.24 at September 30, 2014. We continue to maintain an allowance against deferred tax assets, which was $0.56 per share at September 30, 2014.

The company has been reducing its valuation allowance against deferred tax assets by an amount equal to the amount of income tax expense generated for the period. A full and comprehensive analysis of our tax accounts will take place during the 2014 year-end audit, which could result in future reductions in, or the elimination of the valuation allowance.

This assessment will include, but will not be limited to, continued underwriting profitability, the lack of significant prior year loss reserve development, continuing favorable market conditions, continued positive trend in taxable earnings, and other such indications deemed positive. To the extent that any changes made to our tax accounts or valuation allowance as a result of this analysis, we will clearly articulate the impact on both book value and future earnings on our next quarterly call.

In the next two slides, we include information on our balance sheet. Primarily, as a result of the capital raise completed in the second quarter of this year, Atlas' cash and invested assets at September 30, 2014 increased to 179.2 million as compared to 139.9 million at December 31, 2013. Our balance sheet and investing philosophy is focused on properly preserving our capital to redeploy into our business.

Our investment duration remained consistent with our expected liquidity needs and claim payout patterns at 4.3 years. And the majority of our holdings are on fixed income securities rated AA or better by S&P.

With that, let me turn the call back to Scott for his concluding remarks.

Mr. Scott Wollney: Thanks, Paul.

Last month we announced our pending acquisition of Global Liberty. While I won't reiterate all the comments from our conference call on October 17th, we feel that this is a milestone acquisition for Atlas, and I will again share some of the key takeaways on this call.

In the current market environment, our focus in the M&A area is on companies that will be accretive in the near term and additive to strategic infrastructure over the long-term. Our criteria for companies within our current niche is that they be a complementary fit within the Atlas network while also accelerating our ability to achieve proportionate market share during the current market cycle.

New York is the largest single state in our addressable market, and is an important and complex area in our niche. We estimate the public auto premium universe in New York to be approximately 600 million, or slightly less than a third of our current addressable market. Global Liberty is a specialized business built on decades of experience in the public auto space.

They're a profitable company with excellent workflows, depth and expertise, and a commitment to our niche market. Our focus coupled with Global Liberty's attributes make it an excellent fit for Atlas. Global Liberty currently writes approximately 40 million of annual commercial auto gross written premiums with the majority of this business generated in the New York metro area.

Together, Global Liberty and Atlas' collective market share will be estimated at approximately 7 percent of the public auto segment in New York, and approximately 2.5 percent of the broader commercial auto market in New York. Estimated annual income generated by the businesses to be acquired is approximately 4 million on a pro forma basis. This equates to greater than 20 percent return on equity.

Based on our current outstanding share count and excluding non-recurring transaction expense, pro forma income accretion would be approximately $0.34 per share, or $0.09 per quarter based on expected 2014 results. As communicated previously, non-recurring transaction related expenses are expected to be $0.05 to $0.07 in Q4 of this year, and $0.06 to $0.08 in the first quarter of 2015. No further nonrecurring integration expenses are anticipated beyond that.

We feel this transaction will provide both short and long-term benefits to the company and pending regulatory approval. We expect to close the acquisition early in the first quarter of 2015. I encourage each of you to review our filings and press release for more detail about the transaction.

To sum up, our management team is focused on maximizing return on equity over the long-term with the objective of outperforming the P&C industry by 500 to 1,000 basis points. Leveraging our company's heritage, expertise, and value promise to achieve above-average underwriting results.

Last quarter we indicated that based on market condition and our pricing targets, we expected 2015 gross written premium to approach 200 million. At this point we're confident that with the addition of Global Liberty, next year's premium levels will exceed $200 million. While there is some overlap between Global Liberty's distribution channel and Atlas' current channel outside of New York, there is virtually no overlap in New York, which is the largest market in our niche and the largest portion of Global Liberty's business.

As we begin the integration of Global Liberty and its distribution channel in early 2015, we'll continue to share our views as to reasonable expectations for the future. As always, I want to emphasize that top line growth is not our target. Our target continues to be underwriting profit and resulting return on equity.

We have a defined and consistent operating plan, and are continuing to execute on it. The positive improvement we've demonstrated quarter-over-quarter coupled with managed profitable growth following the strategy laid out when Atlas was initially created is the result. The Atlas team is very excited about the opportunities we're seeing in our niche.

As the only middle market company focused on the specialized segment, we're demonstrating leadership with the objective of maximizing benefit from these opportunities. We'll continue to deliver our strong value promise and believe that we can reach the proportionate 20 percent market share for approximately 400 million in premium with above average underwriting margins as a result. Longer term, we continue to believe that we will be well-positioned to pursue incremental opportunities for horizontal expansion into other specialty areas as we begin to approach proportionate market share in our current niche.

I'd acknowledge the great work delivered by every member of the growing Atlas team. We intend to maintain Global Liberty's New York operations as our east coast regional office, and just as with our Gateway acquisition two years ago, we expect the smooth transition, and look forward to the further expansion of our team.

It's been a great quarter for the company, and I'd like to thank all of our policy holders, agents, and employees. We feel that Atlas is a unique and special organization that has the ability to deliver above-average returns to a laser-focus in specialty areas across all market cycles. The quality of the people with whom we work is critical to that success.

With that, let's open it up for questions.

Operator: Thank you.

At this time, we will be conducting a question-and-answer session. If you would like to ask a question, please press star one on your telephone keypad. The confirmation tone will indicate your line is in the question queue.

You may press star two if you'd like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys.

Our first question is coming from the line of Paul Newsome with Sandler O'Neill. Please proceed with your question.

Mr. Paul Newsome: Thank you. And, congratulations on the quarter, folks.

Mr. Paul Ramano: Thanks, Paul.

Mr. Scott Wollney: Thank you, Paul.

Mr. Paul Newsome: I have a couple of questions, not too heard. The first one is how hard is that 20 percent target for market share within, a state? You know, I know some folks have a view that you don't really want to have a very large market share, because then you start becoming sort of non-competitive.

And--but in New York, your biggest state, you're going to be kind of at that 20 percent. Does that change your appetite within the state when you hit, your underwriting appetite, when you hit the 20 percent, point?

Mr. Scott Wollney: So, I guess the first thing I'd really clarify is that we don't look at the 20 percent as a target so much as we believe that's proportionate. So the way I would phase it is [sp] is that we believe we can grow in virtually every state, if not every state up to the point that we have about 20 percent market share without having a disproportionate share of the market, and I think that's important for the reason that you point out.

You know, we never want to be essentially buying business by being price aggressive. And so, when we talk about the 20 percent, it's really derived from two different approaches. You know, one is looking back across multiple market cycles at the amount of market share that the companies we own, um, have had.

And then the second is anecdotally looking at the level of competition we have in the market. Where in soft markets we tend to be competing with anywhere from two to five different companies for any one account, and so being conservative with five, and we called it 20 percent.

So, I think that's the first thing I'd point out, which I hope kind of responds to the middle part of your question, which is we aren't ever going to grow for the sake of capturing market shares if we're doing it by being price aggressive. So, we always are going to put a priority on underwriting profit margin as opposed to top-line growth.

You know, the point of clarification, you know, with Global Liberty, we expect to be at about 7.5 percent market share, so there will still be considerable opportunity to grow in New York before we reach that 20 percent.

And, you know, I guess finally I would just say in terms of rate of growth, the more market share we have in a given state, like Illinois, for example, where we have about 10 percent market share, you know, the marginal rate of growth as a percentage will generally slow, because, you know, it is generally harder to grow as your market penetration increases. So hopefully that respond to kind of the range of the questions that you asked.

Mr. Paul Newsome: Yep, that's definitely I was looking for.

And my, second question, before letting other folks talk and ask questions, is, I'd like to have a little bit of an update on the outlook, if you could, for the investment, returns. Investment, obviously, not the biggest item in your income statement, but, nevertheless, important.

Mr. Scott Wollney: Yeah.

One of the issues that we're seeing in the third quarter here is the increase in cash on our balance sheet as a result of the, capital raise. So, that's actually, you know, having a negative impact on the overall, yield on the portfolio in the quarter as you annualized the, base. So, at we continue, and as we, put that money to work in terms of the acquisition for Global Liberty, we will see an increase in the yields as we continue into 2015.

You know, we're not picking the market cycles, or we're not picking the market at this point, but, I would suggest that we will see a lift in investment yields as we continue into 2015 and into 2016.

Mr. Paul Newsome: Are you, fully invested as of now, or, does it take you a little bit longer to put the actual cash to use?

Mr. Scott Wollney: No.

So, we--I mean we have about $25 million of cash sitting as cash, pending the Global Liberty transaction, because of the relatively short window between the time that we signed the LOI and the expected close date, other than kind of having it in overnight accounts, which generates obviously a very low yield. It's really sitting there waiting to be used for the acquisition.

If we had not earmarked it for that purpose, you know, we would have been able to invest it. Although as the view as Paul said, you know, we aren't trying to take bets on interest rates, and so we, you know, are not wanting to put a lot of cash in long duration fixed income.

And we do still feel like, the vast majority of our invested assets should be in fixed income with duration matched to our liquidity needs, because of the fact that, you know, we have a very favorable view of the future, in terms of our ability to generate underwriting margin, and so we don’t want to take risks with our portfolio, at the expense of profitable growth in our high ROE, business.

Mr. Paul Newsome: Terrific. Thank you very much.

Mr. Scott Wollney: Thanks for the questions, Paul.

Operator: Thank you.

Our next question is coming from the line of Ryan Burns with Janney Montgomery Scott. Please process with your question.

Mr. Ryan Burns: Good morning, everybody.

Mr. Scott Wollney: Hi, Ryan.

Mr. Ryan Burns: I just had a question, on the, the rate accelerations for commercial auto in third quarter. I just want to see, what kind of market forces were behind that. Again, I just want to clarify, that was for the entire commercial auto, market as well.

Mr. Scott Wollney: Correct.

And so, if you recall in the last call we had indicated that we were actually, you know, not wanting to be prognosticators, but we did anticipate that we might see renewed hardening in commercial auto based primarily on development seen in heavier lines of commercial auto. We think that's what's behind, sort of the pickup in rate.

And really, I think it just comes down to commercial auto writers broadly still needing to increase rate to cover their cost of capital. And a lot of that development seemed to be the tail end of the soft market. And so, you know, I think it's just a function of some of the larger generalists resetting their expectation in terms of how much rate they need to actually, you know, create as opposed to destroy book value. So, I think that creates a general buoyancy.

When you look at rates, across the industry, people who do not specialize in specialty commercial auto niches will often file ISO rates. And those ISO rates generally are heavily biased by the broader commercial auto market more than they are, by precise pricing within specialty niche markets, because they simply don't--you know, the analysis just doesn't get that fine.

And that's one of the competitive advantages we have is that we have actual data from decades of experience in our specific markets. And so while we adopt ISO as starting point, we then file lots of different deviations. And from an underwriting perspective, take into consideration all the detail that we have.

So, um, I think the general, trend is going to be to see continued rate increases. And in our niche, you know, we refer to it as being really hyperelastic to the overall trend. We are still seeing the effect of a lot of the capacity that was brought in through managing general agents in the soft market exiting.

That’s creating opportunity, both in terms of, the number of accounts we’re having an opportunity to quote as well as the price levels that, you know, we’re able to buy in business at.

Mr. Ryan Burns: Okay. Great. Thanks for the color there.

And then quickly just moving to the loss ratio side, in the queue it looked like you guys had a little, you know, reserve releases. So, if I try to back out that, I get you close to, you know, an action year, loss ratio of kind of 63, uh, percent.

And just trying to figure out when we should see kind of leverage from the pricing of better--you guys are pricing to a better than 60 percent, loss ratio, for the past couple of quarters. So, I’m just trying to figure out when we should start seeing little more leverage, on the loss ratio there if it turns out.

Mr. Scott Wollney: Sure, great question.

I mean, Paul had commented that, you know, we aren’t going to take credit for price increase until we see, you know, claims coming in as expected. We are seeing claims coming in as expected, which is why we're, you know, very comfortable that our current case reserves are reflective of future expectation. But, that period is about 12 to 18 months.

Um, so we've commented before that in 2013, we were pricing to about a 60 percent, and then earlier this year, you know, we began pricing to below 60 percent, and so I think the expectation in terms of timing is that, you know, once we get through a 12- to 18-month period following when the business was written in 2013, you'd start to see that portion of the earned premium migrate to, you know, closer to 60 percent number.

You know, that of course is always subject to our regular actuarial reviews and the other processes that the business goes through. But, you know, I think you would want to put a 12- to 18-month window, as the starting point for where we would, in earnest, start really taking credit for pricing activity in prior periods.

Mr. Ryan Burns: I don't think the lost ratio is going to fall off in any one quarter. It's going to gradually coming into play in terms of the loss ratio indications.

Mr. Scott Wollney: Right, because we're not picking a single number, right? We're looking at every intersection of program type and geographic territory, and those loss ratios then roll up on a weighted average basis based on the amount of earned premium for each one of those intersections, and that results in the loss ratio. That ultimately gets carried for a given quarter. So yeah, it is generally going to be a trend.

And obviously the business earns ratably across all the polices written throughout the year, and so will be more gradual. But I think if you're really wanting to kind of model out timing, 12 to 18 months is the starting point for where we really will take the benefit in earnest provided everything is coming in as expected .

Mr. Ryan Burns: Great. No, I appreciate the color, guys. Thanks.

Mr. Scott Wollney: Thank you.

Operator: Thank you.

The next question is coming from the line of Dan Farrell with Sterne Agee. Please proceed with your question.

Mr. Dan Farrell: Thank you and good morning. I just still had a question, on New York. With it getting, a larger piece of your overall book, any differences in loss trend there versus the rest of the book, or any component parts of sort of combined ratio that you'd highlight that might be different? I know you’re still sort of given overall rough targets of where you think you'll trend, but, given that it's become a bigger piece, I'm just curious if there's anything to call out there?

Mr. Scott Wollney: Sure.

I mean, we did see in New York, the New York rate environment firming a little bit later than most of the other areas of the country. I think some of that is just the sheer size of the market place, um, and the fact that there are a number of companies that compete in the space due to that size.

But we are seeing the overall rate environment beginning to improve generally there. And in particular what was attractive to us about Global Liberty is the fact that they have a very focus and specific underwriting process, that ties back to, you know, 25 plus years of experience that the founder of the company has and built into the DNA of the company.

So, we are definitely seeing a healthier rate environment when you can pick your spots as evidenced by the fact that when you roll up all the Global Liberty entities that we're acquiring, their combine ratio is about 90 percent right now, so fairly similarly to ours. We will obviously be able to provide some incremental scale in terms of the overall infrastructure.

Um, and so I think the expectations in terms of accretion from the transaction is that, it should be consistent with our current combined ratio expectations. We do believe that the pricing environment there is beginning to improve. And as such, we do expect to continue to grow that book of business.

And so, you know, we think it's going to be helpful in the short-term, both from a book value and, an income statement standpoint. And then longer term, as we've commented, you know, we really are excited to add that infrastructure to our overall network. And so, look at it is being added to both in the near-term and the long-term.

And as we pointed out, too, there's a very limited amount of transaction-related expense that we expect to see in the fourth--in the first quarters. And then beyond that, you know, it should be, you know, fully positive in terms of the accretion.

Mr. Dan Farrell: Great. That's helpful.

And then just a question, broadly on loss trend [sp]. You know, in the past, you've talked about the difference in loss trend that you're seeing and the light commercial versus, verses the heavier commercial side, or more broader commercial market. Are those differences still holding? Are you seeing loss trends relatively stable?

Mr. Scott Wollney: We are.

You know, we look at that very closely, and we definitely feel like, the underlying loss costs are very stable, and the incremental rate we're getting is definitely marginally more, than the trends in loss costs. In a lot of areas we're actually seeing loss costs from a severity standpoint go down.

And a lot of that we think is because the average age of the vehicles we insure is about 9-years-old. And if you look back at personal auto insurance, you know, 10 years ago, you saw, some pretty significant improvement in terms of severity exposure as a result of the technology being put in the vehicles at the time, things like airbags, better brakes, you k now, collapsing bumpers.

And those sort of technologies, although they're not cutting edge today, are being brought into the fleets that we're insuring. And we believe that that is part of the region why we're seeing, actually some positive trend in terms of underlying loss cost where generally you'd expect that to go the other way because of inflation.

Mr. Dan Farrell: Okay. Very helpful. Thanks a lot.

Mr. Paul Ramano: Great. Thanks for the question.

Mr. Scott Wollney: Thanks, Dan.

Operator: Thank you.

And as a reminder, ladies and gentlemen, to ask a question at this time, please press star one on your telephone keypad. Our next question is coming from the line of Brian Hollenden with Sidoti. Please proceed with your question.

Mr. Brian Hollenden: Good morning, guys, and thanks for taking my call.

Mr. Scott Wollney: Hi, Brian.

Mr. Brian Hollenden: What's your ability and appetite to do acquisitions on the west coast to boost your market share there?

Mr. Scott Wollney: So, you know, we've indicated at this point within the niche we are only interested in acquisitions that would be added to from a structural standpoint, so the West Coast is a large market, where we do not currently have an office. And so we are interested in potentially, either making an acquisition, or building, you know, from the ground up infrastructure on the West Coast.

Right now, we have about 3.5 percent to 4 percent market share in California. but California is obviously a very big state, and there are other larger territories, both right on the coast, and, you know, one or two states in from the coast, where, you know, we would benefit from having local presence. So, it's something we're exploring.

We do not have anything immediately on the horizon in terms of an insurance company target, um, but we are looking at both the insurance companies potentially as well as other avenues to accelerate our ability to create the infrastructure. We'd be wanting longer term on the West Coast. So it's something that we're evaluating, but it's too early to provide any additional color in that regard.

Mr. Brian Hollenden: Okay.

And then one final question. Can you talk a little bit about pricing, on average? What have your, recent year-over-year improvements been like?

Mr. Scott Wollney: So, you know, in terms of rate online, we've been seeing, I would say 7 to 10 percent depending on the geographic territory. But particularly given the amount of new business that we're writing, or recapture business that we're writing, you know, we really try to focus around margin as opposed to great increase, because I think focusing on margin, one, is going to tie more specifically to our return on equity focus, but also, I think is more enlightening in terms of what kind of loss ratio expectation, we should have.

And so, you know, last year we were pricing to a 60. Earlier this year we commented we're pricing to better than 60. For competitive reasons, you know, we are electing not to get more granular than that. But, you know, what I would say generally is that in prior soft markets we've seen pricing develop down into the very low 50s, 51, 52 percent, and in some cases that holds for a number of years.

We aren’t there yet, but we are seeing rate moving in the right direction. And so, you know, that’s probably the most specificity that I'd want to provide. But, we are not seeing anything in our niche that’s making us feel like things are going to slow down in terms of the underwriting margin expectation that we have, nor the rate of growth that we’re seeing, at least through 2015, anyway. You know, beyond that, obviously the market, you know, condition could vary, so we'll keep a close eye on that.

But, I just want to be clear we're--and I think I mentioned this before. We typically feel like 12 to 18 months is kind of the window that weaken with the high degree of confidence to predict, you know, market activity, and we’re obviously looking at that on a real time basis.

Mr. Brian Hollenden: Thanks for the color.

Mr. Scott Wollney: Great. Thanks for the question.

Mr. Paul Ramano: Thank you.

Operator: Thank you.

Our next question is coming from the line of John Leonard with Singular Research. Please proceed with your question.

Mr. John Leonard: Good morning.

Mr. Scott Wollney: Good morning, John.

Mr. Paul Ramano: Good morning, John.

Mr. John Leonard: Regarding the upcoming year-end audit for the allowance against the deferred tax assets, can you provide any guidance as to how much further the allowance, will be reduced? It seems like it would be a meaningful amount given the continued improvement we’ve seen over the past several quarters.

Mr. Scott Wollney: Yeah. Right.

At the end of Q3 we had about $6.7 million of allowance on our balance sheet, which equated to about $0.56 per share at September 30th. So, you know, again we're going to evaluate, all our tax accounts, during the year-end process, and, you know, that could mean up to the $0.56 accretion to book value as a result of a reversal of the, valuation allowance.

Mr. John Leonard: Okay. Great. Thanks.

That's all I have.

Mr. Scott Wollney: Great. Thanks for the question.

Operator: Thank you.

And as a reminder, if you would like to ask a question at this time, please press star one on your telephone keypad. Our next question is coming from the line of Matthew Berry with Lane Five Capital. Please proceed with your question.

Mr. Matthew Berry: Hi, guys.

Mr. Scott Wollney: Hi.

Mr. Matthew Berry: So you, you mentioned in the last couple of quarters, about your, the analysis that led you to believe that, the addressable market had grown by almost 20 percent, and obviously an increase for you guys in, [unintelligible] long run, hopes and expectations for Atlas. Could you--uh, obviously that's a significant increase. Could you, just walk through the analysis that led you to that conclusion, please?

Mr. Scott Wollney: Sure.

So, we work with an outside data analytics firm, every other year to reevaluate market size. They have a proprietary approach that, under confidentiality with us, goes out and looks at a whole range of publicly available information, from census data to other things, department of transportation statistics, etc., to aggregate what we believe to be the vehicle counts within every state in large metropolitan areas for each of the three primary segments we write, the taxi, the livery, and the paratransit, and so that process is a baseline for us.

Um, we then use that to validate our own market research based on our direct interaction and dialogue with agents and industry groups. And so when you look back over the last two years, um, you know, we've indicated that the market size grew about 19.2 percent. Um, about 11 to 12 percent of that growth was the vehicle counts.

And that vehicle count was confirmed through this analysis that I just described. And then the remainder of that is price change, and so it's an increase in the average premium size of, you know, the accounts themselves. And so, those two things together resulted in the 19.2 percent increase in the addressable market size in terms of premium.

Mr. Matthew Berry: And does the, analysis give you any insight into what drives that increase in the vehicle count?

Mr. Scott Wollney: It doesn't directly. We believe, though, that it's a couple of things. The fact that you are seeing increased usage of public automobile, through mobile app, on-demand hailing services, which, you know, there are some companies that everyone's familiar with, and then there's also lots of other smaller mobile hailing apps, some owned by the traditional taxi and livery operators, others developed by third-party software companies.

And we're seeing more and more of those pop up every day. So, I think that's causing more people to utilize the kind of services that our clients provide, and the fact that that allows for owner operators to go off into business themselves more quickly, is being facilitated by that as well.

So, the two things that we're seeing is more demand, more supply demand type pricing, which then increases utilization as well as, the supply because drivers are able to make more in peak demand periods. It encourages them to get out on the road when it's raining on a Friday afternoon, for example, and it encourages more users to actually hail a vehicle on a Sunday/Tuesday because the price might be cheaper.

So, we think that's a big part of it, and some of it is also economics. You know, we've commented before, when the economy tends to weaken, we don't see a lot of our clients' vehicles come off the road because of the underlying costs related to the business, the cost of medallions, for example, or the brand reputation for a livery company.

But when the economy improves, um, and you see unemployment coming down, you know, people do have more money to use to actually take a cab or hail a vehicle, as opposed to, you know, taking the time to ride the bus. So, I think those are the two things together that are resulting primarily in the increase in vehicle counts.

Mr. Matthew Berry: Okay. All right. Thank you very much.

Mr. Scott Wollney: Great. Thanks for the question, Matthew.

Mr. Paul Ramano: Thanks, Matthew.

Operator: Thank you.

Our next question is coming from the line of Adam Patinkin with David Capital. Please proceed with your question.

Mr. Adam Patinkin: Hey, guys. Congratulations on the quarter.

Mr. Scott Wollney: Thanks, Adam. Good morning.

Mr. Paul Ramano: Thank you, Adam.

Mr. Adam Patinkin: Hey, so I just wanted to ask a quick question regarding, ways to kind of accelerate your growth, specifically looking at the balance sheet. Now you guys did an equity raise a couple quarters ago, and I know that you've commented, especially, you know, coast to Global Liberty acquisition, that, you know, the company trades on a pretty low, multiple of 2015 earnings.

So, I assume that, you know, equity would not be an attractive option, or a less attractive option perhaps. And so, I guess I'm curious about, you know, Scott, how you think about potentially using debt as a means to kind of continue accelerating the growth of the business?

Mr. Scott Wollney: Sure.

So, I guess the first point I would make is that we did put in place the quota share program that Paul talked about, and the principal benefit of that is it gives us a great deal of flexibility in terms of when we might choose to raise equity, if we begin approaching, the net written premium to surplus ratio of two times, which we've consistently said is kind of a guardrail.

Um, and so, um, the first part of the response I think is that irrespective of whether we're debt or equity, the quota share gives us the flexibility to not do either. And the cost of capital--the effective cost of capital under that agreement is attractive.

Um, now from a long-term standpoint, you know, we do not look at quota share as a capital structuring tool, but it is a tool that gives us a lot of flexibility in terms of timing. So in terms of evaluating debt versus equity, um, you know, when we raised capital in the second quarter of this year, we chose to use equity principally because at the time we didn't feel our balance sheet, um, you know, we didn’t feel it would be appropriate to add $25 or $30 million of debt on the balance sheet, which is what we were advised would probably be the minimum, debt raise, that would be practical.

At this point, especially with the completion of the Global Liberty deal, we would feel very comfortable potentially adding some debt to the balance sheet. So, you know, I'm not suggesting that we will or won't raise debt or equity, but we certainly, have the ability to consider equity. As I commented we don't have any debt on the balance sheet.

Um, and a lot of it has just come down to the market environment, so the quota share gives us the flexibility to wait for an attractive market environment, and then obviously when evaluating debt versus equity, you know, we would look at the cost of capital, and pursue whatever was the most attractive option, as opposed to feeling like we had limitations the way that we did back when we raised capital last quarter, or, in the second quarter.

Mr. Adam Patinkin: How do you think about the cost of capital of the quota share?

Mr. Scott Wollney: So, from a fundamental basis, you know, with quota share reinsurance you’re basically borrowing somebody else's balance sheet. And so there is a built-in, sort of profit margin expectation, which, you know, for the sake of round numbers, we can say is around 500 basis points. And so, you know, in theory, any time we're writing below a 95 percent combined ratio, it’s accretive to use the quota share.

Um, the reason we don't think of it--so from a cost of capital standpoint, it’s actually extremely cheap, but, the reason we don't think of it as being apart of the permanent capital structure is that, it is portable. I mean, essentially, you know, the reinsurance market today is very competitive.

It seems like it will continue to be competitive for some time, but things can change. You know, we saw a dramatic change in the reinsurance market back in 2002/2003 for example, and so we don't ever want to be in a position where we are relying heavily on quota share as a long-term solution, because you could find yourself in a position where the reinsurance market starts hardening, and the capital markets might not be open. And so we never want to put ourselves in that position.

You know, but again as with the property casualty market, you know, we closely monitor what's going on in the reinsurance environment, and are obviously not going to be using the quota share heavily if we find ourselves in a circumstance where, you know, we think we could find ourselves with kind of a capital crunch. But the current agreement we have is a two-year agreement.

Um, it became effective on, July 1st of this year, and so we know that we have at least that period of time. Uh, and again, you know, at this point, from what we're seeing, the reinsurance markets look like they are softening if anything. And so, you know, it gives us a lot of flexibility.

Mr. Adam Patinkin: Got it. That makes sense.

And again just to confirm, you--the plan, if you did decide to pursue debt to kind of, you know, further accelerate your growth, you'd be able to borrow at the holdco [sp] level and push the capital down into, uh, into statutory capital at your subsidiaries.

Mr. Scott Wollney: Yes, that would be an option.

Mr. Adam Patinkin: Okay. Great. Thanks so much, guys.

Mr. Scott Wollney: Thanks for the questions.

Mr. Paul Ramano: Thanks, Adam.

Operator: Thank you.

We have no additional questions at this time. I would now like to turn the floor back over to Mr. Wollney for any additional concluding comments.

Mr. Scott Wollney: Great. Thank you, Jessie.

And thanks everyone for joining us. Uh, we look forward to speaking with each of you again in the future.

Operator: Thank you.

Ladies and gentlemen, this does conclude today's teleconference. We thank you for your participation, and you may disconnect your lines at this time.