

March 2014 - Market Outlook

PhiloSmith declined 1.3 percent in the first quarter of 2014, behind the 1.8 percent gain of the S&P TR. Our performance was the result of a mixture of gains from roughly half of the holdings offset by declines in the other half.

PhiloSmiths' results in the first quarter of 2014 were impacted by the increased volatility of the overall market. The returns in the quarter were somewhat reminiscent of the market volatility seen during the European sovereign debt crisis/crises; meaning insurance stocks all moving in tandem with little regard to underlying individual company operating performance. Reinsurance company holdings played a meaningful role in performance. The improvement in underwriting results, in addition to being helped by the low level of catastrophes and low inflation exerting downward pressure on loss costs, was driven by the upswing in premium rates. The highest quality reinsurers have been successful maintaining premium volume in the face of pressure from primary companies, Second tier reinsurers have been left with smaller shares of programs at lower rates. In most lines of business, primary premium rate increases are still necessary. Market participants recognize that in a low interest rate environment, underwriting gains are necessary to sustain return on equity. Active capital management strategies, particularly stock buybacks, have increased the ROE of many holdings. In this quarter, stock performance followed the overall market. The market was not discriminating, thereby allowing room for some repositioning. Several stocks with superior performance in 2013 were reduced. Conversely, some positions were added to on weakness.

The Portfolio

At quarter end, specialty property casualty insurers account for 32 percent of PhiloSmith's holdings. The performance of specialty property casualty stocks negatively impacted overall performance. Primary property casualty stocks accounted for 16 percent of the portfolio in the quarter, down from 18 percent in March 2013. Toward the end of 2013, the positions of some of the strongest performing stocks were reduced, which proved beneficial when a couple stumbled in the first quarter.

Outlook and Strategy

The property casualty market is benefitting from the improving economy as well as market upturn. PhiloSmith holds some of the highest quality companies and the real competitive advantages held by these companies will translate into above-average growth and profitability. Underwriting profits continue to be the key to returns. After a strong 2013, the holdings in the portfolio continue to be undervalued relative to intrinsic value. Holdings are generating returns not seen in a few years and companies are actively managing capital, which bodes well for enhanced valuation down the road.

Performance through March, 2014

