Q4 2018 Earnings Call

Company Participants

- Keith McCue, Senior Vice President-Finance & IR
- Kevin J. O'Donnell, President, Chief Executive Officer & Director
- Robert Qutub, Chief Financial Officer & Executive Vice President

Other Participants

- Amit Kumar, Analyst
- Elyse B. Greenspan, Analyst
- Josh D. Shanker, Analyst
- Kai Pan, Analyst
- Ryan J. Tunis, Analyst
- Yaron Kinar, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good morning. My name is Emily and I will be your conference operator today. At this time, I would like to welcome everyone to the RenaissanceRe Fourth Quarter 2018 Financial Results. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. Thank you.

Keith McCue, Senior Vice President for Finance and Investor Relations, please go ahead.

Keith McCue {BIO 20595590 <GO>}

Good morning. Thank you for joining our fourth quarter 2018 financial results conference call. Yesterday, after the market close, we issued our quarterly release. If you didn't receive a copy, please call me at 441-239-4830, and we'll make sure to provide you with one. There will be an audio replay of the call available from about 1:00 PM Eastern Time today through midnight on March 11. The replay can be accessed by dialing 855-859-2056, U.S. toll free, or 1-404-537-3406 internationally. The passcode you will need for both numbers is 5889825.

Today's call is also available through the Investor Information section of www.renre.com, and will be archived on RenaissanceRe's website through midnight on March 11, 2019.

Before we begin, I'm obliged to caution that today's discussion may contain forward-looking statements and actual results may differ materially from those discussed.

Additional information regarding the factors shaping these outcomes can be found in RenaissanceRe's SEC filings to which we direct you.

With us today to discuss our results are Kevin O'Donnell, President and Chief Executive Officer; and Bob Qutub, Executive Vice President and Chief Financial Officer.

I'd now like to turn the call over to Kevin. Kevin?

Kevin J. O'Donnell

Thanks, Keith, and good morning and thank you for joining today's call.

Looking back each year, I think it's only fair that shareholders hold us accountable for the answer to two questions; first, are we satisfied with our financial performance; and second, have we achieved the goals that we set forth for ourselves at the beginning of the year and furthered our strategy?

In response to the first question, 2018 was a year with greater than $80 billion of insured natural catastrophe losses, including the most significant typhoon to impact Japan in decades, record-breaking California wildfires, two land-falling U.S. hurricanes and numerous other events around the world. In addition, there were numerous large individual risk losses and some significant losses of note within the Casualty and Specialty market.

Against this backdrop, we grew both our book value per share by 4% and our tangible book value per share plus change in accumulated dividends by 6.4%. For the year, our return on equity was 4.7% and our operating return on equity was 8.8% and we reported an operating profit for every quarter of 2018.

Bob will discuss our quarterly results in more detail later, but relative to the loss activity I believe we've performed well. We had many other financial successes in 2018.

To begin with, in the fourth quarter, we issued $250 million of our common shares to State Farm, making them our fifth largest shareholder. Earlier in the year, we lowered our cost of capital by raising $250 million in a low interest rate environment through the issuance of Series F preference shares, paying a dividend of 5.75%. And finally, in our joint ventures business, we raised over $1 billion between our existing vehicle, Upsilon Re, and latest vehicle Vermeer Re. Together, these actions not only demonstrate our ability to raise the most efficient and effective capital from multiple sources, but also provide us considerable liquidity and financial flexibility heading into 2019.

At the same time, our operational and capital leverage continues to improve. Over the last five years, we have more than doubled our gross premiums written, while growing shareholders' equity by 30% and keeping the sum of operational and corporate expenses flat.

We have achieved this by working diligently to increase operating efficiency of our business and execute strongly against our strategy to write more profitable business on existing platforms, and also by forming new ones such as Vermeer Re. We expect that our operational and capital leverage will continue to improve moving forward, as bringing in the Tokio Millennium Re portfolio will allow us to continue to leverage our platforms. So, in answer to the first question, I believe that for a year with so many industry hurdles since 2018, we are pleased with our financial performance and the returns we have generated.

On the second question, have we achieved our goals for the year and furthered our strategy, we rigorously develop and review the strategy with clearly defined direction and goals. Every year we review this, evolve it as necessary according to external and internal forcing factors and develop our annual execution targets and tactics that will keep us focused.

In 2018, I believe we executed well and advanced our strategy. We launched a new joint venture vehicle, Vermeer Re, with a strong long-term partner. The formation of this vehicle is significant in several ways. First, it received an A. M. Best rating of A, which is rare for a new carrier; second, a $1 billion capital commitment from a single investor is one of the largest third-party equity commitments ever in the ILS sector; and third, a rated vehicle focused on risk remote and therefore capital intensive end of the market is a unique and powerful capability for RenRe and further enhances our integrated system and ability to match the right risk with the right capital.

One of the main highlights for 2018 was the announcement in the third quarter of our acquisition of Tokio Millennium Re, which I will refer to as TMR. Since then, we have continued to devote significant resources to the TMR transaction. We established an integration management office and are making significant progress on integration planning. As discussed at the time of the announcement, this transaction is both financially and strategically attractive. It increases our access to risk, allows us to scale our platforms with attractive business with minimal dilution to shareholders and should lead to continued improvement in our operating and capital leverage.

Equally important in 2018 was the continued execution of our strategy to profitably grow our business. Bob, will give you a breakdown on the numbers in a minute, but we wrote more than $3 billion in gross premiums at a combined ratio of 88%. This growth was both robust and broad-based, coming from both our segments and all of our major classes of business.

The fourth quarter of 2018 was yet another opportunity to demonstrate to our clients the value of our products and the services we provide by rapidly paying their valid claims. In fact, over the past two years, we've paid almost $2.8 billion in gross claims to our customers. Our value-add to our customers goes beyond simply paying claims, however. We continue to invest in our capabilities and share our knowledge and intellectual insights with our clients and partners through subsidiaries like WeatherPredict. We can help our clients better understand and assess their risk. This benefits us as we are more likely to be first call for new business, especially on the many large, bespoke deals we've been able to exclusively source over the past several years.

In 2018, in addition to the TMR transaction, we also furthered a number of other strategic and tactical projects. As we always do, we sharpened our underwriting toolkit while advancing several initiatives to improve underwriting and operational efficiency. We also continue to develop our bench strength. We've always said that people are our greatest assets and we never hesitate to spend money to improve our already deep reserve of human capital.

So in conclusion, 2018 was an extremely strong year when viewing our performance against our strategic objectives. With all of this as background to our 2018 results, I'll now spend a couple of minutes on high-level comments regarding the broader market.

As December progressed, there was a fair amount of skepticism around the collateralized market and its ability to reload for property renewals. I think that some in the market were once again hoping for a dislocated renewal and similar to last year, were disappointed when it did not materialize. We have seen many market cycles over the last 25 years and have consistently adjusted our tactics accordingly as we did in 2018. As I've said before, price should not be the sole determinant of a successful renewal. So while we remain focused on the quantum of individual price changes, we are committed to building attractive portfolios.

While price is important, being successful in the reinsurance market takes much more than simply charging more. It requires having the right capital in the right structure, at the right time. We brought significant capital, both owned and managed, to assist customers and structured our portfolios to maximize return. A meaningful component of that optimization on our rated balance sheets was the careful execution of our gross to net strategy, including the structuring of our seated protections.

As you saw once again this quarter, our results benefited materially from this approach. As long as capital continues to show interest in the Property Cat business, we will find ways to harness it in the service of our customers as we did to a very large degree in 2018, enhance the returns of our rated balance sheets on a trading basis. Our proprietary underwriting tools and expertise allow us to generate updated risk curves daily. This provides us unique speed and flexibility in assuming and ceding risk, as we possess a deep understanding of how each decision affects expected returns and required capital.

These tools allow us to better understand the shape of the tail of our risk distributions and consequently focus on the points where capital usage is most sensitive. For the first time in many years, however, in 2019, I anticipate that third-party capital will play a smaller role in protecting our customers' risk. This contraction is the result of the increased loss frequency and severity affecting the business. While we believe that third-party capital is an important component of our business, the structures that deliver this capital should be scrutinized in a more fulsome way.

I believe that the capital needs to be intermediated by strong underwriting and we are increasingly seeing more sophisticated diligence being conducted by investors in order to assess the underwriting expertise of their managers. This is a natural next step in the maturation of this market. Ultimately, I see the market migrating to a hybrid model of rated and collateralized capacity that we pioneered with our integrated system.

I'll provide more details on the opportunities we're seeing in 2019 later in the call, but first I'll turn the call over to Bob, for a look at the TMR integration and our financials.

Robert Qutub {BIO 15269353 <GO>}

Thanks Kevin, and good morning everyone. Against the backdrop of widespread industry catastrophe losses and volatile financial markets, I believe we performed well in the fourth quarter and for the full year. Today I'd like to highlight a few of our key financial results, but first I would like to update you on the TMR transaction, the progress we are making, and finally, I'll turn it back over to Kevin.

Starting with the TMR transaction, the preparation for the integration has been a significant focus for us. As Kevin discussed, we have established an integration management office that is administering a number of work streams, each of which is progressing well. As you would expect, we are primarily focused on preparing for what we call day one, which concentrates on those work streams essential to ensuring that business continues uninterrupted immediately after closing. We have also identified the final targets date for the combined companies, along with detailed plans for achieving it.

When we first announced the TMR transaction, we anticipated it will close sometime in the first half of this year, subject to regulatory approval. While we do not dictate the timeline of this progress, we remain optimistic regarding the first half close. Until closing, we continue to operate as separate companies and are confident in our estimated target of between $700 million and $1 billion of acceptable gross written premiums on the TMR business, resulting in a $100 million run rate.

As I discussed last quarter, we project that significant synergies will be achieved with TMR. These synergies will be actioned in the first 12 months and realized over the first two years, and once realized, should allow us to continue to improve our operating leverage from where it stood prior to the TMR acquisition.

As we discussed, the financing of the TMR acquisition has several facets, which increase our financial flexibility going forward. First, we continue to anticipate that TMR will pay a pre-closing dividend of at least $250 million. Second, $250 million worth of RenRe shares will be issued to Tokio Marine at closing. In addition, as Kevin mentioned, State Farm recently closed its purchase of our shares. While not explicitly linked to our purchase of TMR, their investment also provides us increased liquidity and flexibility in 2019.

And I should note that after we close the TMR transaction, comparisons to our financial results in 2018 will become difficult. For this reason, we will not be giving forward projections on this call, but we'll update you further next quarter.

Now, moving on to consolidated results and beginning with the fourth quarter, our annualized return on average common equity was negative 7.8%. From an operating perspective, however, we posted positive annualized operating return on average common equity of 0.1%. We reported a net loss for the quarter of $84 million or $2.10 per diluted common share. On an operating basis, however, our operating income was positive at $1.2 million or $0.02 per diluted common share, which excludes $89 million of realized and unrealized losses on investments. These investment losses were primarily from our strategic equity positions as well as our passive equity portfolio, which comprises 2.6% of our investment portfolio. We had underwriting losses for the quarter of $82 million and reported an overall combined ratio of 114%.

Now, moving on to the full year of 2018, we grew our book value per share 4.4% and realized a return on average common equity of 4.7%. From an operating perspective, our operating return on average common equity was 8.8% and our tangible book value per share plus accumulated dividends grew by 6.4%. We reported annual net income of $197 million or $4.91 per diluted common share and operating income of $366 million or $9.17 per diluted common share. Finally, for the year, we had an overall combined ratio of 88%.

Now, before moving on to our segments, I wanted to update you on our operational efficiency. Our direct expenses, which are the sum of our operational and corporate expenses, totaled $71 million for the quarter, which is up from $33 million in the same quarter last year. $30 million of this increase was in operational expenses, which is from increased compensation costs driven by our continued investment in the business and a larger bonus accrual for 2018 versus a decrease in the bonus accrual in the same quarter last year. And $8 million of the increase was in corporate expenses, which was driven by a number of factors, including an increase in compensation costs, transaction costs related to the TMR acquisition and fees related to a new credit facility.

For the year, our direct expenses totaled $212 million, which, as a ratio of net premiums earned, was only a slight uptick compared to 2017. As I previously discussed, direct expenses have been increasing as we invest in the business and we'll continue to do so as we integrate TMR. However, backing out the impact of the TMR integration, the ratio of direct expense to net premiums earned should continue to improve over time, as we expect to leverage our expense base as we grow our net premiums earned.

And now, moving on to our segments and starting with the Property segment, where gross premiums written in the fourth quarter grew by $105 million over the comparative quarter to $200 million. This growth was driven by $103 million of reinstatement premiums. In total, our Property segment incurred an underwriting loss of $35 million and a combined ratio of 111% in the fourth quarter. The net negative impact to RenaissanceRe common shareholders due to Q4, 2018 Catastrophe Events, including the change in 2018 Aggregate Losses, was $104 million, which was offset by $69 million of favorable development on the Q3, 2018 Catastrophe Events and the 2017 Large Loss Events for a total net negative impact to RenaissanceRe common shareholders of $35 million for the quarter.

We have previously announced an estimated $100 million net negative impact from Hurricane Michael. Due to the impact of Q4, 2018 Catastrophe Events on retrocessional recoveries, we have reduced this number to $72 million. For the year, gross premiums written in our Property segment grew by $320 million or 22%, with $95 million of reinstatement premiums. This broke down to a growth of $245 million or 22% in our property catastrophe class of business, and $76 million or 23% in our other property class of business.

For the full year, our Property segment reported underwriting income of $262 million, and a combined ratio of 75%. Our reinsurance recoverable increased $786 million or 50% from the prior year. This is mostly due to the 2018 Catastrophe Events. We remain very comfortable with the credit quality of these recoverables, as they are predominantly either collateralized or with long-term partners.

There was some movement in our acquisition expenses for both the quarter and for the year. As a net percentage of premiums earned, acquisition expenses were down 2.5 percentage points to 15% for the quarter. For the year, however, acquisition expenses increased to 17% from 12% in 2017. The downward movement in the quarter was largely due to the increase in reinstatement premiums, which typically carry lower brokerage. The increase for the year, however, was due to decreased profit commissions in the third quarter of 2017, which as you recall offset acquisition cost.

Now, moving on to our Casualty segment, our gross premiums written were up $35 million or 11% for the fourth quarter of 2018 over the over the comparative quarter. For the year, gross premiums written were up $192 million or 14%. The top-line growth does not adequately quantify the amount of change in our casualty book. Due to our preferential access to business and the proprietary underwriting tools we have developed over the last several years, we are uniquely positioned to increase on the best business and decrease on the worst.

Consequently, while gross premiums written were up $35 million over the comparable quarter, we wrote $102 million of gross premiums that were either new deals or growth on existing deals. At the same time, we non-renewed or reduced $59 million premiums on deals that did not meet our return hurdles. We're always shaping the portfolio to maximize efficiency and return, and small net changes sometimes mask large underlying shifts.

The Casualty segment printed an underwriting loss of $47 million and a combined ratio of 119% for the quarter, and an underwriting loss of $17 million and a combined ratio of 102% for the year. The results in our casualty book were impacted by losses related to the California Wildfire liability covers we wrote in the second and third quarters. Kevin will provide additional insight on these deals, but our estimate of the potential for losses has been covered in our casualty reserves. If you back out the impact of the California Wildfire liability deals, our Casualty segment would have been profitable for both the quarter and the year.

Similarly, if you adjust for the impact of the Wildfire liability losses, our casualty book continues to run a current accident loss ratio of around mid-60s, which is consistent with recent performance and in line with our expectations.

Now turning to investments and for the year net investment income was $262 million. Due to market volatility, we experienced mark-to-market losses for the full year of $175 million, resulting in total investment results of $87 million.

For the quarter, return on our fixed maturity and short-term investments was $71 million for the quarter. Net investment income however was $53 million and was negatively impacted by losses on our private equity investments of $12 million, and losses on our Medici Cat bond of $5 million. We posted total investment losses of $35 million for the quarter, due to mark-to-market losses of $89 million.

For the quarter, we grew our overall investment portfolio by more than $340 million from the prior quarter and $2.4 billion from the prior year.

Now moving on to cover a couple of topics we'd previously discussed in our ongoing efforts to provide you with enhanced insight into how our joint ventures impact results for shareholders, whereas last quarter we included a new breakout of our fee income in our financial supplement. As part of this effort, we are providing additional disclosures beginning this quarter, to provide further transparency into our company.

You will see that we have revised page 8 of the Financial Supplement to include a breakout of our fixed maturity and short-term investments held in the retained investment portfolio, from those held in our overall managed investment portfolio. The purpose of this breakout is to reflect the portion of the fixed maturity and short-term investments that impact our bottom line. And while there are other consolidated assets from these entities, we felt these had a direct impact on some of our key performance metrics. The retained portfolio differs from the managed portfolio and that excludes a portion, or in some cases, all of the investments held in our joint ventures, as the returns on those assets do not impact RenRe's bottom line.

As we have discussed, several of our joint ventures are fully consolidated because of our control over the entities. However, we only hold a minority interest that is reflected by the non-controlling interest adjustment. Many of these entities have separate investment guidelines requiring highly rated, shorter duration investments that are consequently lower yielding than would be optimal under RenRe Holdings' investment guidelines. The retained portfolio adjusts for the effect of these investments which does not impact our bottom line. The difference in these assets at year-end 2018 is about $3 billion and this has started to distort the yield and duration.

For example, whereas our managed portfolio reported yield to maturity of 3.2% for the quarter, the yield to maturity on our retained portfolio was higher at 3.4%. And similarly, the duration of the fixed maturity and short-term investments in our managed portfolio was down at 2.1 years, whereas the duration of our retained portfolio was 2.3 years and we expect that to lengthen over the next 12 months.

In addition to these enhanced disclosures, beginning in the first quarter of 2019, we will be refining our methodology for calculating our operating results to remove the realized and unrealized gains and losses related to the non-controlling interests from DaVinci and Vermeer.

Now moving on to capital management, we did not purchase any shares in either the quarter or the year. This is consistent with our strategy of deploying capital into the business first and we believe it is the best use of shareholders' money.

And finally, ending with fee income, total fee income was $8.6 million for the quarter. Our fee income for the quarter was down compared to the comparable quarter due to loss performance fees driven by the Q4 2018 Catastrophe Events. For the year, we booked $90 million of total fee income, which is up 38% over 2017.

With that, I'll turn it back over to Kevin for more details on our segments.

Kevin J. O'Donnell

Thanks, Bob.

I'll divide my comments between our Property segments and our Casualty and Specialty segment, starting with the discussion of the 2018 results and then moving on to the January 1 renewal and opportunities in 2019. Then I'll take any questions.

For the full year in 2018, we grew gross written premiums in our Property segment by 22%. As Bob explained, this growth came from increases in top-line premium in both Property Cat and other property, as well as reinstatement premiums, resulting from the year's Catastrophe Events.

We experienced a number of large natural catastrophes in the quarter, primarily in the U.S. Hurricane Michael made landfall at Mexico Beach on the Florida Panhandle, as a very strong Category 4 hurricane with 155-mile-an-hour winds at landfall. Hurricane Michael was the most intense U.S. hurricane since Hurricane Camille in 1969, based on central pressure and the strongest by winds speeds since Hurricane Andrew of 1992, and industry loss estimates are around $10 billion for the storm at this time.

California once again experienced wildfires in Q4. The Camp and Woolsey Fires were the most significant, with the campfire being the deadliest in California history, as well as the most destructive in terms of both acres and structures destroyed. We expect that the combined insured cost from these fires will ultimately exceed $15 billion.

As Bob discussed, two casualty deals that we wrote in 2018 added materially to the underwriting loss for the wildfires. I spoke about these deals on prior calls. They were the result of our decision to pivot our net participation in this market to write more wildfire liability coverage. Our decision was driven by the more favorable risk-adjusted returns these deals offered, versus traditional Property Cat deals in the California market.

The California Wildfire liability market is small, but experienced substantial dislocation following 2017, so expanded our participation on these programs. As you can see from the quarter's results in our Casualty segment, we have reserved substantial losses to these programs. Due to the nature of the liability business, it will take many years to determine if these losses will materialize, but we decided that it would be prudent to recognize their potential now. Absent the wildfires, our Casualty segment would have been profitable. I would like to spend a minute to explain how we thought about these wildfire liability deals when we wrote them.

While in hindsight we lost money, I remain convinced that our decision to participate in this market was nonetheless a correct one. First, we determined that risk returns were superior on the casualty deals and that our risk capital was best placed against this exposure. We view our clients as partners however, and we prioritize providing consistent capacity to them and subsequently managing our net risk.

Consequently, we wrote the casualty deals and through application of our gross to net strategy, we optimized our exposure to California overall by reducing the risk that we took on the Property side, to retrocessional purchases. Our decision to enter the California casualty market was well modeled, thoughtful from a portfolio construction perspective and therefore appropriate. The loss experience does not nullify a good process and a correct decision.

The industry has experienced ongoing adverse development on the 2017 Catastrophe Events, most notably, Hurricane Irma. By itself, the industry's 2018 adverse development on Hurricane Irma would be one of the largest events this year. Thankfully, we had favorable development overall on the 2017 events, which is a testament to our years of experience in superior loss estimation processes.

That said, I think even we have been surprised by the persistence of adverse development in Florida. A number of factors have contributed to continuing 2017 loss creep and none of them augur well for the future health of the Florida market. This is especially true for the worrying trend around loss adjustment expenses, especially the aspects that are within the control of insurance companies.

After three years of losses, hopefully the market will finally recognize that not all insurance companies have performed equally well and that when underwriting Florida risk requires more than just generating a model loss estimate.

We once again recognize the benefits of our gross to net strategy through 2018. Gross to net is much more than simply buying reinsurance protection and encompasses the various balance sheets and vehicles that we manage. That said, we are significant buyers of retrocessional coverage and saw the value of this cover in relation to the Catastrophe Events of 2018. Vermeer Re augmented our gross to net strategy at the January 1 renewal, providing us with additional flexibility to see desirable risk to efficient capital at a time that retro markets have diminished capacity.

The January 1 renewal occurred late this year, but in my estimation it was successful. Some reports on the market paint the picture that reinsurance rates were flat to down, but that is taking too broad brush an approach and not in line with our experience. Certain property reinsurance and retrocessional lines of business experienced hardening, particularly, were impacted by losses in 2018.

The California Wildfires seem to be the straw that broke the camel's back, especially for third party capital. We saw the largest price increases in Property Cat retro, which has been predominantly supplied by third-party capital in recent years, with 15% to 30% risk-adjusted increases year-over-year. We saw increased demand for reinsurance at the renewal and anticipate that this trend will continue as the year progresses.

There currently is a disconnect between retrocessional and primary reinsurance pricing. At January 1, the U.S. loss-impacted primary Property Cat reinsurance market was up, on average, around 10%. U.S. non-loss impacted business was flat to up 5% and European business, which wasn't loss impacted and has generally performed well for the past few years, was down a few points.

In general, the January 1 renewal was consistent with our expectations, which on the surface may appear disappointing. However, we currently expect to see larger rate increases throughout the year on loss-impacted deals and regions, specifically, the April 1 Japanese renewal post-Typhoon Jebi losses, the June 1 Florida renewal following three consecutive years of hurricane losses, and the deals that were impacted by California Wildfires, which renewed before these losses occurred. The other property class of business also experienced flat to up 10% pricing at January 1.

Generally, we have been renewing our expiring lines, but also had a couple of large one-off private opportunities with long-term partners. I believe the market is moving once again and, in particular, retro is becoming more adequately priced. Seeing these changes early and structuring portfolios accordingly is what we do.

The game plan for 2019 will be different from 2018. But our experience, access and expertise in underwriting gives me the confidence in our abilities to maintain (00:34:20) the risk-adjusted returns of our portfolio. Going into wind season, I anticipate that the expected return on our portfolio will be roughly similar to last year. But anticipate that the shape is skewed such that no-loss return will be higher and since we're being paid better, we will accept that our tails may be a little larger.

For the year, we grew gross written premiums in our Casualty and Specialty segment by 14%. This growth was broad based and came across all major classes of business. The casualty market was relatively stable at the January 1 renewal and our in-force portfolio is essentially flat. We did not see significant improvements in terms and conditions except on some troubled accounts.

That said, ceding commissions have held flat for a while now and where we saw improvements, it was in response to underlying performance of client portfolios.

Underlying original rates continue to improve. And for the most part, rate changes are at least keeping pace with loss trend.

Obviously, there are several subclasses to monitor within our casualty portfolio, but this comment holds true at a high level. The impact of the California Wildfires on liability business, however, may create opportunities in the Casualty business going forward.

This renewal, we found that global clients continued to desire broad relationships with their reinsurers. And our ability to assume casualty risk increased our access to property risk. The robust tools we have developed in the Casualty business have allowed us greater confidence in providing multi-line coverage to our global clients, which has been an important component of our overall strategy, including Property.

Even for core clients, however, we remain disciplined and grew on the best and shrank on the worst. Our Specialty business, on the other hand, experienced strong growth at 1/1 in a number of areas. Specialty includes a number of sub-classes, but in financial lines, for instance, we introduced several new products on the mortgage side that highlighted both our first-mover advantage and ability to execute quickly.

We also continued to leverage our growing market position in political risk in order to gain bigger shares on key placements. Similar to our Property segment, we continue to execute our gross-to-net strategy in Casualty and Specialty, with ceded purchase remaining fairly consistent during the quarter and for the full year. We continue to cede approximately one-third of premiums in this segment.

With another quarter marked by significant loss activity to the industry, we also experienced significant volatility in both debt and equity markets. Against this backdrop, however, I believe that we had a strong quarter and year. We're also making good progress in preparing for the TMR integration. As always, we remain resolutely focused on executing our strategy and maximizing shareholder value, and are optimistic about the opportunities ahead for us in 2019.

Thank you. And with that, I'll turn it over to questions.

Q&A

Operator

And our first question comes from the line of Josh Shanker from Deutsche Bank. Your line is open.

Q - Josh D. Shanker {BIO 5292022 <GO>}

Yeah. Good morning, everybody. I bet there's going to be a lot of California Wildfire liability questions, but I'm not going to ask those. I'd rather talk about the TMR transaction a little bit. You've had about three months since the last time you talked to us about it. What's your internal assessment on how much excess capital there is going to be generated by the combination of your two businesses? And how do you come to that? Is that a conversation with the rating agencies? And second, in terms of your conversations with the Swiss regulators, what is your confidence that you might be able to pull that capital out and over what timeframe?

A - Robert Qutub {BIO 15269353 <GO>}

Hi, Josh. Good morning. Let me see if I can kick this off. In terms of getting approval for the dividend, that's really TMR and working with FINMA, which is the regulators in Switzerland, and I've pointed out we're confident on $250 million, and hopefully we're going to get more, but that's what we're working on right now. The dialogue with them has been very, very good. So then the question is how much is existing in there that's excess capital? It's somewhere north of $250 million, hopefully, more that we can get out of there.

Going forward, the amount of capital will be dependent on a couple of different factors: one, what we renew on; and again then, also that's the $700 million to $1 billion. It's also going to be a factor of now we'll be able to consider the adverse development cover on that book. So, that'll help us on some capital, and then the ongoing performance of the business. So, there's a number of different factors. But I would sum it up as we feel very good. We've gotten a lot more insight into the process and the dialogue with us and the regulators in FINMA, as well as the rest around the world, the others has been very positive.

Q - Josh D. Shanker {BIO 5292022 <GO>}

And do you have a timeline to - will you know more before the close or are you going to - will be a discussion in progress over the next year or two, I guess?

A - Robert Qutub {BIO 15269353 <GO>}

No, we anticipate to have the dividend coming out that we've been talking about prior to our closing.

Q - Josh D. Shanker {BIO 5292022 <GO>}

Okay. Thank you very much.

Operator

Our next question comes from the line of Elyse Greenspan from Wells Fargo. Your line is open.

Q - Elyse B. Greenspan {BIO 17263315 <GO>}

Hi. Yes. Good morning. My first question, you know Kevin, throughout your remarks you referenced pricing getting better. You also pointed to some alternative capital being tied up at 1/1 and not necessarily seeing as much of this collateralized capacity throughout the year. What gives you conviction I guess that we won't see capital come back in in advance of April 1 and then the mid-years in Florida, just as we hear chatter about prices being better for those two renewals?

A - Kevin J. O'Donnell

So, thanks. I think the – from my perspective, we believe capital allocated from the ILS market to the reinsurance market will be down in 2019 compared to 2018. Part of that is – is based on the fact of how much is tied up and how much has been lost. What I would say though is – is regardless of what happens with third-party capital going into the renewals that I mentioned in my price expectations, we're in a preferred position to most, to access that business and also to manage the third-party capital as it comes in.

I believe going forward, the market is going to continue to consolidate with the highest quality managers of which we are certainly one, and I think the formation of Vermeer Re in the fourth quarter points to success in that management.

So I think we – from the Florida renewal, which is where a lot of this capacity is targeted, we will be in a preferred position whether there is increased ILS interest or not and the retro market, frankly, is really largely a one-to-one market, and we did see a diminished participation in that by ILS capacity and we were able to take advantage of that.

Q - Elyse B. Greenspan {BIO 17263315 <GO>}

Okay. And then my subsequent question, so you just said diminished ILS capacity within retro, so it sounds like you guys wrote more retro and then also it seems like you're purchasing as much as you purchased last year. So, is that correct in meaning that rates went up but you both wrote more and then also were able to – did choose to purchase more just at higher rates or the same, I'm sorry.

A - Kevin J. O'Donnell

Sure. So I'll divide it between our inwards and our outwards. With our inwards book, we did write more retro at one-to-one both on our owned balance sheets and then with some of our third-party partners. With regard to our purchasing, we have significant relationships that are long-term and those are already in place for 2019. Secondly, we have purchases that are mid-year and we'll make determinations frankly based on price and the overall impact on our portfolios, whether we're going to use those or other structures when it comes to structuring the portfolios at mid-year.

So, we're not tied to renewing the mid-year retro that we have. We can either put it into the ceded structures we have or retain it or put it on to other vehicles that we can either form or have.

Q - Elyse B. Greenspan {BIO 17263315 <GO>}

Okay. Thank you very much. I appreciate the color.

A - Kevin J. O'Donnell

Sure.

Operator

Our next question comes from the line of Amit Kumar from Buckingham Research. Your line is open.

Q - Amit Kumar {BIO 15025799 <GO>}

Thanks and good morning, and congrats on the print. Two questions if I may. The first question I guess goes back to Elyse's question on the pricing. I was trying to look back at the transcripts for the 6/1 call, and then compared it to the last Q1 - I'm sorry Q4 call, I just want to be very clear here, is that outlook for 6/1, is that similar to what we have seen at the one-month renewal i.e., are we expecting mid-teens or better pricing based on the losses over the past three years? Or does it sort of just go down a bit from these levels?

A - Kevin J. O'Donnell

So - now let me just explain what I think is happening in Florida. There's kind of two cycles I think of in Florida. There's a behavior cycle, and then there's a profitability cycle. From a profitability standpoint, Florida has not been a good bet over the last couple of years because of the loss activity, and I think there's a growing sense of frustration with the behavioral market in Florida.

I think the structures that are being placed are not as precise as they need to be. The loss adjustment expense flowing through to reinsurers is at significantly elevated levels, more elevated than what we've historically seen, and there's been the AOB issues and other issues. So with that, I think there is a sense of frustration with reinsurers who are protecting in that market from both a pricing and the behavioral side which will driver a increase in required return and a reduction in supply if it's not materialized. So I'm more optimistic about the Florida renewal than it was last year.

Q - Amit Kumar {BIO 15025799 <GO>}

Okay. That's a fair point. The only second question I have is going back to the discussion on TMR. If you go back to the PowerPoint at that time, we had started with a $700 million number. I think the $1 billion was more aspirational at that time. The earnings on rate of $100 million I think was based more on the $700 million number. I'm curious - am I overthinking, but it seems to mean, now that we have changed that number to a definitive range of $700 million to $1 billion, is there upside to that $100 million number or is there something else going on?

A - Robert Qutub {BIO 15269353 <GO>}

Thanks for the question and clarification. We have kept the range at $700 million to $1 billion as you're correct. You know, the $100 million was what we thought would be our target, sure there's upside to it, it depends on a number of different factors, the performance of the investment portfolio will definitely be a key contributor to it. The timing of the synergies will help the profitability and I gave you a timeframe on that which is now more definitive than the last update and then also the profitability of the book; you know, the $700 million to $1 billion, we have that optionality on improving on the best. So, there very well could be upside to it, Amit.

Q - Amit Kumar {BIO 15025799 <GO>}

Got it. I'll stop here. Thanks for the answers and good luck for the future.

A - Kevin J. O'Donnell

Thanks.

Operator

Our next question comes from the line of Yaron Kinar from Goldman Sachs. Your line is open.

Q - Yaron Kinar {BIO 17146197 <GO>}

Good morning, everybody. So, listening to your comments earlier in the call, it sounds like Florida may still – will not be the most attractive market for you. Is that a market that you'd expect to shrink in 2019? And if so, where do you see the greater geographical opportunities?

A - Kevin J. O'Donnell

You broke up a little bit. I think – did you say the Florida market?

Q - Yaron Kinar {BIO 17146197 <GO>}

Yes. I was just asking if the Florida geography is one that you'd expect to shrink in this coming year and if so, are there other geographies that still present a better opportunity?

A - Kevin J. O'Donnell

So, I think if you go back in our history, there have been periods of time where Florida was a significant portion of our gross written premium. Florida currently represent about 5% of our premium, which is a representation of the fact that we believe the profitability and the excess return that was available historically is no longer available. So I think we have upside in rate change in Florida and if rates do not improve, terms do not improve, I would expect that that 5% will reduce.

Q - Yaron Kinar {BIO 17146197 <GO>}

Okay. And in terms of other geographies?

A - Kevin J. O'Donnell

So, I think what we've – so Florida is going to be a unique market and you know I think we all know some of the – some of the reasons for that. I would say that the restructuring of the way in which we are thinking about taking risk holistically is the – is the new Florida geography. The fact that we are looking to broadly protect across Casualty and Property and which provides us unique access particularly for bespoke deals is where we're getting a significant output to the market. So I feel it's not switching Florida to a different geography, that's replacing it. It's looking at how we're structuring our capital and then how we're positioning with our core clients to make sure that we have access to them and the most desirable covers is really the way that we're thinking about building the portfolios currently.

Q - Yaron Kinar {BIO 17146197 <GO>}

Okay. Got it. Great. My follow-up would be, thoughts on being in aggregate covers as opposed to prevent – or is there more appetite to get deeper into ag areas or ag covers?

A - Kevin J. O'Donnell

So aggregate covers are enormously valuable for buyers. With that we're much more likely to sell aggregate covers to the companies in which we have the broadest and deepest relationships, so I think we have a very strong ability to understand aggregates, I think there has been some pressure on aggregate pricing, particularly from ILS Capital and I think we generally have put in a more fulsome loss assessment, particularly from non-critical Cat elements that can contribute to that. So, I feel like we're in a pretty good spot to continue to sell those, but we will target our sale of those to our biggest and strongest relationships.

Q - Yaron Kinar {BIO 17146197 <GO>}

Got it. Thank you very much, and great quarter.

A - Kevin J. O'Donnell

Thanks. Appreciate it.

A - Robert Qutub {BIO 15269353 <GO>}

Thanks.

Operator

Our next question comes from the line of Ryan Tunis from Autonomous Research. Your line is open.

Q - Ryan J. Tunis {BIO 16502263 <GO>}

Hey. Thanks. Good morning. My first question is on I guess in regard to the fee disclosure which was helpful, Bob, thanks, but I had three questions on it. The first was, because this seems like a pretty significant area of earnings growth, but management fee income went from $50 million to $71 million last year. I guess based on everything you did on Jan 1, is there any visibility on how we could see the management fee number growing next year?

And then my other question was performance fees didn't really grow a lot, but I'm not sure if that's because of performance, so just trying to get a feel for like what that number would look like if you didn't have losses last year. And then lastly, how do we think about margins on that fee – on that fee income? Thanks.

A - Robert Qutub {BIO 15269353 <GO>}

Hi. Those are good questions. Thanks, Ryan. I hope you're doing well. On the management fee decline, those tend to be more stable. There is a little bit of unique volatility in it. You can see it more pronounced in Q3 to Q4. As a result of – one of our joint ventures was down about $6 million. That's really timing. That's timing and rounding effect, but in that quarter we reduced it, but then we recaptured it back over time, similar to what we did last year with the events.

On the performance, you kind of have to look at – that's going to be volatile. When you saw Q4 and Q3, this year having volatility, similar to what we saw last year. If you look at a non-cat quarter, you start to see it more normalized in Q2. Q1 is kind of where you should look at it in the event we don't have stress on it. And fee income, on your question on margin, it's a reflection of the business overall. We don't carve that out, but all of these results are reflected in our Property book right now.

A - Kevin J. O'Donnell

One thing I would add on the margin for this business is, because we are so tightly integrated, the way we think about risk and capital, the underwriters that write on behalf of RenRe Limited are the same underwriters that allocate into our third-party vehicles. So, in many instances, we are just writing a larger line and then allocating it to different balance sheets that have different supporting capital. So, we are able to leverage our infrastructure in a way that's difficult for many others who are managing their third-party capital in a less integrated way.

Q - Ryan J. Tunis {BIO 16502263 <GO>}

Okay, that's helpful. And then my follow-up, just trying to – I mean, obviously, a volatile business, but this year your overall return on equity was about 9%. And I think you mentioned earlier on the call, you had the big cat year, you had Japanese typhoons, you had wildfires, but I mean your results didn't really seem to be that negatively impacted by either of those, and you also benefited from quite a bit of favorable development on the 2017 events. So looking at that, that 9% ROE actually feels like a pretty good result, how are you thinking about where that could go next year? And how dependent is that on loss experience. I'm just trying to get a feel for what you think normal returns are in this business?

A - Kevin J. O'Donnell

So, what I said in my comments is that our strategy for the way we'll construct our portfolios in 2019 will need to be different than what we did in 2018. But we anticipate that, on an expected basis, our portfolios will be at least as profitable as they were in 2018. With that, because of the structural changes that we think we're going to build into our portfolio, I think our no-loss return will be higher, but we'll probably take a little bit more tail risk. That'll be panned out as – back to Elyse's question, dependent on what we see for ceded opportunities at mid-year.

So, we're not going to give guidance as to what we think an expected basis would be. I think this year was a heavy cat loss year. Next year, who knows what 2019 will bring, but we'll build a portfolio that we think will perform against all potential outcomes.

Q - Ryan J. Tunis {BIO 16502263 <GO>}

Thanks so much.

A - Kevin J. O'Donnell

Sure.

Operator

Our next question comes from the line of Kai Pan from Morgan Stanley. Your line is open.

Q - Kai Pan {BIO 18669701 <GO>}

Thank you and good morning. Since nobody has asked the California Wildfire yet, so I obliged to Josh question on that. So, I'm more interesting inbound the Property side. So, you said industry lost more than $15 billion versus last year, just less than that, yet your loss is much, much less than last year's. So just wonder if that change anything this year in the Property underwriting. And also, just your general sense of, going forward, seeing like last two years, of elevated losses in California. Is California insurable from both property as well as the liability perspective going forward?

A - Kevin J. O'Donnell

So, our face to the market for California risk was similar to our face to the market in 2017 from a profit perspective. So yes, we did things differently. And the part of the reason we did that differently is because we wanted to manage our overall risk at the holding level. And in order to do that, we needed to hedge down our Property risk so that we created room to take the better return in casualty risk. So yes, we did do things differently. I won't get into all the elements of it, but you should assume that we deployed the gross-to-net strategy in a quite fulsome way and that is beyond just using ceded retro.

With regard to is California insurable going forward, I think the answer to that is yes. But one needs to think very carefully about what not only is the stochastic probability of loss, but are there elements in a given year that will raise or lower the expected loss. Is there drought? Is 2019 going to change behavior of the cedents with regard to whether they shut power off or leave power on? And I think there is a significant difference in the risk control measures within the public utilities, in particular, in California. So I think picking your spots, understanding the overall climate regime that's in place, and then being specific about how you want to structure it against the capital you want to retain and the capital you want to cede, I think it's absolutely insurable, but it's one that it's going to take a fulsome analysis beyond just looking at a cat model.

Q - Kai Pan {BIO 18669701 <GO>}

So, just to be sure on the liability side, even without any legislative changes, you still think you would participate in the public utilities?

A - Kevin J. O'Donnell

At the right price, we will participate in the California public utility market.

Q - Kai Pan {BIO 18669701 <GO>}

Okay. Great. My second question, follow-up question is on the capital management. Last year, you took a pause in terms of like share buybacks, because a lot of deals going down and elevated catastrophes. I just wonder going forward this year, do you still feel you have a lot of things or opportunity on your plate that you will continue to take a pause on the share buybacks?

A - Robert Qutub {BIO 15269353 <GO>}

Well, you're right. 2018, we made a significant investment all the way through the course of the year into the business. Culminating with this year will be the investment or acquisition of TMR. So, that's where our capital is now. We're constantly looking at where we can deploy it. And I think we've shown in the past we've done a good job, have been a good steward of it. But obviously we have, overall, a long-term track record of being fair and balanced between investing in the business and returning capital back to our investors.

Q - Kai Pan {BIO 18669701 <GO>}

Okay. Great. Thank you so much and good luck.

A - Kevin J. O'Donnell

Thanks.

Operator

Our last question comes from the line of Josh Shanker from Deutsche Bank. Your line is open.

Q - Josh D. Shanker {BIO 5292022 <GO>}

Thank you for taking another question from me. So I'm going to ask some more California Wildfire questions, these should be quick ones. The California Wildfire loss, that's not included or is included in your net negative impact disclosures at the top of your press release?

A - Robert Qutub {BIO 15269353 <GO>}

The California - no. The casualty losses are not in the net negative impact.

Q - Josh D. Shanker {BIO 5292022 <GO>}

Okay.

A - Robert Qutub {BIO 15269353 <GO>}

Net negative...

Q - Josh D. Shanker {BIO 5292022 <GO>}

And.

A - Robert Qutub {BIO 15269353 <GO>}

Go ahead.

Q - Josh D. Shanker {BIO 5292022 <GO>}

And given that you guys are always so precise about giving that information, you've told us like that you'd have been profitable, can you give us some specific numbers around that or just that you would have been profitable is as good as we're going to get?

A - Robert Qutub {BIO 15269353 <GO>}

I think, I mean, what we showed is that in our overall construct of our reserves, we think we have it covered. The incremental amount that we had to rebalance, I was trying to direct you down to some numbers between $50 million and $60 million if you go back to the mid-60s, that's the number I was trying to steer everybody to on the call, Josh.

Q - Josh D. Shanker {BIO 5292022 <GO>}

Okay. And then the investigators cleared PG&E of liability in the Tubbs Fire of 2017. I know you said that this might take years to resolve. Understanding the timeline of that situation, is the Tubbs situation resolved and could the campfire situation be resolved in terms of liability within a single year?

A - Kevin J. O'Donnell

Potentially I guess it could be resolved within a single year, but the way these typically happen is CAL FIRE makes a determination of, in these instances, whether the public utility is culpable in the ignition of the fire. Once that happens, then you'll go through a process of assignment of costs and liabilities which can take a long time and is very complex. So, any time I guess is potentially achievable, but I wouldn't expect that these will be settled in a particularly timely fashion.

Q - Josh D. Shanker {BIO 5292022 <GO>}

Okay. Thank you very much and have a great day.

A - Kevin J. O'Donnell

You too.

A - Robert Qutub {BIO 15269353 <GO>}

Thanks.

Operator

And that is all the time we have for questions. I will turn it back to Kevin O'Donnell for closing remarks.

A - Kevin J. O'Donnell

Thank you for your time today and we look forward to speaking to you next quarter.

Operator

And this concludes today's conference call. You may now disconnect.