Q3 2018 Earnings Call

Company Participants

- Brian Meredith, Managing Director
- Kevin J. O'Donnell, President and Chief Executive Officer
- Peter Hill
- Robert Qutub

Other Participants

- Amit Kumar, Analyst
- Elyse Greenspan, Analyst
- Jay Cohen, Analyst
- Kai Aknin, Analyst
- Meyer Shields, Analyst
- Ryan Tunis, Analyst
- Unidentified Participant

Presentation

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's Third 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. (Operator Instructions)

Thank you. Peter Hill, you may begin your conference.

Peter Hill {BIO 3135705 <GO>}

Good morning, everyone, and thank you for joining our third quarter 2018 financial results conference call. Yesterday, after the market closed, we issued our quarterly release. If you didn't receive a copy, please call me at 212-521-4800, and we'll make sure to provide you with that. There will be an audio replay of the call available from about 1:00 PM Eastern Time today through midnight on December 1. The replay can be accessed by dialing 855-859-2056 or +1 404-537-3406. The passcode you will need for both numbers is 18690173. 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 January 9, 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 to discuss today's 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, Peter. Good morning and thanks for joining today's call. It was an active quarter on many fronts. Last night, we announced that State Farm agreed to invest $250 million in our shares. We also announced our definitive agreement with Tokio Marine to acquire their reinsurance platform Tokio Millennium Re, which I will refer to TMR. And of course, it was an above average quarter from the perspective of natural catastrophes.

I'll open with a discussion of State Farm's investment, then discuss the TMR transaction and how it accelerates our strategy and advances our global reinsurance leadership. Bob will then discuss the financial impact of the TMR transaction and highlight some of our quarterly results. Finally, I'll address the loss activity for the quarter and how our segments performed before taking questions.

I should also point out that in addition to Bob, I have included a few members of the deal team today, including Ross Curtis, our Group Chief Underwriting Officer; Aditya Dutt, our Treasurer and Head of our Ventures Unit; and Steve Weinstein, our Group General Counsel.

First, we announced last night that State Farm has agreed to make a $250 million investment in RenRe at yesterday's closing price of $128.37 with the intent of remaining a long-term shareholder. Our association with State Farm stretches back decades, and they are founding investor in both Top Layer Re and DaVinci Re. It is humbling to have the largest PC insurance provider in the US want to deepen its relationship with us in such a significant way.

Next, moving on to the TMR transaction, we will be acquiring Tokio Marine's reinsurance business in a transaction that values at a 1.02 times tangible book value for about $1.5 billion. I'm very excited about many aspects of this deal, not the least of which will be the multiple ways it will enhance our relationship with Tokio Marine.

As part of this transaction, we will be entering a business cooperation agreement with Tokio Marine relating to their non-Japanese reinsurance purchases. Further, Tokio Marine will provide us with an adverse development cover over their existing business, including unearned premiums, which will provide a significant downside protection. We expect the transaction to acquire TMR to close sometime in the first half of 2019, subject to all regulatory approvals.

By the way of background, TMR was established by Tokio Marine in 2000 and is based in Switzerland. It is a multi-line Property and Casualty reinsurer with 1.4 billion in shareholders' equity. They have a strong underwriting platform and a robust risk culture, as well as Switzerland, TMR platforms in Bermuda, the US, London and Australia. You will see that we posted in Investor Presentation this morning on our website laying out the details and the benefits of the TMR transaction.

I would now like to address some of the more important benefits of the transaction, which we present in greater detail starting on page six of the deck. To begin with, the TMR transaction will accelerate our strategy by providing us greater penetration into the reinsurance market at a time when desirable risk remain scarce.

Last quarter, I discussed our value proposition as a standalone reinsurer as well as my optimism about our strategy, including the growing -- leadership, the growing recognition of our leadership in Casualty and Specialty lines would afford us frequent, large, one of a kind opportunities to provide comprehensive solutions for important customers.

I believe this transaction does that and provides beneficial outcomes for both sides. For us, we were able to accelerate our strategy through access to a well protected pool of reserves and an attractive book of business that will enhance our portfolio. TMR is exclusively reinsurance, and we are intimately familiar with most of their business lines. The attractive multiple on this deal as well as the fact that Tokio Marine will receive $250 million of RenRe shares makes this transaction immediately accretive to shareholders and augments our financial strength and financial flexibility. Later in the call, Bob will explain in greater detail how the transaction benefits our financial results.

The TMR transaction is also a great example of how our strategy allows us to continually adapt to a changing market and permits us to offer more comprehensive solutions to a greater number of clients. Upon completion, we will increase our pro forma capital to over 6 billion, while our gross premiums written should approach 4 billion.

This growth in scale will increase our access to risk, which should allow us to apply our core strengths to a broader client and broker base. It also reinforces our strategy of being independent leading reinsurer able to solve our client's toughest problems. We have worked with TMR since it was initially formed in Bermuda in 2000. Since that time, they've expanded their footprint and growing their reinsurance portfolio, which now stands at 1.4 billion in gross premiums written, excluding their third-party capital management business.

By applying our superior risk selection capabilities, we will have the opportunity to re-underwrite their reinsurance portfolio and refocus the business on its most profitable areas. As a result of our efforts, we hope to improve TMR's combined ratio by improving both its loss and expense ratios. Our market leadership in reinsurance makes us uniquely positioned to assume and benefit from TMR's substantial reinsurance portfolio.

In the Investor Deck on pages 13 and 14, we present a conservative base case of 700 million of gross premium written, being that could meet our underwriting hurdles. In all likelihood, there is probably closer to about 1 billion of premiums that falls within our risk appetite. We will continue to evaluate the remainder post closing and through the application of our integrated system in gross to net strategy, we believe we have many options that we can consider for this business.

In addition to re-underwriting TMR's portfolio, we will further optimize it by bringing new sources of capital to the risk and more generally applying our gross to net strategy, which will lower the required capital needed to support this business and enhances return on equity. Conversely, the TMR portfolio will bring incremental risk to our joint venture business, increasing its ability to efficiently match desirable risk with efficient capital.

While I believe that we are obtaining this business at an attractive price, the transaction includes several structures designed to reduce our downside. Most importantly, Tokio Marine will provide us with an adverse development cover with $500 million of limit. From our perspective, this substantially removes the risk from the specific reserves we are adding to our balance sheet, and we will only be on risk for the business we choose to renew going forward.

The transaction includes TMR's fronting business, which is a very different business than our third-party ventures business. As part of the transaction, we have an agreement with Tokio Marine Group to continue to provide their capacity until 2021, allowing us to provide continuity to the fronting business (inaudible). While we work through the process of determining the future of this business, we will take no risk on our balance sheet related to these activities.

Tokio Marine has been a customer since 1994 and one of the more exciting aspects of this transaction is how it will further enhance our relationship. They have recognized our unique capabilities to provide bespoke solutions for their needs and have agreed to enter a business cooperation agreement with us. This agreement facilitates our cooperation on a portion of the non-Japanese reinsurance purchases of Tokio Marine and its affiliates.

To be clear, this gives us preferential access to attractive risk from a longstanding respected cedent with a global footprint, which is invaluable in an environment where risk is scarce and capital is abundant. In summary, I'm very excited about the TMR transaction and its ability to accelerate our strategy. We have work to do in order to realize these benefits, but I feel comfortable that we have the best team in the business, and we are eager to engage with TMR once the transaction closes.

I will discuss our business segments, recent losses and future opportunities in greater depth later on the call, but first, I'll turn the call over to Bob to discuss the financial aspects of the TMR transaction and update on our overall financial performance.

Robert Qutub {BIO 15269353 <GO>}

Thanks, Kevin, and good morning, everyone. We had a quarter that presented us with both opportunities and challenges. I know you probably have many questions for us today, so I'll limit my comments to discussing the TMR transaction, introducing some enhanced disclosure that we will be providing on fee income and highlighting a few financial results. Then I will turn it back over to Kevin.

Now starting with the TMR transaction, I'm very excited about this deal. It demonstrates our ability to bring multiple forms of efficient capital to large opportunities while simultaneously meeting our commitments to customers in a very active quarter. RenRe's financial foundation is solid and through application of our gross to net strategy and integrated system, we will be able to acquire material attractive book of business. The TMR transaction will have little goodwill associated with it, and it will be immediately accretive to book value per share, tangible book value per share, operating earnings per share and operating return on equity.

The purchase price will be 1.02 times tangible book at closing or approximately $1.5 billion based on June 30 valuations. We will pay this with cash in RenRe shares. The cash component will be slightly more than $1.2 billion and consist of a pre-closing dividend estimated at about $250 million and $969 million of available cash. Any variance in the pre-closing dividend above or below $250 million would result in an adjustment to the available cash component of the purchase price and keep the cash component constant.

Tokio Marine will also receive $250 million of RenRe shares priced at yesterday's closing price of $128.37 per share, which they have agreed to hold at least one year. Given the significant overlap between our reinsurance books, we expect that there will be substantial synergies between us and TMR. As you know, however, realizing these synergies must be done responsibly and will occur over the course of the next couple of years.

We will do the rest of our business as we do with the rest of our business. We will manage expenses intelligently and with an eye towards maximizing shareholder value. We will not issue any debt in conjunction with the transaction. On a pro forma basis, however, we anticipate that our total capital will increase approximately $500 million. This should reduce our debt to capital ratio slightly more than 1 percentage point from its current 14.8% to 13.6%.

In addition, on a pro forma basis, we expect the TMR transaction to increase operating leverage and investments float. At our closing, our invested assets should increase by approximately $3 billion. We expect to bring significant underwriting acumen to TMR's existing book, which we anticipate will result in a smaller portfolio of higher quality risks. We will also use our gross to net strategy to optimize this risk with ceded and third-party capital. As we optimize TMR's book, we will aggressively manage its capital and allocate any excess responsibly. I should note that our approach to capital management has not changed. We take a long-term view, and we will look to deploy capital into underwriting and business opportunities first. Since our inception as a company, we have returned 60% of our GAAP net income to investors or $4.3 billion in the form of dividends and share repurchases.

Now moving on to our consolidated results for the third quarter, we reported net income of $32.7 million or $0.82 per diluted common share. Our operating income was $20.6

million or $0.52 per diluted common share, which excludes $13.6 million of net realized and unrealized gains on investments.

The gains were primarily from our strategic equity investments and were partially offset by losses in our fixed maturity investments as a result of increased interest rates. We had underwriting loss for the quarter of $29 million and reported an overall combined ratio of 105%. Our gross premiums written were down in the quarter to $626 million from $640 million in the comparable quarter. This decrease is largely due to $170 million of reinstatement premiums that we booked in the third quarter last year versus $17 million of reinstatement premiums in the current quarter.

In our ongoing effort to help you think about our business consistent with the way we do, I wanted to discuss some enhanced disclosure around fee income that we will be providing going forward. You will note that we have added a new page 15 to the supplement, where we break out the fee income component of our business. While we have been providing this information for several years now in our SEC filings, we wanted to make it more detailed and transparent. Fee income includes the management fee income and performance fee income of our property catastrophe focused joint venture business, managed funds and structured reinsurance products.

While we also have other deals and structures where we trade risk income for fee income, we wanted to give you increased transparency into the fees generated through our ability to bring third-party capital to risk. In addition to providing the fee income so far in 2018, we have also included four prior years to give you a better idea of our historic performance.

There have been some variance in fee income over the last five years due to both the 2017 catastrophe events and now the 2018 catastrophe events, both of which reduced the size of our performance fees. I should remind you that the way we account for our fee income serves to reduce the underwriting expense ratios in our property catastrophe business. More specifically, management fee income reduces our operational expenses and performance fee income reduces acquisition expenses.

I would like to add that even with this increased transparency into our fee income, our strategy has not changed and our focus will remain on serving our customers need, not accumulating assets. Our choice to balance sheet is driven by matching our customers' needs with the most efficient source of capital. This approach is consistent with our strategy of applying our integrated system to match attractive risk with efficient capital.

Now before moving to our segments, I wanted to highlight again for you this quarter the continued improvements in our operational efficiency. You should expect operational expenses to increase in the coming quarters as we invest in the business and especially as we undertake the process of integrating TMR. However, the operational expense ratio should remain relatively stable over time due to expected growth in net earned premiums. One of the other benefits of the TMR transaction will be to continue to improve our underwriting and investment leverage.

Now moving onto our segments and starting with the property segment where property gross premiums written in the third quarter were down 7% over the comparative quarter. Gross premiums written in our catastrophe class of business decreased by 12.8%. We booked $162 million of reinstatement premiums in the third quarter of 2017 versus $17 million in the current quarter. Backing out the effect of these reinstatement premiums, we grew property catastrophe premiums by $114 million.

Now consistent with finding large opportunities with customers seeking unique capital solutions for existing business, the growth in our property catastrophe business this quarter was supported by over $100 million of gross premium written that, by its nature, will be non-recurring. The majority of this premium was earned this quarter and will be fully earned by year-end. This premium was from large transactions where we provided bespoke solutions. While we have increasingly benefited from these one-time opportunities over the past few years, we caution that by their nature, these deals are unpredictable, which could result in variability and premium going forward.

In our other property class of business, we grew gross premiums written by almost 9% over the comparative quarter. In total, our property segment incurred an underwriting loss of $44 million and a combined ratio of 115% in the third quarter.

We reported $152 million in net negative impact to the 2018 catastrophe events. This broke down to $68 million from Typhoon Jebi, $56 million from Hurricane Florence and $28 million from other catastrophic events. I should also briefly mention that Hurricane Michael on the basis of some very preliminary figures, we currently estimate that it will have a net negative impact of $100 million on our Q4 financial results.

Now moving on to our Casualty segment, our gross premiums written were up 3% in the third quarter of 2018 over the comparative quarter. The Casualty segment generated underwriting income of $15 million and a combined ratio of 94%. Our Casualty book continues to run at current accident year loss ratio of around the mid 60s, putting 64% for the quarter. This is both consistent with recent performance and in line with our expectations going forward. We experienced modest favorable development in the Casualty segment from prior accident years of 3%.

Now turning to investments, we reported total investment results of $94 million in the third quarter, resulting in an annualized total return of 3.3%. Included in total investment results was $81 million of net investment income, largely from our fixed maturity and short-term investment portfolios.

We have benefited from higher average invested assets and the impact of interest rates during the recent periods. For the quarter, we grew our overall investment portfolio by over $800 million from the prior quarter. The yield to maturity on our fixed maturity and short-term investment portfolios was 3.1% at September 30, 2018, which was up slightly from the previous quarter.

The duration of our fixed maturity and short-term investment portfolios was down at 2.0 years. As I explained last quarter, our reported duration has been decreasing recently due to the short duration of assets held by our collateralized balance sheets, principally and so on. The duration of the portion of our investment portfolio that impacts shareholders is somewhat longer at around 2.2 years.

And with that, I'll now turn the call back to Kevin for more details on our segments.

Kevin J. O'Donnell

Thanks, Bob. Starting with Property, there were a number of natural catastrophes in the quarter, both in the US and around the world. While there was a high frequency of events, none was particularly outlier from a severity perspective. Bob touched briefly on the financial impact of these events, so I would like to provide some additional details related to the losses.

This summer in California, the (inaudible) Mendocino wildfires were very destructive from the perspective of the number of acres burned, with the latter being the largest in modern California history. From an industry loss perspective, however, they were not as impactful as the number of acres burned would imply with estimated loss of around $1 billion, primarily in personal loans.

Moving on, Japan experienced an extraordinary amount of loss in the third quarter. In late June through mid-July, successive heavy downpours caused widespread devastating floods and mudslides, resulting in industry insured losses of up to about $4 billion. Then on September 4, Typhoon Jebi struck Japan, impacting a second most populated region after Tokyo.

Jebi was the strongest typhoon to strike Japan since typhoon Yancy in 1993 and comparable in intensity to Typhoon Murray in 1991. Multiple locations experienced record high winds speeds with widespread damage and extensive flooding. At the end of the quarter, Typhoon Trami struck Japan, while not as powerful as Jebi, there was still a large storm.

Increasing its overall impact to the reinsurance sector will be the level of aggregate deals purchased in Japan, as together with the flooding in Jebi, there probably has been at least 11 billion industry loss during the quarter there.

In the United States, Hurricane Florence made landfall in North Carolina as a strong Category 1 storm on September 14. While losses from this storm will be largely from extensive flooding in mid-Atlantic region due to record-breaking rainfall, the result of substantial wind damage. We think Florence will be around a $4 billion loss, and there are several factors increasing the loss to the reinsurance market, including the impact of the state windfalls, the buying habits of several smaller regional players and aggregate deals.

Moving onto Asia, we had Typhoon Mangkhut in September, which reached peak intensity as a Category 5 storm and was the strongest typhoon to strike Hong Kong since Allen in 1983. Bob briefly mentioned the estimated net-negative impact of Hurricane Michael. This is a fourth quarter event that I will touch on in more extensively during our next call. We think this is about a 10 billion industry event. Of course, this is Florida, and we will be monitoring the situation closely for assignment of benefits and loss adjustment expense issues, and we'll update you on its development on next quarter's call.

We continue to track the 2017 catastrophe events. And as we discussed in the last call, adverse industry trends from Hurricane Irma persist. The persistence is being driven by the challenging Florida legal environment combined with high loss adjustment expenses. That said, we remain comfortable with our reserves for the 2017 cat events.

Moving on to other property business, I wanted to add that along with its many other benefits, the TMR transaction is likely to add about 150 million in gross premiums written to our property cat over the long term. In our other property portfolio, we experienced solid growth this quarter as gross premiums written increased by about 9%. The growth in other property came primarily from our London platform. Moving forward, we will continue to see growth in our other property business, both organically and from the TMR transaction. We estimate the optimized TMR portfolio may add up to 180 million of gross written premiums to our other property business.

Looking at Casualty, we grew our Casualty segment's gross written premium by 3% on a year-on-year basis in the third quarter. Underneath this apparent, muted growth rate, however, was quite a bit of change. This quarter, we had another first call opportunity to write a large bespoke deal for the California wildfire liability market, similar to the deal we discussed with you last quarter.

In addition to bringing a substantial amount of capital to a dislocated market, we're able to apply our gross to net strategy and integrated system to see two-thirds of this risk to our partners. This includes Epsilon and what is the first instance for us, ceding casualty risk to a collateralized vehicle. As you know, collateralized vehicles have tended to focus on short tail property CAT risk. So ceding liability risk to Epsilon represents another instance of our innovative market leadership.

The pricing trends we have discussed all year in Casualty have continued into the third quarter with improving terms and conditions on the more troubled accounts. While underlying rates continue to increase, loss trends are also up. Going forward, the TMR transaction is likely to have the most profound impact on our Casualty segment. Once optimized, it could result in additional gross written premium of over 360 million.

In conclusion, we had a very active quarter. Despite multiple large events, we grew tangible book value per share, plus accumulated dividends, and we're able to [technical difficulty] substantial foundation for future success with the TMR transaction. We remain committed to executing our strategy as the most effective means of maximizing shareholder value, and it was gratifying to have two outstanding organizations such as Tokio Marine and State Farm agreeing to become shareholders.

With that, I'll turn it over to questions.

Questions And Answers

Operator

(Operator Instructions) And our first question comes from the line of Kai Aknin from Morgan Stanley. Your line is open.

Q - Kai Aknin

Thank you, and good morning. My first question, if you can give us a little bit background about the deal with TMR. Is that happened before you discuss it with Time Square Capital? And you said the processes is a compounded bidding process. Just wonder why you could get such attractive price relative recent deals, if you can provide any color around it? And it sounds like you will continue -- be like a your independent strategy going forward.

A - Kevin J. O'Donnell

Thanks, Kai. As I mentioned, we've known Tokyo for many years and have worked with them on different risk solutions over time. I would say it be difficult to pinpoint exactly one specific discussion started, but it was certainly -- be easy point to a more formal discussions beginning in early summer.

With regard to your Time Square comment. The Times Square letter and publication of that letter really had no influence in our thinking about this transaction. We believe this transaction is consistent with our strategy and is long-term beneficial to shareholders. With regard to the process, that's a better question for Tokyo. So we found Tokyo to be straightforward and collaborative partner and thinking about how to structure this transaction and I think the transaction reflects the needs that they hope to achieve, which was a comprehensive exit from the reinsurance business and was able to meet the needs that we have, which was bringing deal that we've was long-term accretive to our shareholders.

Q - Kai Aknin

Okay, that's good. And then my second question is on the sort of like -- you expected after-tax run rate earnings about $100 million. You leave the three component of that. One of them is vast income $3 billion and if you time like 2.5% investment yield that's really $75 million. So I just wonder how much of the other two factors, including improving combined ratio on the $700 million gross premium written, as well as how much cost synergy would it contributed to these $100 million run rate.

A - Kevin J. O'Donnell

So, thanks. The way that I think about it is, I think the investment portfolio is pretty straightforward. Long term, our objective is to -- by line of business, apply the same metrics we have for our existing businesses and math their businesses into our risk appetite and our risk management systems. So I would look at buy a line of business, the expectation is that our underwriting will converge with the margins that we achieved on our platform.

In order to do that, we've assessed that we believe 700 million is clearly within our risk appetite and as we became more transparency on the business after close, we think that could be up to a billion. With regard to the synergies, Tokyo Millennium is a reinsurer and we are reinsurers with that, there are synergies that need to be realized. I would say long term. I would look to rationalize the loss ratios --

Operator

Are you still on the line?

Q - Kai Aknin

Yes, I am. I couldn't hear them.

Operator

My apologies. Our line has just disconnected, just one moment.

A - Kevin J. O'Donnell

What I said is the investment portfolio trends pretty transparent as to how that will roll over long term. On a combined ratio basis, we will look to rationalize and target the renewals on their book to be at the same metrics and risk tolerances that we have on our existing books which you should expect on a run rate basis that the $700 million that we believe clearly fits our risk appetite could be as much as $1 billion once we have more clarity on the portfolio.

We will be at our average returns. And then you asked about the cost synergies. And I would say, again, our long-term view is that we would like to maintain the expense ratio that we have with the organization, prior to the acquisition. It will take some time to get there, but we believe we have a plan and a runway to be able to do that.

Q - Kai Aknin

Okay. Last one if I may. Will you pass buybacks throughout 2019?

A - Robert Qutub {BIO 15269353 <GO>}

As I said in my prepared comments, Kai, our approach to capital allocation has not changed. As demonstrated with this transaction, we will first invest in the business and continue to further our strategy and buybacks are a part of our capital allocation plan and always in our consideration, we've got a long history of returning capital to shareholders.

Q - Kai Aknin

Okay. Well I take that you probably could do some buybacks even with like that about a billion dollars cash outlay?

A - Kevin J. O'Donnell

It's all about deploying the capital in the right area to further our strategy, Kai. Right now, this transaction is really right up our alleyway and this is what we think it's best deployed.

Q - Kai Aknin

Okay. The other way to ask for that is that after the deal, you still think you have excess capital?

A - Robert Qutub {BIO 15269353 <GO>}

Yeah, we have. We have excess capital that we look to deploy as we come into the renewal seasons. That's where we look to deploy. Again, nothing's changed, Kai.

Q - Kai Aknin

Great.

A - Kevin J. O'Donnell

One amplification I would make to Bob's point is as I mentioned in my comments, the re-underwriting, I talked a little bit about our risk appetite, one of the components of the transaction will be that on the larger diversified platform, TMR's business will require less capital. So I think over the long term, we can get closer to the equity issue rather than the purchase price.

Q - Kai Aknin

I see. But thank you so much for all the answers, and good luck.

A - Kevin J. O'Donnell

Appreciate it. Thank you.

Operator

Our next question comes from the line of (inaudible) from Goldman Sachs. Your line is open.

Q - Unidentified Participant

Hi. Good morning, everybody. I have a couple of questions on the deal. So it seems like some of the right sizing of the portfolio of Tokio Millennium would come or mostly, it would come from the Casualty and Specialty side. How long does it take to right size and what's the tail risk involved with that portfolio.

A - Kevin J. O'Donnell

I think your observation is correct. The Casualty and Specialty is it bigger portfolio for them most deals are annual, so depending on close, it will take 12 months. There are a few multi-year deals, which will take longer. Your second question about the risk. Our balance sheet will be exposed to risk associated with any business on the TMR balance sheet until we renew it assuming that the reason being is that the adverse development cover that we purchased in conjunction with the transaction covers the unearned premium reserve meaning only renewed business will hit the balance, the new balance sheet and that we will be exposed to.

Q - Unidentified Participant

Okay. And as you consider the options for what to do with the elements that you don't necessarily want to take on your own balance sheet, can you maybe talk through the process of allocation to some of your partners, the other procedures going to third-party retro market or simply not renewing?

A - Kevin J. O'Donnell

I think most of the lines of business that they're in, we're familiar with. They have some businesses that from a class perspective are more challenged. So those probably will be the area in which we'll focus our re-underwriting. I think once we have the risk in our balance sheet, our normal systems will be applied where we will measure the return on equity on our owned balance sheets and our partner balance sheets and then determine which is the appropriate capital to apply to the risk and which ultimately optimizes the specific portfolio and maximizes our return. So it's not a simple answer that it will be for this book of business, we'll do X or Y, I would say that if I look at ours ceding ratios for 2018, my anticipation is they'll be reasonably flat in 2019. It wouldn't set up the target, but it's an easy way to think about how the book will be structured.

Q - Unidentified Participant

No, that's helpful. And one quick final one. It sounds from your earlier comments that you're not necessarily looking to reallocate the investment portfolio coming from Tokio Millennium. Is that correct?

A - Robert Qutub {BIO 15269353 <GO>}

I think the investment portfolio that outlined was about $3 billion in total assets. There's a few things in there that will look to optimize that we will bring into ours. The duration of their liabilities given its casualty specialty lends itself to a little bit longer duration, but I think we should integrate that pretty well -- pretty seamlessly.

Q - Unidentified Participant

Got it. Thank you very much.

Operator

(Operator Instructions) And our next question comes from the line of Jay Cohen from Bank of America Merrill Lynch. Your line is open.

Q - Jay Cohen {BIO 1498813 <GO>}

Thanks. Two questions, actually. The first is, it looks like in the third quarter, you're paid losses were negative, which you typically don't see. I'm wondering if you can explain what happened there.

A - Kevin J. O'Donnell

We'll look that up. Why don't you ask your second question?

Q - Jay Cohen {BIO 1498813 <GO>}

Sure. You had mentioned that you're beginning to see some Casualty business to Epsilon, which is an interesting development. I guess the concern one might have is that if the, call it, in general, the alternative market, it gets more interested in assuming Casualty risk, does that limit pricing ability on the Casualty side if we bring more capital into market that's already fairly competitive?

A - Kevin J. O'Donnell

So there has to be in my experience for third-party capital to -- for risk to be structured in a way where third-party capital to be interested in Casualty. It has to be a pretty specific set of circumstances . So I think we are uniquely positioned to kind of construct that risk and have access to it. Secondly, I would say that one of the primary drivers for interest in the reinsurance market is the diversification that extreme events or catastrophes bring to more traditional investment portfolios. And as we know, a lot of Casualty business' income is related to the float associated with the tail. So I think it is something that we're kind of in a unique spot to be able to bring that risk to that capital. I think from an investor appetite, it's one in which they have expressed interest in having Casualty business, but it doesn't meet a primary objective, and one of the primary reasons they like the Property cat business. As I mentioned, I've got -- I'm going to turn (inaudible) if you had any comments there.

A - Robert Qutub {BIO 15269353 <GO>}

Sure. Hi, Jay. I will just add, our focus is actually on innovating and trying to put together solutions for our clients, as Kevin mentioned, for us, it's about matching risks and efficient capital and as long as we can do that, we don't focus too much on what effect that might have on pricing necessarily. We'd rather be on the front foot trying to get capital in to help our clients and solve their issues. So that was really the motivation for doing what we did.

Q - Jay Cohen {BIO 1498813 <GO>}

Got it. That's helpful, guys. Thank you.

A - Kevin J. O'Donnell

Thanks. And I think, Bob, you've got the first one.

A - Robert Qutub {BIO 15269353 <GO>}

Yeah. That's basically you're starting to see the recoveries come in from prior years. If you look back, we had about $1 billion and a half year ago recoveries from Q3 '17, we're starting to see those recoveries come in, which is a good thing to bring the assets down.

Q - Jay Cohen {BIO 1498813 <GO>}

Definitely. Great, thanks for that.

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. I had a follow-up question to Kai. This deal obviously looks phenomenal for you from a financial perspective. That said, if I flip the equation you have one of your large shareholders asking you to look at other options. You have a market where we have seen decent multiples on two out of three deals, which means you could have fetched north of a 1.5 multiple, yet you still chose to go in the other direction. Why not benefit from the deal climate right now and provide the appropriate exit value to RenRe shareholders?

A - Kevin J. O'Donnell

So thanks for the question, Amit. Where we've looked at it is our primary metric is to grow tangible book value per share, plus accumulated dividends over the long term. And we believe that our strategy and the advancement of that strategy through the execution of this transaction achieves that. So when I think about the activities that we've done this quarter, we've always talked about our preferred use of capital is to deploy it in the business. This deal on every financial metric is accretive. So I think it is absolutely consistent with everything we've talked about with what our strategy is and how we're executing it and think about it from the perspective of our primary measure, it is the best way for us to achieve that growth over the long term.

Q - Amit Kumar {BIO 15025799 <GO>}

But again, the stock is trading at a modest premium to book. It just seems that there is -- I'm not sure if there is a clear overlap between what the investors are looking for. I hope you understand the total return metrics having known the story for so long, but clearly you have introduced execution risk for multiple quarters now and you have chosen the other direction. I'm just trying to understand was there any thought of ever given as to let's see what the market is looking for out there or did you just choose to stick to your internal metric and focus on value creation?

A - Kevin J. O'Donnell

So, you mentioned several things in your comments. One is, I believe there is a limited execution risk in this transaction. It's a reasonably simple structure, it is all reinsurance, there's nothing that they do, that we don't understand and embedded in the construct of the transaction are significant downside protection, so from that perspective, I think it's a pretty clear choice that executing this transaction is by far the long-term most beneficial way for us to build tangible book value. Your second question is, from a transaction perspective is one in which we have great governance and any bonafide transaction that is presented to us, we would carefully consider.

Q - Amit Kumar {BIO 15025799 <GO>}

Last question. Do you think the stock is appropriately valued?

A - Kevin J. O'Donnell

I look at these calls as a good opportunity for me to explain our strategy and to discuss our earnings. I think what the stock market decides our valuations are beyond the scope of what I think is appropriate for the call.

Q - Amit Kumar {BIO 15025799 <GO>}

Thanks for the answers.

A - Kevin J. O'Donnell

Sure.

Operator

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

Q - Elyse Greenspan {BIO 17263315 <GO>}

Hi, thank you tell my question on. Kevin, interesting timing, you guys are announcing this deal kind of is were, virtually done with hurricane season. And couple months away from January 1, 2018, can you provide us your outlook and how you saying the cat market will turn about next year, I think there has been some other players, I think mainly the losses of 17 combined with the losses that we've also seen this year should put a floor on cat prices, but it seems like you guys entering into this deal kind of one counter to potentially needing more capital for better opportunities at 1.1 next year.

A - Kevin J. O'Donnell

I think I heard two questions in there. I think the timing of this deal is going to end over that we are in the calendar year. These things take a long time to bring together and closing is really a matter of when negotiation sees rather than trying to constructed against whenever renewal begin.Your second question is around the hurricane season, I would say that the way I think about where we are with regard we've talked many times in the past about whether this is a secular shift or cyclical shift. You believe is a secular shift, but we do believe that cycles will persist. An important driver for this year end renewal I think will be the behavior of the retro market, there is a lot of dependence on for many of our peers on retro for them to participate in the market. A lot of that retro frankly comes from 3rd-party capital, their willingness to continue to support, but also the traditional markets willingness to support retro. I think we'll have the biggest impact on pricing. I don't anticipate that there will be a overly meaningful shift in demand, there will be few customers are purchasing more, but I would recognize that on a macro level demand will be reasonably stable. I think supply could be constrained depending on retro availability and I think a lot of the pricing in the market is supported by there being ample constructive retro available.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay. And so, based upon what you see, do you think rates for retro and then also down to just traditional reinsurance will be flat or down or marginally up when we get to January 1.

A - Kevin J. O'Donnell

So, the platform that we've built, allows us to compete in any rate environment as long as there's positive margin in the transaction. If there is rate enhancement next year, we'll benefit from that rate enhancement. If there is not rate enhancement, we'll optimize our portfolio against the environment in which we are plenty. I don't have a portfolio as per the 1.1 pricing.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay. And then, my other question relates back to TMR and the margin outlook there. So, I think part of -- they had pointed to a 99% combined ratio in '18. So part of the delta to get to your 100 million probably stems from not renewing some of the business, but is there a way to tell us when you come to that 700 million to a billion of business that you define is addressable for you guys, what the margin that that business is currently running at? And I guess my second part of the question is when you guys did the platinum deal, is there a way to say that you brought that business on and how much you took off of margins to kind of show that you can see some material margin improvement with this transaction as well?

A - Kevin J. O'Donnell

So, the way I think about it is it will take time for us to bring the TMR risk and capital onto our platform. But as we do that, it will be done at the same margins of our existing business, by line of business. So from that perspective, I think we are looking at a book that is -- it will be underwritten and will be at the same margins as the business that we have, and we like the book of business that we have. Additionally, we'll apply our gross to net strategy which will optimize the amount of capital associated with the support of that business, which will enhance the ROE.

Your second question, I think, is addressed with the amount of risk we're taking until it is re-underwritten. And as I mentioned earlier, the adverse development cover which protects -- what we believe is to be a solid pool of reserves is protected by the ADC. So until we renew the business, it will be in the reserve pool and that reserve pool will be protected by the ADC.

Operator

(Operator Instructions) Your next question comes from the line of Brian Meredith from UBS. Your line is open.

A - Brian Meredith {BIO 3108204 <GO>}

Yes, thanks. Couple of quick questions here. First, I'm just curious, can you give a little more clarity upon why the State Farm transaction? It doesn't sound like, Bob, what you're saying that you needed that capital to do this transaction, you got plenty of liquid assets in your balance sheet and excess capital. So, why do the State Farm Equity raise?

A - Kevin J. O'Donnell

In structuring the deal, we always contemplated $500 million of equity, and I think what I tried to comment on, what Bob tried to comment on is we're not a company that at frequent intervals is issuing equity. So being that we had the transaction which contemplated the issuance of equity, it was a natural time for State Farm to enter our stock.

A - Brian Meredith {BIO 3108204 <GO>}

Got you. Okay. And then the second one unrelated, just on the one-off transactions you had this quarter, just curious, how much is still to earn in the fourth quarter on those transactions and should we expect that it's going to -- looks like it pretty much falls to the bottom line from the underwriting profitability generated on it in the quarter.

A - Robert Qutub {BIO 15269353 <GO>}

Yeah, Brian, this is a small piece, but there is a small amount that we figure we would throw it in there, but it's nowhere near the size of what we saw this quarter, so I would round that down to nearly zero.

A - Brian Meredith {BIO 3108204 <GO>}

Got you. Great, thanks.

A - Kevin J. O'Donnell

Thank you.

Operator

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

Q - Ryan Tunis {BIO 16502263 <GO>}

Hey, thanks. Just a couple on the deal. The first one, just focusing on the fact there has 56 million of average after-tax profits in TMR in the last five years. First of all, will number look different with your tax structure and is there a tax synergy element of this? And also I think going back to Lisa's question, when you trim that book from 1.3 billion to 700, is that 56 million, would that have gone up or down? In other words, the part of the book you don't like, is that higher than 100% combined ratio?

A - Robert Qutub {BIO 15269353 <GO>}

A couple of things on that. Yes, it would look better on a Bermuda tax platform than the existing platform. So that helps give its some uplift there. Regarding the the book of business we're keeping on the technical ratios or the expense ratios, we would be going into what Kevin said, we'd be optimizing to have a better combined ratio on the book of business that we select, plus there will be synergies in the deal, so we see a number of different levers that are driving that up to the 100 million that we put out there, plus you've got the investment portfolio as well supporting that.

Q - Ryan Tunis {BIO 16502263 <GO>}

Any order of magnitude on the tax benefit and how much the tax helps?

A - Robert Qutub {BIO 15269353 <GO>}

It's an amount we haven't talked about, but it is a factor and I think you could see there tax on their website what they disclose.

Q - Ryan Tunis {BIO 16502263 <GO>}

Got it. And then my other one was just on thinking about how this may be changes your mix in Specialty, Casualty, is this more quota share, primary layer type of stuff? And then if I recall with platinum, it seems like there may be some, not issues, but you loss picks are more conservative in Casualty, Specialty. Is it possible we'll see something like that here or perhaps there combined ratios in those businesses are as comparable as where you guys may make their selections.

A - Kevin J. O'Donnell

So it is more of a Casualty bias to their book and probably more quota share within that bias as well. I wouldn't focus too much on -- our objective is to bring this on at the same loss ratios that we have with our in-force book. So I think -- that's the point of the re-underwriting frankly is to basically enhance the portfolio both by concentrating on the most profitable lines and then concentrating on the most profitable deals. Again, I think the 700 million is clearly within our risk appetite and it could easily stretch to the billion.

Operator

And our next question comes from the line of Meyer Shields from KBW. Your line is open.

Q - Meyer Shields {BIO 4281064 <GO>}

Great, thanks. Two very quick questions. One, is it fair to sort of scale the required capital at TMR to the amount of gross return premium you will be beekeeping?

A - Kevin J. O'Donnell

So I think what I said earlier on the call is the back of the envelope number that I'm looking at is the re-underwriting portfolio with the enhanced profitability and then having it on our diversified platform probably brings it closer to the equity number. The one thing I'd point out though is due to the flexibility of our platform, we control how much risk capital we're deploying and how much fee capital we're deploying, but as a beginning point, that's probably not a crazy target to have.

Q - Meyer Shields {BIO 4281064 <GO>}

Okay. No, that's helpful. Sorry, I missed that. Second question, and this is going to sound a little naive, but to the extent that TMR was writing capacity premium when was it based on comments you made in the past about how you have a look at most of business was available, how difficult will be going be to retain that.

A - Kevin J. O'Donnell

Can you restate your question? I want to make sure I understood it.

Q - Meyer Shields {BIO 4281064 <GO>}

Right. So, overly simplistically, I would assume that if (inaudible) to someone other than RenRe for catastrophic risk, there's a reason for it. So wondering whether there's a risk that it will be more difficult to retain the cat premium written by TMR?

A - Kevin J. O'Donnell

Okay. So I think that's -- that's a risk with any transaction is do you look at what is the overlap and then what is the likely outcome of that overlap. I think we did extremely well in protecting the book of business with the targeted book of business when we did the platinum transaction and I feel that our relationships with our customers will be sufficient for us to maintain that business. I think it's a broader question than simply the property cat book. I mean, it get applies to the Casualty and Specialty business as well, but it's certainly a risk within any transaction, but it's one that I feel pretty well suited and pretty well equipped to manage.

Operator

And there are no further questions. Apologies.

A - Kevin J. O'Donnell

I was just going to say -- and the other thing I would say is that when we think of the 700, we believe that that is a target that's achievable, both as within appetite and within risk, moving up to the billion is more risk on the comment you made.

Operator

And there are no further questions at this time. I will turn the call back over to Kevin O'Donnell for closing remarks.

A - Kevin J. O'Donnell

I know we throw a lot after this quarter. We appreciate your attention on the call and as always, if there's follow-up questions, we're happy to take them. Thanks again for your attention and for your time.

Operator

This concludes today's conference call. You may now disconnect.