Q4 2017 Earnings Call

Company Participants

- Albert Benchimol, President and Chief Executive Officer
- Linda Ventresca, Head of Corporate Development and Chief Transformation Officer
- Peter Vogt, Chief Financial Officer

Other Participants

- Elyse Greenspan, Analyst
- Jay Cohen, Analyst
- Joshua Shanker, Analyst
- Kai Pan, Analyst
- Meyer Shields, Analyst

Presentation

Operator

Good morning and welcome to the Q4 2017 AXIS Capital Earnings Conference Call. All participants will be in listen-only mode. (Operator Instructions) After today's presentation, there will be an opportunity to ask questions. (Operator Instructions) Please note this event is being recorded.

I would now like to turn the conference over to Linda Ventresca, Investor Relations. Please go ahead.

Linda Ventresca {BIO 5930519 <GO>}

Thank you, Kate, and good morning ladies and gentlemen. I'm happy to welcome you to our conference call to discuss the financial results for AXIS Capital for the fourth quarter and the year ended December 31st, 2017. Our earnings press release and financial supplement were issued yesterday evening after the market closed. If you would like copies, please visit the Investor Information section of our website, www.axiscapital.com.

We set aside an hour for today's call, which is also available as an audio webcast through the Investor Information section of our website. A replay of the teleconference will be available by dialing 877-344-7529 in the United States and the international number 412-317-0088. The conference code for both replay dial-in numbers is 10115814. With me on today's call are Albert Benchimol, our President and CEO, and Pete Vogt, our CFO.

Before I turn the call over to Albert, I will remind everyone that the statements made during this call, including the question-and-answer session, which are not historical facts may be forward-looking statements. Forward-looking statements involve risks, uncertainties and assumptions. Actual events or results may differ materially from those projected in the forward-looking statements due to a variety of factors, including the risk factors set forth in AXIS' most recent report on Form 10-K, Form 10-Q, and other documents on file with the SEC, as well as the additional risks identified in the cautionary note regarding forward-looking statements in our earnings press release issued on February 7th, 2018. We undertake no obligation to update or revise publicly any forward-looking statements. In addition, this presentation may contain non-GAAP financial measures. Reconciliations are included in our earnings press release and financial supplement, which can be found on the Investor Information section of our website.

With that, I'd like to turn the call over to Albert.

Albert Benchimol {BIO 2023727 <GO>}

Thank you, Linda, and good morning everyone. Thanks for joining us today. I'm happy to welcome Pete Vogt to his first call as our CFO, having taken over from Joe Henry after his retirement at the end of 2017.

Let me begin with some initial observations, after which Pete will run us through the details of the financial results and then I'll come back and provide some comments on the market. 2017 was a year of two themes for AXIS; a challenging year in terms of market conditions and financial results, but a very strong year in terms of organizational development and market positioning. Last night, we reported operating income of $20 million or $0.24 per diluted share for the quarter and an operating loss of $265 million or $3.15 per diluted share for the full year. We finished the year with diluted book value per share of $53.88, a decrease of 7.5% from the prior year.

The drivers of operating performance were the same in both the fourth quarter and the full year; the cumulative effect of ongoing price reductions, the Ogden rate change in the UK, higher non-cat losses in property and a near record catch year for the industry, including record California wildfires in the fourth quarter. Our book value was also impacted in the quarter by the change in the US tax law, which caused us to write down our deferred tax asset by $42 million or $0.50 per share.

Before Pete walks you through the details of our financial results, which we recognize are more complicated this quarter, as for the first time they include the operations of Novae and purchase GAAP assumptions, I do want to share a couple of observations to put these results in context. The reported figures mask a number of positive signals throughout the year. Amid an epic year for insurance industry cat losses, which at approximately $120 billion is second only to 2011. The impact of cats on our combined ratio and book value was much less than it was in the two previous $100 billion plus cat years. It's a result of our efforts to reposition our portfolio and reduce the volatility of our earnings. Our experience this year was well within the range of our peer group for all of the events. We still have more work to do to further reduce our susceptibility to volatile cat losses, but the results of this year confirm we're on the right path.

Importantly, our progress also continued on our other lines. Indeed, other than property and property cat lines that suffered high attritional losses this year, our core ex-cat technical results improved. In insurance, the aggregate ex-cat technical ratio for all lines other than property fell by almost 2 points in the year as underwriting actions more than offset market price reductions. In reinsurance, the full year ex-cat technical ratio for all lines other than property and catastrophe also improved by 1 point even with the impact of the Ogden rate change of the UK motor book.

This is tangible evidence that our efforts to deliver improved underwriting results are bearing fruit. And we've already taken actions to improve our property book, including the exit of US retail property and insurance at the beginning of 2017, and additional portfolio enhancements at the January '18 renewals across the portfolios. Thus we believe our property portfolio is better positioned today than it was last year.

Beyond financial results, it was a stellar year in terms of organizational progress for AXIS. We took bold actions to enhance the quality of our underwriting, expand our franchise, and establish leadership and relevance in key markets across the globe, including recruiting top talent, enhancing our data analytics capabilities, opening new offices, increasing third-party capital and closing on the acquisition of Novae.

With regard to Novae, notwithstanding the impact of the record third quarter cats, our experience to date gives us confidence that all other outcomes will exceed our initial expectations. The early stages of the integration are going well. The market has welcomed our new position as a top 10 player in the London market for global specialty risks, and indeed, we were able to control substantially all of our renewals since the merger. We secured finality on the 2015 and prior reserves. We now believe synergies will exceed our initial estimate of $50 million, approaching $60 million by 2020, and pricing conditions are much better than we expected when we developed our initial projections. We are thus very optimistic that Novae will deliver substantial strategic and financial benefits to AXIS.

Through all these actions, we completed in 2017 our transformation from an intelligent provider of capacity for volatile lines in a hard market to relevant and respected leader in key core markets, including top 10 positions in the US wholesale E&S markets, North American professional lines and the London market for global specialty lines while we're a top 15 global reinsurer of P&C lines.

We've never been better positioned with our clients and partners in distribution, nor had more tools at our disposal to deliver improved results to our shareholders. We're also encouraged by recent changes in market conditions, which I'll cover after Pete reviews our financial results in more detail. Pete?

Peter Vogt {BIO 17059745 <GO>}

Thank you, Albert, and good morning everyone. During the quarter, we generated a net loss of $38 million with an annualized ROE of negative 3.3%. Our operating income for the quarter was $20 million with an annualized operating ROE of 1.7%. The drivers of the difference between our net loss and operating income for the quarter were the following items not included in operating income; a tax expense of 42 million related to the revaluation of our net deferred tax assets associated with US tax reform, and transaction and reorganization related expenses of 21 million, and FX losses, although these are partially offset by gains in the balance sheet.

Of course, the quarter started with the closing of the acquisition of Novae on October 2nd, 2017, which means the full quarter of Novae results are included in this quarter's results, the first such quarter. A few items related to the acquisition warrant mention before I walk through the various aspects of our results including purchase accounting adjustments and the finality achieved with respect to Novae reserves for 2015 and prior years.

The purchase price for Novae of 616.9 million was allocated to the assets acquired and liabilities assumed of Novae based on estimated fair values at the closing date. In our 8-K of January 29th, we provided supplemental information on the historical results for Novae as well as P GAAP adjustments. We identified purchase intangibles including value of business acquired, VOBA, and finite lived other intangible assets. VOBA represents the present value of the expected underwriting profit within policies that were in force at the closing date of the transaction and was estimated at 108 million after- tax. Finite lived other intangible assets primarily related to distribution networks were estimated at 107 million after-tax. We also identified indefinite lived intangible assets related to Lloyd's of London syndicate capacity of 79 million after-tax and goodwill of 54 million.

The allocation of the purchase price to the assets acquired and liabilities assumed of Novae were based on estimated fair value at the closing date. Other notable purchase accounting adjustments included the write-off of the deferred acquisition cost asset of Novae balance sheet as the value of policies in force on that date are covered and considered within VOBA.

Consequently, our underwriting income in the quarter includes the earnout of premium attributable to the unearned premium reserve of Novae as of October 2nd without the recognition of associated acquisition costs. This stack would have normally been amortized in acquisition expenses. So we estimate that the consolidated acquisition costs on an as if basis would have been approximately $33 million higher, resulting in an approximate 22% acquisition cost ratio versus the consolidated 19.5% that was reported. I will discuss this impact to our two segments later in my remarks.

Amortization of intangibles at 53 million was mostly driven by amortization of the VOBA of 50 million. This expense affected the company's operating net income, but was not included in the results of the segment underwriting results. As we disclosed earlier, we expect the majority of the VOBA to be amortized during 2018.

Following the closing of the acquisition early in the fourth quarter, we advanced work initiated by Novae prior to our transaction with a view to significantly reduce reserve risk by transferring all 2015 and prior reserves in a Reinsurance to Close transaction. We completed this transaction, and in line with our findings during due diligence, this transaction generated positive economic value that is reflected in the opening balance sheet.

Moving on to a discussion of our results. Our operating income this quarter bore the weight of an elevated level of catastrophic losses, including the wildfires in Northern and Southern California and losses associated with an aggregate excess of loss reinsurance cover. Further, our accident year underwriting results were adversely impacted by higher attrition, which featured in particular lines already in run off. These factors were partially offset by increased net earned premium, continued favorable prior-year development and strong investment income.

Moving into the details of our income statement, our fourth quarter gross premiums written increased by 50% with an increase in both reinsurance and insurance segments. Our reinsurance segment reported an increase of 80 million or 65% in gross premiums written in the fourth quarter of 2017 compared to the same period in 2016. The increase was attributable to favorable prior-year premium adjustments and RIPs of 25 million, favorable current year premium adjustments of 18 million in our agriculture line, good organic growth in new business of 37 million spread among our number of lines, and the additional Novae reinsurance premiums in the fourth quarter of approximately 4 million.

On a year-to-date basis, our reinsurance segment reported gross premiums written of 2.4 billion, an increase of 178 million or 8% compared to 2016 attributable to our cat, agriculture property and motor lines, partially offset by a decrease in our credit and surety lines. We believe a year-to-date perspective provides a more meaningful view of premium growth.

Our insurance segment reported an increase in gross premiums written of 286 million or 47% in the fourth quarter compared to the same period in 2016 . This increase included gross premiums written of 241 million attributable to our recent acquisition of Novae. In addition, gross premiums written increased by 45 million or 7% attributable to good growth in our accident and health, professional lines and liability lines, offset by a decrease in our property lines, following our exit from US retail insurance operations last year, and a decrease in our marine lines largely driven by timing difference and norm [ph] renewals .

For the 12 months ended December 31, 2017, gross premiums written were 3.1 billion, an increase of 408 million or 15% compared to gross premiums written of 2.7 billion or 2016. This increase included gross premiums written of 241 million attributable to our acquisition of Novae. In addition, gross premiums written increased by 166 million or 6%, primarily for the reasons noted above for the quarter as well as an increase in our aviation lines associated with the acquisition of Aviabel completed earlier this year.

Consolidated net premiums written increased by 57% in the fourth quarter of 2017 compared to the same period in 2016. Insurance net premiums written increased by 48% compared to the same period in 2016. Excluding the impact of our recent acquisition of Novae, net premiums written increased by 11%. This growth reflects the increase in gross premiums written together with a decrease in premiums ceded in our property lines.

Reinsurance net premiums written increased by 93% compared to the same period in 2016, reflecting the growth in gross premiums written in the quarter, together with a decrease in premiums ceded due to timing of premiums ceded in the same period in 2016. On a year-to-date basis, reinsurance net premiums written were comparable to 2016. In 2017, we increased our premiums ceded to strategic capital partners, particularly in our cat, credit and surety, agriculture liability and pro lines, offsetting the growth in our GWP.

Our fourth quarter consolidated current accident year loss ratio increased by 8% -- 8 points to 74% compared to the same period in 2016. During the quarter, we incurred catastrophe and weather-related losses net of reinstatement premiums of 133 million or 11.2 points principally due to the California wildfires together with losses associated with an aggregate excess of loss reinsurance cover. Comparatively, we incurred catastrophe and weather-related losses net of reinstatement premiums of 59 million or 6.4 points in 2016.

Our fourth quarter current accident year loss ratio ex-cat and weather increased by 3.2 points to 62.8%. Our insurance segment current accident year loss ratio ex-cat and weather increased by 5.8 points to 61.4% from 55.6% principally due to an increase in attritional loss experience in our property lines, increased attritional loss experience in our aviation line, and increased attritional loss experience in the Novae marine line together with the adverse impact of rate and trend.

I would note that our attritional property experience was exceptionally good in the fourth quarter of 2016 and that impacts the quarter-on-quarter comparison by about 3.5 points. These negative factors were partially offset by changes in business mix within our A&H line where we responded to opportunities to write more limited benefits insurance business in the US, which carries a lower loss ratio, but higher acquisition expense ratio.

Our reinsurance segment current accident year loss ratio ex-cat and weather increased by 1 point to 64.6%, particularly due to the ongoing impact of the Ogden rate change on our motor lines and attritional losses associated with the legacy Novae discontinued lines. Year-to-date, our consolidated current accident year loss ratio increased by 16.7 points to 84.1, driven by a 14.8 point increase in the cat loss ratio. During the year, we incurred 835 million of pre-tax catastrophe and weather-related losses net of reinstatement premiums compared to 204 million in the same period in 2016.

After adjusting for these events, our current accident year loss ratio increased by 1.9 points to 63.7%, primarily driven by the Ogden rate change and higher year-over-year property losses. These two items had a 3-point impact on our current accident year loss ratio year-over-year.

We believe a year-to-date perspective, which is not impacted by the vagaries introduced from quarter-to-quarter distorting comparable period analysis provides a more meaningful view to our current accident year loss ratio ex-cat and weather. On a year-to-date basis, our insurance segment current accident year loss ratio ex-cat and weather increased by 1 point to 61.6 from 60.6, principally due to an increase in attritional loss experienced in our property lines, mainly in lines discontinued by AXIS together with the adverse impact of rate and trend. This was partially offset by improved experience in other lines. In fact, in aggregate, excluding property, the business delivered an improved current accident year loss ratio ex-cat and weather.

On a year-to-date basis, our reinsurance segment current accident year loss ratio ex-cat and weather increased by 2.9 points to 65.9 from 63, principally due to increased large loss experience in our property lines and the Ogden rate change in our motor lines. Here again, lines other than property and motor delivered improved year-over-year underwriting results. Turning to loss reserves established in prior years, our results benefited from net favorable loss reserve development of 57 million during the fourth quarter with 38 million attributable to reinsurance and 18 million attributable to insurance.

During the fourth quarter, acquisition cost ratio decreased by 0.9 points compared to the same period in 2016. Our reinsurance segment acquisition ratio decreased 3.2 points to 22.7% from 25.9%, primarily related to the favorable adjustments related to loss sensitive features and changes in business mix as well as the impact of reinstatement premiums adjustments earned in the quarter. On an as if basis, without P GAAP adjustments, the acquisition ratio would have been 24%. Our insurance segment's ratio increased by 2.1 points to 16.6 from 14.5, primarily related to business mix, partially offset by increased ceding commissions. On an as if basis, without P GAAP adjustments, the acquisition ratio would have been 20.6 points.

Our G&A expense ratio in the fourth quarter decreased by 5.8 points compared to the same period in 2016 relating to both segments, principally associated with a decrease in performance-related compensation costs as well as an increase in net earned premium. In the fourth quarter, fee income from strategic capital partners was 8 million included as an offset to G&A expenses compared to 7 million in the prior-year quarter. Our G&A expense ratio for the full year of 13.9 is low. Normalizing our G&A for unusual items throughout the year and considering a full-year impact of Novae, G&A of approximately 700 million for 2017 is a good base to use. This base would have produced a 14.9% G&A ratio in 2017 full year.

Our balance sheet is strong and today we have more sources of capital available to us than we've ever had in our history. AXIS is well positioned to continue to support clients across our portfolio in lines where we feel we can get an appropriate return on our capital. During the quarter, we issued 350 million of 4% senior notes. We used a portion of the proceeds from the issuance of senior notes to repay a Novae term loan and used a further portion of the proceeds from the issuance of senior notes to repay and redeem our senior notes due on April 1st, 2019.

As previously disclosed, we've suspended share repurchase for the balance of 2017. We expect this will continue through 2018. As was the case following other major cat loss years, we are focused on restoring our capital levels held prior to the 2017 catastrophes and Novae acquisition. We closed the acquisition of Novae during the third quarter of 2017. We are working diligently to implement our future-ready operating model to support our underwriting strategy.

We expect now to achieve run-rate cost savings of 60 million. We expect to achieve these savings approximately 30 million to 35 million in 2018; cumulatively, 50 million to 55 million in 2019 and the balance in 2020. We would expect to incur non-operating charges of approximately 50 million, of which 15 million has already been spent and most of the rest will be spent in 2018. To conclude, 2017 was a busy year. We're now looking forward and focused on creating value in 2018.

With that, I'll turn the call back over to Albert.

Albert Benchimol {BIO 2023727 <GO>}

Thank you Pete. Let me spend a few minutes going into the details of the market and the recent price changes we've seen across our business. As we expected, the market responded positively to the substantial cat losses and deteriorating profitability in other lines. Pricing started picking up in October and accelerated through December, which was the strongest month of the year with insurance pricing averaging 3.5% in that month. Not surprisingly, lines and markets that were the most affected saw the strongest price action.

The average insurance rate increase for the fourth quarter approached 3%. It was strongest in our US division where we achieved average increases of 6.9% overall with solid double-digit increases in E&S property and increases approaching 6% in casualty. In our international insurance division headquartered in London, the average rate change for the fourth quarter was 3.3%, but the range was very wide, including double-digit increases in cat exposed property and onshore renewable energy, down to modest declines in aviation and terrorism. On average, in London, specialty lines achieved rate increases of 4.3% while professional lines were up 2.2%.

Our US and Bermuda professional lines division was close to flat with two-thirds of the premiums renewing flat to up and the remaining still had modest declines. As in recent quarters, primary layers achieved price increases while pricing softened as coverages moved up the tower, reflecting recent loss experience. The positive market momentum continued into January across our insurance book where we renewed over $600 million of insurance premium, including both the legacy Novae and AXIS books at average rate increases of 4.1%.

The reinsurance markets also experienced broad improvement. As you've heard elsewhere, in the 1/1 cat renewals, we generally observed pricing in the flat to up 5% range in loss-free accounts and 5% to 15% in loss-impacted business where some exceptional examples of 30% price adjustments in some cases was required. As you know, the majority of the loss impacted cat book will renew later between April and July and we're optimistic that rate increases will continue through those renewals.

Property treaties are also responding with increases that are consistent with cat exposure and recent loss experience. We're seeing the beginning of price activity in other lines. Professional lines and casualty quota share treaties are generally renewing flat or at a 1 to 2 point reduction in the cede. Our overall January 1 quota share renewals in the US averaged about a point of lower ceding commission. In excess of loss lines, we're seeing average price increases in the mid-single digits with the exception of European motor excess of loss treaties that have averaged in excess of 30% in our case. This of course makes up for the year of unprofitable results that follow the changes in the Ogden rates and brings the profitability of that book back to acceptable levels. Overall, we believe the reinsurance business we do in '18 should deliver better technical results than the expiring book, absent unusual frequency or severity.

I would add that notwithstanding the higher property cat reinsurance pricing, cat business will be less critical to our net results than it was in prior years, as we are now ceding over 50% of our gross cat reinsurance premium, up from 42% in 2017 and continue to work with strategic capital partners to ensure we can provide substantial and consistent capacity to our cedings across a number of lines and geographies.

We currently have access to about $1.9 billion of third-party capital with about 55% dedicated to property cat reinsurance, and the rest across a variety of other lines. In 2017, we ceded almost $500 million of premium and collected $36 million in fees. This represents rates of growth of over 60% in 2017, and given our greater capacity available in '18, we would expect further growth in both these important metrics. With our strong balance sheet and access to substantial third-party capital, we are very well placed to take advantage of improved market conditions and leverage our enhanced market positioning to make the most of available market opportunities.

But while we welcome the much needed changes in market conditions, we are also determined to continue our ongoing efforts to improve our own profitability under any market condition. All of our actions, including the recently announced organizational changes to align our accident and health units to our core insurance and reinsurance businesses, the creation of a group underwriting and analytics unit, and the integration of our finance and IT functions into more centralized centers of expertise, are meant to increase our agility and efficiency in the marketplace and empower our underwriters, claims experts and actuaries to better serve our clients and partners in distribution, construct more profitable portfolios and deliver better outcomes to all of our stakeholders.

We're confident AXIS can do very well in this market. With our enhanced positioning, better tools and analytics and a focus on delivering stronger underwriting results, we believe we can construct a portfolio that delivers a double-digit ROE with lower volatility with improving results as the impact of discontinued lines fades away during the year and more recent business earns out through our income statements.

And with that, we'd be happy to answer your questions. Thank you.

Questions And Answers

Operator

We will now begin the question-and-answer session. (Operator Instructions) The first question comes from Kai Pan of Morgan Stanley. Please go ahead.

Q - Kai Pan {BIO 18669701 <GO>}

Thank you and good morning. So my first question, Albert, is on the pricing commentary, and it looked -- can you talk a bit more about the market dynamics in both traditional as well as alternative market and what gives you confidence the momentum can continue?

A - Albert Benchimol {BIO 2023727 <GO>}

Well, certainly if you look at the last four quarters, what you will see is that the rate of decline that we were experiencing in the first, second and third quarters of 2017 was already improving. I'm not saying we had increases, but the rates of decline were smaller and smaller as we were going through it. And essentially what we were seeing was the market already started to respond to what is obvious to all of us, which is that the business was simply not profitable enough and we needed to get paid more. 2017 fourth quarter, I believe, was -- and the catch was the momentum to really push everybody into thinking we need to do something, and we started seeing that in the fourth quarter, and as I mentioned, we started seeing a little bit more improvement into the first quarter. So our position has been that we are certainly not anticipating a hard market like we've had in the past. I think there is just too much capacity for that, especially in the cat world, but I believe that there is a real recognition in the industry that we need to get back to acceptable profitability. And given where the pricing is now, I think we need to see some more. It's not going to be 10%, 15%, 20%, 25%, that's not what we're talking about, but what we're talking about is I think that we need to continue to see, in some cases, mid single digits; in some cases higher, but I believe there is a recognition by brokers, by companies, and by insurance companies that that needs to happen.

The impact of the alternative capital, in my mind, is to dampen the increase in particular on the cat business. I think that the January 1 certainly answered all of the questions about the sustainability of alternative capital. It's there, it reloaded, it increased its desired price, but certainly not by doubling it, and so I think we're seeing a new normal with regard to alternative capital and catastrophe in particular. I think that this is likely the environment that we're going to continue seeing through 2018.

Q - Kai Pan {BIO 18669701 <GO>}

Great. As the pricing actually is improving gradually, but you will still continue pulling back on the property underwriting, especially you look at the PML, it's reduced by 20%. And could you talk about the philosophy behind that and would that impact your overall business mix that would be making your like a underlying combined ratio or even higher going forward?

A - Albert Benchimol {BIO 2023727 <GO>}

That's a fair question. I think that we have been working on our property and property cat book for a number of years now, reducing the overall exposure. So if you look at PMLs in general, they are a multi-year reduction in PMLs. I would like to split our property strategy, if you would, in two. One is in the property book in the insurance and the other is in the cat. I think the property book in the insurance is one where we've been working very hard to change the nature of that book to improve the profitability of that book and to reposition it. And one of the issues that you will see in 2017 is increases in the experience in property, but a large part of that loss comes from business as we've identified earlier that we exited at the beginning of '17. So a lot of the negative experience that we had in 2017 is actually down to discontinued property lines, which will have a significantly lower impact in 2018.

We believe that with regards to the insurance book that we will actually be able to improve our overall underwriting results and our overall underwriting of -- not just for property, but for insurance in general with regards to a change in our approach to property. So I think that's in a good place now and will continue to improve as we apply our new tools and approach to pricing and construction to the rest of the book.

I think with regards to reinsurance, that's one where we are taking our cat exposure down overall, and I think there you are right to the extent that you are writing less cat premium. In a non-cat year, you are not going to do as well as somebody who writes more cat premium, but we believe that overall we will end up with a portfolio that will have better ROEs. Let's be honest. Where the world is right now with the alternative markets, driving the price for cat, cat is no longer offering insurers strong double-digit returns. And so we have to make sure that we allocate our capital appropriately for the risk and returns that are provided by the cat business.

Q - Kai Pan {BIO 18669701 <GO>}

Great. Last one, if I may on tax reform. You cede about 20% to your offshore affiliates and how do you change that program and because you said you see no material impact to your overall effective tax rate going forward?

A - Albert Benchimol {BIO 2023727 <GO>}

Pete, why don't you take that?

A - Peter Vogt {BIO 17059745 <GO>}

Hi, Kai, this is Peter. If you look at our book of business, today we're about over $6 billion in premium. About 2 billion of that's coming out of North America, and as you note, about half of that was ceded to -- was ceded offshore in 2017. What we have done is cancel those quota share treaties, and so now all 2 billion of that premium will stay in North America. We don't see a real impact to our ongoing tax rate because the billion-dollar one, is we're talking about 15% of our overall portfolio. So it's not a substantial -- it's an important part of our operations, but not the majority of our operations. But I would also tell you that the half of the business that we're staying in the US now has a reduced tax rate from 35 to 21 and so the business that's staying there will achieve a lower tax rate. And we don't expect that overall when we aggregate it all up, we'll see a material impact in our tax on a go-forward basis.

Q - Kai Pan {BIO 18669701 <GO>}

Is 4% still a good run rate?

A - Peter Vogt {BIO 17059745 <GO>}

We don't like to give a forecast on a go-forward, but I would say we should be consistent to what we've seen in the past.

Q - Kai Pan {BIO 18669701 <GO>}

Okay. Great. Thank you so much.

Operator

The next question is from Elyse Greenspan of Wells Fargo. Please go ahead.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Hi, good morning. Thank you. First couple of questions, following up on some of the market commentary. How much did your business potentially grow by on the reinsurance side at January 1? And from the commentary that I've been hearing in the market, it seems like part of the reason that people think momentum might continue to June and July is because of multi-year covers that potentially haven't gone up for renewal. How big of a portion of AXIS' book is multi-year covers? And do you share that view, I guess, that business written on a multi-year or some business that's not coming up until June or July, do you think that we'll see the same level of price increases we saw at January 1?

A - Albert Benchimol {BIO 2023727 <GO>}

So that's multiple questions. Let me deal with one at a time. I think with regards to the reinsurance book overall, I think if you look at it year-over-year, and the first thing that we do is we look at the expiring treaties, we adjust them for FX, which obviously given the weakening of the US dollar in the last 12 months, that was a little bit more than in the prior year. But in US dollars, I would say that we had expiring premium of about 1.5 billion and we renewed about 1.5 billion. So there was a fair amount of movement in our books. There were some cancellations and non-renewals. We increased our share in some; we decreased in others. We had some new business, but the net of it all is approximately a flat book year-over-year.

With regards to pricing as we go forward, I would say two things. One is, we didn't see as a percentage as much increase because most of the book that was renewed in January 1 was essentially European and with less experience. The books that you are going to see in April and May, June are going to be more cat-exposed. So by definition, you'll see more of those 10%, 15% plus increases coming through simply because that's consistent with what we saw in January 1, but with the appropriate mix.

I think your point on multi-year treaties -- but I would say the following on multi-year treaties. If you look at pricing in cat in particular, where we are now, given where the rates are, we're probably somewhere in late '15, early '16 pricing, right? So it's not like we've made a huge recovery yet. I still believe that there should be more to go, but if you had a treaty that was priced in '14 or '15, it's probably at levels that are not inconsistent with what you see today. So those multi-year treaties might actually renew flat because they didn't take the dip-down, but they're not pricing the correction either.

So I think you really have to take a look at where those multi-year treaties were written, what happened in those lines of business in the interim. And I don't think it's a foregone conclusion that you're going to see material increases in multi-year treaties. I would say that in our own experience. First of all, we wrote less multi-year business in '17 than in '18. So we have less of that, but when you look back on the last four years, last four, five years, and you look at the multi-year business that we wrote, on a net basis, that was a net positive for AXIS because in the last five years, we were able to lock in prices for two or three years in some cases when the annual renewals were actually done at lower prices. So multi-year treaties can be a very good way of managing the overall profitability of your book. I think we did it well, but I wouldn't read any immediate foregone conclusion until you dig deeper into when and in which lines those multi-year treaties were written.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay. That is helpful. In terms of some of the purchase accounting adjustments as we think about '18, you guys talked about a $33 million benefit going to acquisition costs in the segment level. Is that something that we'll see come through as a benefit also in 2018?

A - Peter Vogt {BIO 17059745 <GO>}

Hi, Elyse, this is Pete. Yes, we will see a benefit to the acquisition costs come through through '18. It will be a little bit lower because we wrote that $209 million of the Novae DAC [ph] off when we closed its balance sheet on October 2nd. So we'll see a number come through. It won't be that exact number. It's going to earn off in relation to their unearned premium reserve at that point, but we will see a benefit come through there. So we'll keep you in mind with that as we go through the year, but we will see our acquisition cost ratio be a little under what I would call a normal run rate through the year.

Now, I will say that offsetting that, the VOBA, which we disclosed a couple of weeks ago of 171 million amortization in 2018, we'll also show that running off each quarter. I will tell you that the VOBA, we do expect to amortize about 65% of that in the first half of the year, probably split evenly between the quarters with a little bit more in the first quarter and the other 35% running off in the second half of the year with again a little bit more in the third quarter than the fourth quarter.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay, that -- and then as we think about 2019, I guess just because of the P GAAP adjustments, the acquisition ratios would go up higher because we won't see the benefit come through.

A - Peter Vogt {BIO 17059745 <GO>}

Yeah. When you -- if you -- when we get to '19 and we're looking year-over-year, it will look higher because by then we'll get into, like I'll call it, a run-rate state, which is why I think what we'll do is continue to give you some guidance as we go through the quarters this year on what a real as is acquisition cost run rate is.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay, that's great. And then at the start of the call, you guys mentioned kind of reaffirming, and if not, more positive about the Novae deal than when you announced. I know you had pointed to some level of accretion figures in year one and year two. Did that take into account the potential at this point there is probably some lower level of investment income due to the reserve to close deal or if maybe the higher expense is offsetting that. I'm just trying to think through the modeling impact of the reserve to close as well as the higher expenses as we think about 2018.

A - Albert Benchimol {BIO 2023727 <GO>}

Yes, Elyse. I think that when we look at Novae overall, we really do believe today that we're going to get better than we actually projected both strategically and financially. And let me give you a few insights on that one. So we've now been kind of inside the doors of Novae since July of 2017, and I can tell you that we have found absolutely no negatives. One of the things that people are always concerned is once you get inside. We have found no negatives. In fact the staff is very strong. We've been able to build a great team, which is the best of both and I feel very good about that.

One of the things that we model, of course, is we're going to lose some business. I can tell you that to date we haven't lost any real business, and we've maintained control of substantially all of our renewals. I want to be clear. Some of those renewals, we chose not to renew for all the right reasons, but it was really under our control. Secondly, I would say that when we did our projections, we thought this was going to be a flattish year for pricing and we're now looking at mid-single digits pricing. So I would say that the pricing assumptions are better than we originally modeled. The synergies, as we'd pointed out and we thought would be about 50 million. We thought -- we think now they are going to be about 60 million. So that's a positive.

And with regard to the RITC, Elyse, you're absolutely right. We are thinking that the transfer of the premium probably makes for low single-digit investment income offset, but when you think about what that means in terms of finality on the reserve and reducing reserve risk, we think that was a good trade for us. So net net, you're right; probably the higher synergies and the investment income kind of close to offset each other and everything else is a net positive.

Q - Elyse Greenspan {BIO 17263315 <GO>}

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

A - Albert Benchimol {BIO 2023727 <GO>}

No problem.

Operator

The next question is from Josh Shanker of Deutsche Bank. Please go ahead.

Q - Joshua Shanker {BIO 5292022 <GO>}

Yes. Thank you. Albert, you talked about the increases in the motor book and how that book has now reached pricing adequacy. To what extent are you maintaining business and lines that are not currently at pricing adequacy because you believe over the longer term they will be adequate as pricing evolves to a proper view?

A - Albert Benchimol {BIO 2023727 <GO>}

Josh, I'm sorry. I just want to make sure I properly understand your question. Are you asking essentially about staying in certain lines, but temporarily reducing premiums? I'm not sure I understand.

Q - Joshua Shanker {BIO 5292022 <GO>}

Or staying in certain lines even though they are inadequate because you have a longer-term view that they won't be inadequate forever.

A - Albert Benchimol {BIO 2023727 <GO>}

Okay. Well, that's a fair question. I think as you can see, there is a normal amount attempting to stay in a market and not to be ruled by the immediate market, but really take a look at what is it going to look like over the medium to long term. And of course, part of what we do as good insurers and reinsurers is, if we believe that a business is good longer term, but not currently, we manage down by either reducing our exposure temporarily or by more reinsurance or a number of things.

But there are times when you look at a market, and importantly you look at your own position in that market and you say, am I going to be a winner in this market? Are we going to generate strong and consistent profitability long-term? And if you realize that that market is not going to do that for you, you've got to take the tough actions. And I would say that over the last three years, we have done a number of these actions, and let me go through a few of them.

You of course recall that we got out of the Australian market where we realized that we didn't have the scale to succeed in that market. We got out of the Canadian retail property market. We just announced last year that we were getting out of the retail property and retail casualty markets in the US because we thought we had much more firepower, more potential in the E&S and wholesale markets. We announced in December that after many years of losses for the market in onshore energy, we weren't seeing the kind of progress that we wanted to see, so we were reducing that. So I think that we've made a number of calls on lines of business where we did not see long-term profit opportunity. And we will make the tough calls when we need to make that.

In other areas, we've practiced what I believe is good cycle management where we are reducing our shares, but staying in the market while we find ways to either improve our profitability or look for more improvement. If the improvement does not happen, we will take whatever action is necessary. But for the moment, I think that we've shown the right balance of cycle management in terms of reducing, but staying in markets that we think are good long-term, of taking the tough actions and exiting markets that we do not believe are good long-term for AXIS.

But also importantly, and we haven't talked about it, investing in new businesses and growing in new businesses that we believe are going to provide substantial opportunity going forward. We've already spoken about A&H being a success story for AXIS. And as we noted, we wrote $500 million of that business and it's profitable and we think that's going to continue. We've been doing great strides in new lines with great promise like renewable energy where we believe we're a top five in the world. We have leadership positions in cyber where we believe we're top five in the world. So there are also a lot of other lines with great long-term potential where AXIS has done very good work of implanting itself as a relevant and leading insurer in lines that we believe have positive futures.

Q - Joshua Shanker {BIO 5292022 <GO>}

Do any of those lines currently have pricing that's below adequate level of returns, but you're more confident longer term will resolve that?

A - Albert Benchimol {BIO 2023727 <GO>}

If you're asking are all of our lines delivering target ROEs today, the answer is no, but we are working on those both through pricing actions, portfolio construction, and other efforts to get them to where they need to be. And if they're not, we will take additional action whether that's either further underwriting actions or exits, but we will take care of that as we move forward.

Q - Joshua Shanker {BIO 5292022 <GO>}

Okay. Well, thank you for all your answers and good luck with all the changes.

Operator

The next question is from Meyer Shields of KBW. Please go ahead.

Q - Meyer Shields {BIO 4281064 <GO>}

Thanks. Just a couple of brief modeling questions. First of all, did the Reinsurance to Close arrangement have any impact on underwriting profits in the fourth quarter?

A - Peter Vogt {BIO 17059745 <GO>}

No, it didn't, Meyer. It was actually all pushed back to the opening balance sheet.

Q - Meyer Shields {BIO 4281064 <GO>}

Okay. Perfect. And second, historically, the excise tax on premiums that were ceded offshore from the US, were those reported in the tax line or in one of the expense categories?

A - Albert Benchimol {BIO 2023727 <GO>}

It's in the acquisition expense line. These are very --

Q - Meyer Shields {BIO 4281064 <GO>}

Okay. And then -- go ahead. I'm sorry.

A - Albert Benchimol {BIO 2023727 <GO>}

We put expenses that are tied to -- we put expenses that are tied to -- variable expenses tied to variable volumes are associated with the acquisition expense.

Q - Meyer Shields {BIO 4281064 <GO>}

Right. No, I'm not suggesting that it's inappropriate. I just wanted to know what it is up for in the model. And then third, just broadly speaking, we've heard some sort of inconsistent rhetoric about accelerating loss trends in some casualty lines. And I was wondering if you could talk about what you're seeing.

A - Albert Benchimol {BIO 2023727 <GO>}

I think certainly the most obvious places have been in commercial auto, and certainly we've seen that too. You may recall, Meyer, we are not very aggressive on commercial auto. It's a very small part of our book and in fact we reinsure it, I think, to 90%. So whatever adverse we've seen on commercial auto has not had a material impact on us. And it's also been the part of the casualty market that has accelerated the most in pricing. So that's happening.

I think what you will see, just to give you an even broader answer, is that there is certainly appropriate level of concern around casualty. I mean, we've got social inflation going on, we've got a lot of -- as the market, a lot of limits in casualty. We're seeing increased class actions on the professional line side. And so those are the kinds of factors that are making people recognize that we need better pricing in those markets. And that's what's been driving pricing in the casualty markets.

I will tell you that in fact in 2017, we did not grow as much as we thought we would in casualty because although we saw pricing increases, we did not think they were adequate for the rates that we -- for the loss trends that we were seeing. And so in fact, we slowed down our growth in casualty growth because we didn't get the pricing increases that we thought we should get. And that's improving a little bit now, but I can say that in '17 (inaudible).

And with regards to D&O and E&O, you are also starting to see some increases in the primary layers, reflecting the loss activity that we're talking about here.

Q - Meyer Shields {BIO 4281064 <GO>}

Great. Thank you very much. That was very helpful.

Operator

The next question comes from Jay Cohen of Bank of America. Please go ahead.

Q - Jay Cohen {BIO 1498813 <GO>}

Thank you. I guess for Peter, two questions. One is, can you talk about the new money yield you're seeing out there relative to your portfolio yield?

A - Peter Vogt {BIO 17059745 <GO>}

Yeah. Hey, Jay, it's Peter. Right now we're seeing our new money is getting invested at a slightly higher yield than we have on the overall book yield. Our new money yields about 2.7% and the overall book yields about 2.5.

Q - Jay Cohen {BIO 1498813 <GO>}

It's finally a good comparison, huh?

A - Peter Vogt {BIO 17059745 <GO>}

Yeah, yeah. We agree with that.

Q - Jay Cohen {BIO 1498813 <GO>}

Secondly, amortization of intangibles, there is a lot of moving pieces, and I did miss some of the call. So I apologize if you've answered this, but can you actually give us a sense of what the quarterly pattern will be over the next couple of years for this amortization?

A - Peter Vogt {BIO 17059745 <GO>}

Yeah. Probably we did talk about it a little earlier, Jay, but that's okay. The biggest part of the amortization is going to be the VOBA. It was in the fourth quarter, it was 50 of the 53 million. So we think about the VOBA, if you look at the disclosures we gave out a couple of weeks ago, we expect a 171 million of that to amortize in 2018 and I really think the -- we'll see 60 -- probably about 65% of that in the first half of the year, Jay.

Q - Jay Cohen {BIO 1498813 <GO>}

Actually I did catch that, sorry.

A - Peter Vogt {BIO 17059745 <GO>}

Yeah.

Q - Jay Cohen {BIO 1498813 <GO>}

Beyond the VOBA, I guess the other intangibles, the amortization is going to be relatively small?

A - Peter Vogt {BIO 17059745 <GO>}

Yeah. Actually if you go back to the disclosures we put out on the 29th, on page six, the disclosures, we actually give a by-year breakdown for the other ones, and they are pretty small because they amortize over such a long period.

Q - Jay Cohen {BIO 1498813 <GO>}

Yeah. That's helpful.

A - Peter Vogt {BIO 17059745 <GO>}

Okay.

Q - Jay Cohen {BIO 1498813 <GO>}

Thanks.

Operator

There are no additional questions at this time. This concludes our question-and-answer session. I would like to turn the conference back over to Albert Benchimol for any closing remarks.

A - Albert Benchimol {BIO 2023727 <GO>}

Thank you, operator, and thank you everyone for joining us. As Pete said, 2017 was a year with a lot of moving parts, but what I feel very good about is that we entered the year with a integrated company with Novae and the rest of our operations. I think we've started to see some of the benefits of our underwriting actions in '17 in terms of being able to demonstrate that our technical ratios ex-property were actually coming down even in the face of reduced pricing. I think that we are entering '18 with a very strong sense of purpose and improved market position and a sense that we can truly make progress and deliver on our improved shareholder returns. So I look forward to reporting to you on that in future quarters. Thank you for joining us.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.