S&P Capital IQ

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Old Republic International Corporation

NYSE:ORI

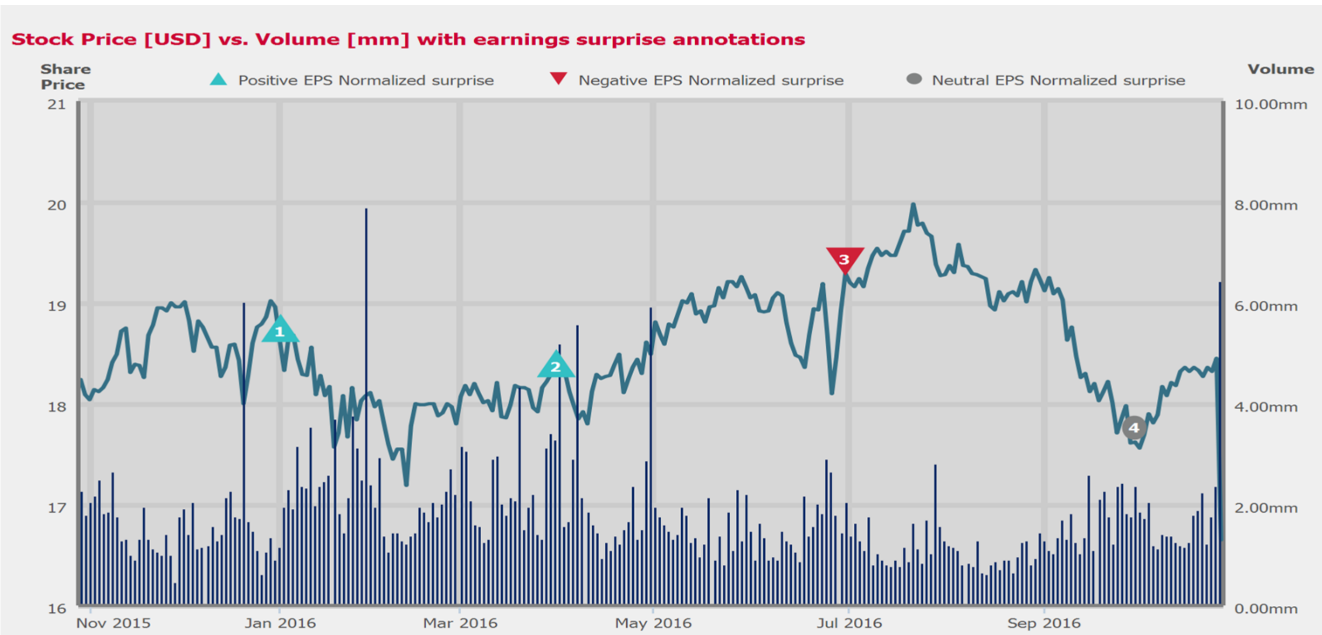
FQ4 2016 Earnings Call Transcripts

Thursday, January 26, 2017 8:00 PM GMT

S&P Capital IQ Estimates

	-FQ4 2016-			-FQ1 2017-	-FY 2016-		
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL	
EPS Normalized	0.31	0.43	▲38.71	0.32	1.34	1.46	
Revenue (mm)	-	-	-	1347.00	5848.00	5827.60	

Currency: USD
Consensus as of Jan-26-2017 7:30 PM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ4 2015	0.27	0.29	▲1 7.41 %
FQ1 2016	0.28	0.33	▲2 13.79 %
FQ2 2016	0.32	0.31	▼3 (6.06 %)
FQ3 2016	0.37	0.37	●4 0.00 %

Call Participants

EXECUTIVES

Aldo Charles Zucaro
Chairman and Chief Executive Officer

Craig R. Smiddy
President & COO of Old Republic General Insurance Group Inc

Karl W. Mueller
Chief Financial Officer and Senior Vice President

Marilynn Meek

Rande K. Yeager
Chief Executive Officer and President

ANALYSTS

Adam C. Liebhoff
Loomis, Sayles & Company L.P.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

John Eric Deysher
Bertolet Capital Trust - Pinnacle Value Fund

Presentation

Operator

Good day, and welcome to the Old Republic International Fourth Quarter 2016 Earnings Conference Call. [Operator Instructions]

I would like to remind everyone that this conference is being recorded, and would now like to turn the conference over to Marilynn Meek with MWW Group. Please go ahead.

Marilynn Meek

Thank you. Good afternoon, everyone, and thank you for joining us for the Old Republic conference call to discuss fourth quarter and year-end 2016 results. This morning, we distributed a copy of the press release and posted a separate statistical exhibit which we assume you have seen and/or otherwise have access to during the call. Both documents are available at Old Republic's website which is www.oldrepublic.com.

Please be advised that this call may involve forward-looking statements, as discussed in the press release and statistical exhibit dated January 26, 2017. Risks associated with these statements can be found in the company's latest SEC filings.

Participating in today's call, we have Karl Mueller, Senior Vice President and Chief Financial Officer; Craig Smiddy, President of the Old Republic General Insurance Group; Rande Yeager, Chief Executive Officer of the Old Republic Title Insurance Company; and Al Zucaro, Chairman and Chief Executive Officer.

At this time, I'd like to turn the call over to Al Zucaro. Please go ahead, sir.

Aldo Charles Zucaro
Chairman and Chief Executive Officer

Okay. Well, thank you, Marilynn, and we'll just begin by pointing out to a few key items from this morning's release.

As you can see, the results for the most recent quarter were at once very stable for the General Insurance business. Though a little disappointing in as much as we had anticipated, seeing a little more growth at the top of the income statement. But the total Title Insurance and RFIG run-off books, as you can see, more than made up the slack at both the top and the bottom lines.

As Craig Smiddy will note in a couple of minutes, our General Insurance business continues to improve, of course, very gradually on the underwriting front. And we remain very positive about our prospects in all of our other segments. We think that the North American economy, in which we do our business, is likely to remain in a relatively slow growth mode for a while longer but that our services in some of the more important sectors of that economy, such as housing and construction; transportation; trucking, in our case; health care; and in alternative market insurance solutions for large national accounts, that all of that should enable us to grow the overall consolidated business at a faster clip than the economy at large. And in addition to all this, we're managing the business with a very sturdy balance sheet that Karl will go over with some highlights in a few minutes. And that balance sheet is what allows us to, on the one hand, play for the long run, as we must in our business, and to compete on a level playing field with all comers in our areas of underwriting and related services competencies.

So with this preamble, I'll turn the discussion over to my 3 colleagues, and we'll go in order with you, Craig, and put some additional color to the numbers in the news release this morning, starting with General Insurance. Okay?

Craig R. Smiddy
President & COO of Old Republic General Insurance Group Inc

Okay. Thank you, Al. As the release points out, the General Insurance group experienced a small increase in net premiums earned in the last quarter and year-to-year. This result is from some increases in some areas and decreases in others. We experienced increased writings in commercial auto, mainly coming from rate increases earning through as well as increases in our warranty books of business. These increases were offset by some nonrenewed business in our large construction book as well as lower exposure units in our energy services book of business.

While rate increases are moderating on our workers compensation line of coverage, we continue to see fairly strong rate increases on the commercial auto line of coverage to offset the severity trends that we've observed and we've been discussing for some time now. Generally, we continue to experience strong persistency ratios on our renewal business as well as reasonable growth of new business, particularly from our newest underwriting operation that we announced in the first quarter of 2015. With that said, most of our underwriting operations continue to operate in what we would say is a very competitive insurance marketplace.

Getting to some specific results, the group's overall composite ratio declined to 98.2% in the fourth quarter of '16 compared to 99.5% for the same quarter last year. Year-to-date, this composite ratio is relatively stable compared to last year at 97.8% versus 97.6%. Our expense ratio of 24.6 for the quarter and 24.8 for the year is right in line with our 10-year average of 24.9.

As shown in the statistical exhibit, the commercial auto claim ratio declined in the fourth quarter to 76.8% compared to 80.3% in the fourth quarter of 2015, which is indicative of the compounding rate increases that I referenced earlier, which continue to earn through.

We'll continue to address the commercial auto severity that we're seeing through rate and risk selection until that claim ratio on this line comes down and is more in line with our historical experience in the low to mid-70s. In line with our previously stated expectations, we've experienced improved workers compensation claim ratios quarter-to-quarter and year-to-year as shown in the statistical exhibit. For the general liability line, the claims ratio is relatively stable quarter-to-quarter and year-to-year. And from both a premium and claims standpoint, all of the remaining lines of coverage performed very well and within our expectations.

So looking forward in 2017, we'll continue to focus on profitable growth within each of our underwriting operations, and that goes for each line of coverage that is written by those underwriting operations.

So short and sweet, Al, but I think that sums it up for the General Insurance group.

Aldo Charles Zucaro
Chairman and Chief Executive Officer

Okay. And I'm sure we'll get some more questions and you can add some more color as necessary. So Rande, why don't you pick it up and speak to the title business?

Rande K. Yeager
Chief Executive Officer and President

Sure. Thanks, Al. This is a really good report to give. The title group set records in numerous categories in 2016. Most importantly, pretax operating income of $85.6 million for the final quarter was an all-time record, and it represented an increase of 77.9% over last year's $48.1 million that we experienced in the fourth quarter. And for the full year, pretax operating income of $210.2 million also set another record and it represented an increase in excess of $43 million over 2015's record year.

Now related to fourth quarter, premium and fee revenue of $619 million, was up 13.2% compared to the prior year's quarter and also set an all-time record. Now 2016's total revenue of $2.2 billion was also an all-time record -- I could almost just reiterate this for the whole thing -- and surpassed 2015's record year of approximately $2.1 billion by 7.9%. Pretax operating margin for 2016 was 9.4% and, of course, that compares favorably to the 8% margin that we achieved in 2015.

The claims ratio for 2016's fourth quarter was a 0.4% standout, obviously, compared to the preceding year's 3.4%. Both 2015 and '16 reflect the continuation of more favorable claim trends for our recent policy years. The thing is we don't believe this is an aberration. There are a number of factors that have contributed to this favorable trend and I'd like to go over them with you because I think it's important.

First, the lending industry standards for mortgage lending have tightened considerably since 2008. That makes our environment safer. Second, our market share over that same period of time in both residential and commercial transactions has tripled. This has magnified our favorable results. Third, new technologies contributed to a safer workplace and it really minimized our title risk. And fourth, we have expanded and strengthened our auditing and control procedures. And quite honestly, looking into our crystal ball, and we have one, we expect more of the same for the foreseeable future.

I think one more thing that's worthy of some discussion is comparison of our operating results exclusive of the favorable loss reserve developments the past 2 years. Removing the favorable claims development from these years' results produces operating income of $154 million in 2015 and approximately $187 million in 2016, representing an increase of 21.3% year-over-year. And on a quarterly basis, the results are even more emphatic. Fourth quarter's 2016 operating income resulted in a 72% increase over 2015, excluding the favorable reserve development.

We point to this metric as an indication that the success of title operations are experiencing after eliminating the annual reserve development variability. As always, we can't predict the future. Interest rates have ticked up and inventories of properties are not as high as the industry would like to see them. But we feel that with the strengthening economy and the possibility of positive regulatory changes that 2017 bodes well for the Old Republic title business.

And with that, I'll turn it over to my friend, Al Zucaro.

Aldo Charles Zucaro
Chairman and Chief Executive Officer

Okay. So on that note from Rande, let me just talk a bit about the RFIG run-off business. As the release shows, the mortgage insurance portion of that run-off is moving along pretty much along the lines of the run-off model that we had penciled out beginning in 2011 or thereabouts. I mean, we tend to be spot on in terms of both premium levels as well as the bottom line, exclusive of any legal expenses that could not be anticipated.

So given our expectations for a fairly decent housing and mortgage banking market for the foreseeable future, we continue to think that this business is likely to run-off positively until the policy is currently enforced, continue to drop off the inventory, and we think that, that should occur by 2022 or thereabouts.

And so between now and then, we will certainly figure out, I'm sure, an appropriate way for the best long-term outcome for what we consider to be still a very valuable and certainly very viable operating franchise called RMIC.

On the other hand, the consumer credit indemnity, or the CCI portion of the business, as we call it, that continues to perform pretty much as anticipated. But here in a much more forceful way, the fly in the ointment is the 8-plus year litigation saga that we've had to deal with in regard to a commercial dispute we've had with Bank of America, and its ill-fated Countrywide mortgage banking subsidiary.

And some of you who follow us on a fairly regular basis may remember that at various times during the last couple of years in particular, we believe that a mutually satisfactory settlement could be had with Bank of America Countrywide. But obviously, that's not happened, as the 2 sides have remained far apart in their respective expectations.

So for the foreseeable future, it looks like we are going to continue doing battle and march all the way to the courthouse. Unless something gives, hopefully that will happen. As we've said in the past, this experience certainly with one of the nation's iconic banking institutions is a pretty sad commentary on dispute resolutions emanating from the very bad lending practices, which, as you know, were a root cause of the Great Recession. Nothing else to say, I think easy as she goes with respect to the RFIG run-off, and other than potential for claim settlements down the road, we don't think we should surprise anyone with the outcome of that run-off.

So Karl, if you want to take it over from here.

Karl W. Mueller
Chief Financial Officer and Senior Vice President

Thank you, Al. And as usual, let me make a few comments on certain key elements of Old Republic's financial condition and operating results, and let me first start with the balance sheet.

The high-quality liquid investment portfolio that we've consistently reported over the years remains intact. Fixed maturity and short-term investments make up approximately 77% of total invested assets. This diversified portfolio has an average maturity of just shy of 5 years, and it carries an overall credit quality rating of A.

Equity securities now make up a little more than 23% of the total investment portfolio, and that's up from 18% at year-end 2015, but virtually unchanged from our third quarter results.

Approximately 36% of the stock portfolio's growth this past year has -- or is attributable to market appreciation. Our continued focus is to seek investments in high-quality dividend-yielding stocks. At year-end, the portfolio consisted of about 90 individual securities that mostly represent blue chip companies, 1 REIT index fund and a series of utility company stocks. And we said during the third quarter call, we do not expect the allocation to equity securities to increase substantially from current levels.

Net investment income, as reported, appears relatively flat in both 2016 periods by comparison to a year ago. However, let me clarify a couple of important points about this. You may recall that during the third and fourth quarters of 2015, net investment income benefited from 2 nonrecurring special dividends that totaled $3 million for the fourth quarter and $13 million for the full year period. Of this total, $2.3 million and $9.2 million was attributable to the General Insurance group for the fourth quarter and year-to-date periods, respectively.

So absent these special dividends, our net investment income would have risen by approximately 3% on a consolidated basis for 2016 by comparison to the same period in 2015.

The second contributing factor that impacts the reported net investment income is the increased allocation to state and municipal tax exempt securities that carry a lower stated yield. These securities are reported in the balance sheet as held to maturity investments, and that balance has grown from $355 million at the end of 2015 to $974 million, or roughly 8% of the portfolio, at the end of 2016.

As a consequence, the pretax yield on the portfolio has declined slightly. Post-tax, however, the yield has reflected a small improvement year-over-year.

Consolidated claim reserves continue their favorable development during the final quarter of 2016. The effect was to reduce the reported loss ratios by approximately 1.6 percentage points for the fourth quarter and 1.3 percentage points for the full year. As noted in this morning's release, the General Insurance group experienced some unfavorable development in the fourth quarter of 2016. But despite this slight reversal from the breakeven development achieved through the first 9 months of 2016, the results are better when compared to the development experienced during the comparable 2015 periods.

The reserves in the mortgage insurance portion of the RFIG run-off business continued to develop favorably during 2016, albeit on a smaller scale as the book of business predictably shrinks.

And finally, the title group experienced favorable development of reserves as noted in the release and as Rande commented on earlier. Reserve adjustments were made in the fourth quarter as a result of our normal reserve review process, and reflect the continuing favorable loss development trends experienced at recent times in our book of title business. We should also draw your attention to Page 5 of the financial supplement that was referred to earlier and to the line that's titled Reserved to Paid Losses Ratio. Now this ratio measures the carried reserves at any point in time in relationship to the average of the past 5 years paid claims. The higher the ratio, the greater a title insurer's ability is to meet its obligations to policyholders. This table in the supplement shows the increasing ratio over the past several years that we believe is reflective of a very good reserve position.

Moving on then. The decline in operating cash flow reported on Page 5 of the release stems mostly from accelerated claim payments emanating from the General Insurance group, offset to a degree by improvements in both the title and RFIG run-off segments. Book value per share increased 14.5% this past year to $17.20 for all of the usual reasons, as summarized on Page 7 of the release. And finally, the capitalization ratios, as shown on the table on Page 7, are essentially unchanged from those reported at the end of the third quarter. So those are the highlights.

And with that, I'll turn it back to you, Al.

Aldo Charles Zucaro
Chairman and Chief Executive Officer

Okay. So there you have it. Our business is beginning to hum very nicely on most of the cylinders that pull it along. As Craig Smiddy noted a few minutes ago, the underwriting ratio trends the past couple of 3 years in General Insurance are moving progressively better, and that's a good augury for what's likely to be gradually and further improving profitability for General Insurance. We think that we'll gain a little more bottom line debt from the investment operations in General Insurance, but most of the gain in this segment has to come and is expected to come from the basic underwriting function, which is, of course, our main focus as managers of the business.

We think that in the past 3 years or so, we've done most of the heavy lifting that was necessary to address pockets of underwriting issues which had arisen out of the Great Recession years, dislocations across many business lines and as well as from a couple of books of business that we had brought on board in the last 10 years or so. But we're positive that these issues have pretty much been put to rest and so we can look forward to achieving some very good organic growth in General Insurance at a somewhat faster clip than the growth that is to be experienced by the North American economy.

With respect to title, boy, oh boy, I think we've got the wind at our back. We're able to compete with all comers as the third-largest title business in the country, as Rande said before. And we do have very good, very strong firepower from what we consider to be a world-class balance sheet that should help us navigate through all sorts of business climates.

The only thing that could de-escalate this positive momentum we have in title would be a serious setback on the housing and commercial real estate sectors, but we just don't see that happening in the next several years. So title should, as I say, hum along very nicely over the next several years.

Let's see, as we've noted, the run-off mortgage and financial indemnity segment business should continue to throw off some profits, albeit on a declining scale as a result of the policies enforced working themselves off the inventory. We continue to believe that the ultimate resolution of the Bank of America and a few other remaining legal disputes that we have should not be of calamitous proportions in any degree to our company's interests.

So when we wrap all of this up, that makes us confident that the business is going to move in a very positive mode and in line with our long-term strategy. And speaking of strategy, if you have a chance, you might take a peek at a couple of charts that are on our homepage of the Old Republic website. And there, you will see that starting at the end of 2012 and, again, as some of you who follow us are probably familiar with these 2 charts, we set ourselves a work plan, so to speak, which assumed that we would have to grow primarily, if not exclusively, on the basis of our General Insurance and Title Insurance business and achieve the results by 2017, i.e., 5 years later, achieve the same kinds of results that we had achieved in 2005, 2006. Both of which years were the most successful and most profitable years for our Old Republic family of companies. And those were years incidentally when the RFIG run-off business of today and, more specifically, the mortgage guaranty business accounted for some 40% of our bottom line and some very, very -- 3%, I think, of our capital. And most of that is gone, as you see in this release. And when you look at the chart, which -- the second chart on the website that shows where we've been and where we'd like to go, I think you will see that we're pretty much on track with respect to our expectations on revenues. And when it comes to the earnings, the pretax earnings that we had set for ourselves as an objective, I think we are -- we have to have a very good chance by the end of this year, by the end of that 5-year strategic period for us, to achieve the earnings that we did in fact, put on the board in 2005, 2006, which, as you will see, was between $680 million, $661 million roughly, call it $650 million.

So from where we sit today, I think we have a good chance of achieving that. There are never any guarantees as Rande said before, nobody knows what lies ahead. But based on our view of the business today, we feel very comfortable in our ability to come within range of those revenues and. more importantly, operating income objectives.
So we think it's all good when we look at our numbers and look at the business and its prospects based on what we have achieved through year-end 2016. So as was indicated initially, I think we reached the end of our comments, so we'll open it up to your questions and hopefully, we'll have good answers to them.

Question and Answer

Operator

[Operator Instructions] And we'll go first to Greg Peters with Raymond James.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

So just opening comment, I was -- towards the end of your comments, Al, I was looking at the slide on -- that you were referring to about your 5-year strategic plan. I guess at some point in 2017, you're going to roll out your next 5 years and, hopefully, you'll be as successful on achieving those as you were for this past period.

Aldo Charles Zucaro
Chairman and Chief Executive Officer

We'll do that probably in February or March of 2018, after we've got a handle on 2017 results.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Excellent. I wanted to -- I was going to focus 3 or 4 questions, the first probably in Craig's direction. I was looking at Slide 4 of your supplement or Page 4 of your supplement, and looking at that category where you talk about the 3 above coverages combined. And for 2016, Craig, as you noted, revenue growth, premium growth was challenging and yet, your benefit and claim ratio is getting close to the 10-year average. When I think not just to 2017 but I think about 2018, are we going to see a growth of those 3 main areas of coverage? It certainly seems like market conditions are putting downward pressure there. And then is 76%, which is a 10-year average, about as good as it gets or can you get it even lower?

Craig R. Smiddy
President & COO of Old Republic General Insurance Group Inc

Sure, Greg. I'm happy to address that. I guess your second part I'll address first. We would expect that those 3 lines combined perform in the low to mid-70s. So there's a lot of history in why that 10-year average is at the 76%. But our target is to have that perform, as I say, in the low to mid-70s. So we're still working to bring that down. We're not satisfied with where -- certainly where it stands currently. As far as top line goes, you're absolutely right, as I indicated in my comments that we generally are operating in a pretty competitive environment. However, as I also noted, we're getting fairly strong rate increases on commercial auto, so that will continue to contribute to the top line as we move forward. And in addition to just the organic growth, the other things that plug into what Al was saying, as the general economy grows, so will our book. You look, for instance, at the energy services sector of our business. And as I mentioned I think last quarter, our policy counts haven't really gone down substantially, but our exposure units have gone down substantially just because of the reduced work effort that is happening in those sectors. So as those pick up, we would expect to see premiums pick up commensurately. We have the policies in place and would expect to see the kind of correction that would offset the pressure that we've had over the last couple of years. And then as I also commented on, we are starting to see the premiums earn through from the underwriting operation we started at the beginning of 2015, and we already have a pretty good indicator on what we'll be earning through in '17. And I can tell you that we'll continue to see contribution from that. And then lastly, I would just add that I spoke earlier about our expense ratio and that it's pretty much consistent with the 10-year average. And the thing I would note is that the current expense ratio includes a lot of investment in operations to build product, to hire people, to put systems in place. That's across several of our underwriting operations. So as those investments start to bear fruit, we would expect those operations to continue to grow as well. So all of those things said, I think, will help us continue to move forward in a very positive fashion even though, as you indicated, there are market pressures out there, certainly.

Charles Gregory Peters

Raymond James & Associates, Inc., Research Division

Just 1 follow-up before I turn to another area. Were guaranty fund associations or assessments have any impact on workers comp or some of the other areas of your exposures?

Craig R. Smiddy
President & COO of Old Republic General Insurance Group Inc

Very small. Very, very small, negligible.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Excellent. Rande, real quick. I was looking at the fourth quarter direct orders opened and closed, and the closed number increased substantially versus the fourth quarter of '15, and there's growth in the opened number as well but not nearly as much as there was in the closed. Is there something going on there?

Rande K. Yeager
Chief Executive Officer and President

I think the only mitigating issue there, Greg, is that in '15, the CFPB rules were brand-new, looking at the changes that were made in October of '15. And so we were still catching up on -- with the lenders on trying to sort out the new rules and making sure that we were closely and in an appropriate way, to not violate any of the new rules or regulations that have been posted just a couple of months before. So that was it.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Got it. And then just to close out, the corporate and other line -- this is probably for you, Al. The corporate and other line showed year-over-year, nice improvement for the full year. I'm just wondering about what levers impacted the results for 2016 and what we should think about for 2017. And then in your comments about the continuing litigation, it's -- are you suggesting that there's actually a trial date that's been set that you think that you're going to -- that we can point -- look to as sort of here, it's coming, and we'll get some finality to that issue?

Karl W. Mueller
Chief Financial Officer and Senior Vice President

Well, Greg, this is Karl. Let me address the first part of your question and Al can touch upon the litigation matters. Within the corporate and other segment, that's where we house our small life operation that's fundamentally in run-off. And being a small book of business, it tends to be volatile, both up and down. And for this period, the results were more favorable than they were a year ago. So that's pretty much what was driving the corporate and other.

Aldo Charles Zucaro
Chairman and Chief Executive Officer

Plus we had some income from the funds.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

I'm sorry, I didn't hear that.

Aldo Charles Zucaro
Chairman and Chief Executive Officer

Plus we had some extra cash flow from operations that flowed to the parent company. And of course, we had the funds that flowed from the debt offering. As you know, what happens there is that you invest those funds, as we did, and so that shows up as investment income. And then you have the cost of those funds appearing as interest. And to the extent that what you're making on the funds exceeds what you're incurring on the funds, you've got a profit there.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Got it. Al, maybe you can just -- go ahead.

Aldo Charles Zucaro
Chairman and Chief Executive Officer

The combination of what Karl said and the strength. And then you wanted to know about whether we have a date certain by which we can expect to get a resolution of the Bank of America case in particular. And the way it looks right now, we're still dealing with an avalanche of paper coming from the lawyers and so you've got to sift through that. The best I can say right now is we're probably looking at the beginning of 2018 before we step into the courthouse.

Operator

[Operator Instructions] We'll go next to Adam Liebhoff with Loomis, Sayles.

Aldo Charles Zucaro
Chairman and Chief Executive Officer

Whom are we speaking with?

Adam C. Liebhoff
Loomis, Sayles & Company L.P.

It's Adam Liebhoff from Loomis, Sayles. I think just one question for Rande. If you could give us a little bit of more color on what was driving the top line in the title business. And I think just from the perspective of residential versus commercial, new purchase versus refi. And then I guess, a second question, you talked a little bit about the trade impact in the previous answer, but maybe you could just give us a little bit more quantitative information on what that impact might have been in 2016, and whether it's kind of been fully cycled at this point. I presume it has been.

Rande K. Yeager
Chief Executive Officer and President

Yes, I'd be happy to answer it. Yes, to start kind of backwards. Yes, I think we've sort of cycled through the CFPB issues. We had not only our direct operations, where we're doing closings for our customers on a direct basis, but our agents were working through that, and we were helping the agents. So that tends to slow things down and it may be pushed a little bit of revenue that may have been closed in the fourth quarter of '15 into the first quarter of '16, so that certainly had an impact. We had a lot of business we were doing in the Western Title group which is composed primarily of direct operations. And they really kicked it out of the field this fourth quarter, so things are clicking on the West Coast. You have to kind of dissect the country into different markets in terms of where you're strong and where the business is coming from and what's available. And we just happen to be, I'd like to say by design and strategically, in all the right places. We've targeted states where there's a lot of business and we've done very well in them. And so that overall influences our business quite a bit. And then in terms of just the markets that we're seeing, refinances have been declining but at the same time the residential markets, the purchase money markets are outperforming maybe what we expect it, and so it's -- when you add all those things up, the residential, the huge growth that we've had in the commercial arena more in the past 4 or 5 years than the last 8, like the residential arena, we've established ourselves there. So we're seeing a lot more business and you tend to see that stuff in the fourth quarter because commercial deals all try to get done by the end of the year. And there's a lot of extra activity that's preceding the election and trying to get things done, not knowing exactly what might happen. So they were dealing with the known as opposed to the unknown, and so we were a benefactor of it. And I don't think it's over with. We're seeing interest rates tick up a little bit, but I rely on the MBA for most of my statistics and try to temper that with some experts that have an opinion about the markets. And nobody sees huge rates increases and that's all good in the commercial or residential area. We might see the fed funds rate. I mean, they were talking this morning about maybe 3 increases this year. But I don't think it's going to affect us to a great extent and so we look forward to -- I'd like to say more of the same. I don't think you can set a record every quarter like we've been doing. But if we stay stable and keep you in our job and keep our heads down, I think that you'll see more favorable results from the title group.

Adam C. Liebhoff
Loomis, Sayles & Company L.P.

Okay. And just 1 or 2 follow-ons, if I could. I know that the commercial business can be lumpy at times. Are there any particularly large transactions in that $619 million number, because 13% growth is pretty strong. So that's number one. And then number 2, is there a cap to how profitable this business can be? I think you did about 9.5 or so pretax for the year but where could that go in an optimal situation?

Rande K. Yeager
Chief Executive Officer and President

Yes, I think as I may have said before is that we have seen a growth in the commercial units over the past -- more recent years, last 3 or 4 years, and that's really influenced what we see on the bottom line as far as commercial is concerned. I think that the commercial market is a little softer than it was. I mean, if you read everything, it would tell you that it wasn't quite as good as it was in '15, but our market was much better. And that's all market growth, it's not because of the market getting better and it's not because it's single transactions. It's numbers of transactions that we're involved in. Yes, we're involved in bigger transactions that produce more revenue per order transaction, but that's not the primary cause. It's just the numbers of transactions and the acceptability of Old Republic Title in that arena that has never been before. And what do I see as limitations on it? Really nothing more than our ability to get out and present ourselves in terms of the strength of our balance sheet and the strength of our underwriting and people in the field.

Operator

At this time, we have one question remaining in the queue. [Operator Instructions] We'll go next to John Deysher with Pinnacle.

John Eric Deysher
Bertolet Capital Trust - Pinnacle Value Fund

Back to the Title Insurance business, two specific questions and then 1 general question. What was the mix percentage-wise of refi versus new buy in the year? And was it trending one way or the other as the year progressed?

Rande K. Yeager
Chief Executive Officer and President

Yes, certainly as the year progressed, refinances tailed off a little bit, but it was much higher than we had anticipated going into the year. We thought we entered the year at, say, 50-plus percent, between 50% and 60%, when you were looking at individual months, and we expected, as did the industry, that those refinances would tail off to the 25%, 30% range maybe. And analyzing the business in our fourth quarter, and I can't talk about the marketplace, because I know the marketplace seems to be lower than what we're experiencing. But we have strong lender units, and we haven't seen much of a tail end. Looking at our direct operations on the West Coast and even in December and November, they were running 50% refi to purchase money transactions. So that's a really healthy mix. And I think I commented maybe in the third quarter about this, but the rate, as everybody believes and rightfully so, that influences whether you refinance your home or not is not necessarily the driving factor. The driving factor, I think, more has been numbers. You've got to have a good rate, which we have, and you've got to have equity in your home. And when people didn't have equity in their home, it didn't matter that the interest rates were down below 3%. They were running around 2.8%, 2.9%, variable rates at 2.6%. What mattered was could I get my hands on that money and is it less than I can cash out? Or can I cash out for less and I can go get a consumer loan for? So those are factors that play into refinance activity as well as just having a great rate so you can reduce your monthly payment. Some people are willing to stay a little bit longer. So I still think those are factors.

John Eric Deysher
Bertolet Capital Trust - Pinnacle Value Fund

Okay. So if I hear you correctly, Rande, for both the year and the fourth quarter, the mix is roughly 50-50?

Rande K. Yeager
Chief Executive Officer and President

Yes. That would be my guess. Now that varies by area, but that would be my best guess.

John Eric Deysher
Bertolet Capital Trust - Pinnacle Value Fund

Okay. And another mix-related question. What would the mix be between commercial and residential for both the year and the quarter on a percentage basis, roughly, between commercial...

Rande K. Yeager
Chief Executive Officer and President

Yes, we look at that -- yes, we analyze it all the time and that's important to us. And we've climbed up to almost 20% of our transactions revenue. Now not numbers of transactions but 17%, 18% commercial. So that's huge compared to where we were. If you look back 8, 9, 10 years ago, we were at that 5%. So it's quite a -- once you get a seat at that table, it makes a huge difference. And if you perform, it makes an even bigger difference. And by the growth that we've seen, I have to say that we're doing a good job at doing that.

John Eric Deysher
Bertolet Capital Trust - Pinnacle Value Fund

Was there any particular area of commercial that you can point to as being a source of strength for you in the commercial segment by type of property?

Rande K. Yeager
Chief Executive Officer and President

No. We get involved in absolutely everything, from wind farms to strip centers to apartment complexes, commercial-type buildings. It's just a mix literally of everything. And a lot of that is driven by law firms. And once they get accustomed to you, whether they're dealing with any type, any one of those different segments of the commercial business, your acceptability and the way you performed and get the deal done for them is what's important. So they don't direct a certain kind of business to you, it's just they're commercial transactions.

John Eric Deysher
Bertolet Capital Trust - Pinnacle Value Fund

Right. Okay. Well, that's helpful. And a more general question, there's been some talk in terms of Fannie Mae and Freddie Mac perhaps taking them off government life support. The stocks have obviously reflected that possibility. How should we think about that from your perspective on the Title Insurance business? How would that impact you if it went through?

Rande K. Yeager
Chief Executive Officer and President

That's a really interesting question, and I'd like to have discussions about that. And I tend to think that the mortgage lending industry will find sources to provide capital to support the lending market here in the United States. We're safe. I mean, you look at foreclosure rates at this point and we're not talking about the recession years, when we go back to '08, '09, '10, when we saw the really bad performance in terms of securitized mortgages. And so whether Fannie and Freddie change or whether they're there or whether they're strong, I think there's a lot of ability in terms of the market's dynamics to be able to provide money for mortgage lending. So we're a great place to invest your money. I don't care where in the world you live.

John Eric Deysher
Bertolet Capital Trust - Pinnacle Value Fund

So you think it would be positive if in fact they were taken off government life support?

Rande K. Yeager
Chief Executive Officer and President

I don't think it will hurt us one way or the other. I think people will still invest in Fannie and Freddie if it's a -- it they're -- they're not going to be as profitable as a shareholder, I guess you'd have to ask some shareholders. But I think that what they're selling is still going to be a good product.

John Eric Deysher
Bertolet Capital Trust - Pinnacle Value Fund

Right. Al, did you have any thoughts on that?

Aldo Charles Zucaro
Chairman and Chief Executive Officer

No, I echo what Rande just said.

Operator

[Operator Instructions] And it appears there are no further questions at this time. I'd like to turn the conference back to the management team for any additional or closing remarks.

Aldo Charles Zucaro
Chairman and Chief Executive Officer

Okay. Well, again, we're very grateful that all of you choose to attend these calls of ours and read the stuff we put out. And we're happy to embroider on it as well as we can. And so in that light, we expect things to be pretty even Steven. And we're looking forward to some reasonable normalcy in our business for the foreseeable future. And so in that light, we thought that we would be together once again in July, after we got our midyear numbers under the belt. And on that note, we'll bid you a good afternoon, and thank you again.

Operator
And ladies and gentlemen, that does conclude today's conference. Thank you for your participation.