

Markel Corporation NYSE:MKL

FQ1 2019 Earnings Call Transcripts

Wednesday, May 01, 2019 1:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ1 2019-			-FQ2 2019-	-FY 2019-	-FY 2020-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	9.52	7.99	▼ (16.07 %)	9.49	38.85	41.99
Revenue (mm)	1828.31	2472.49	▲ 35.23	2016.93	7734.45	8154.32

Currency: USD

Consensus as of May-01-2019 11:14 AM GMT

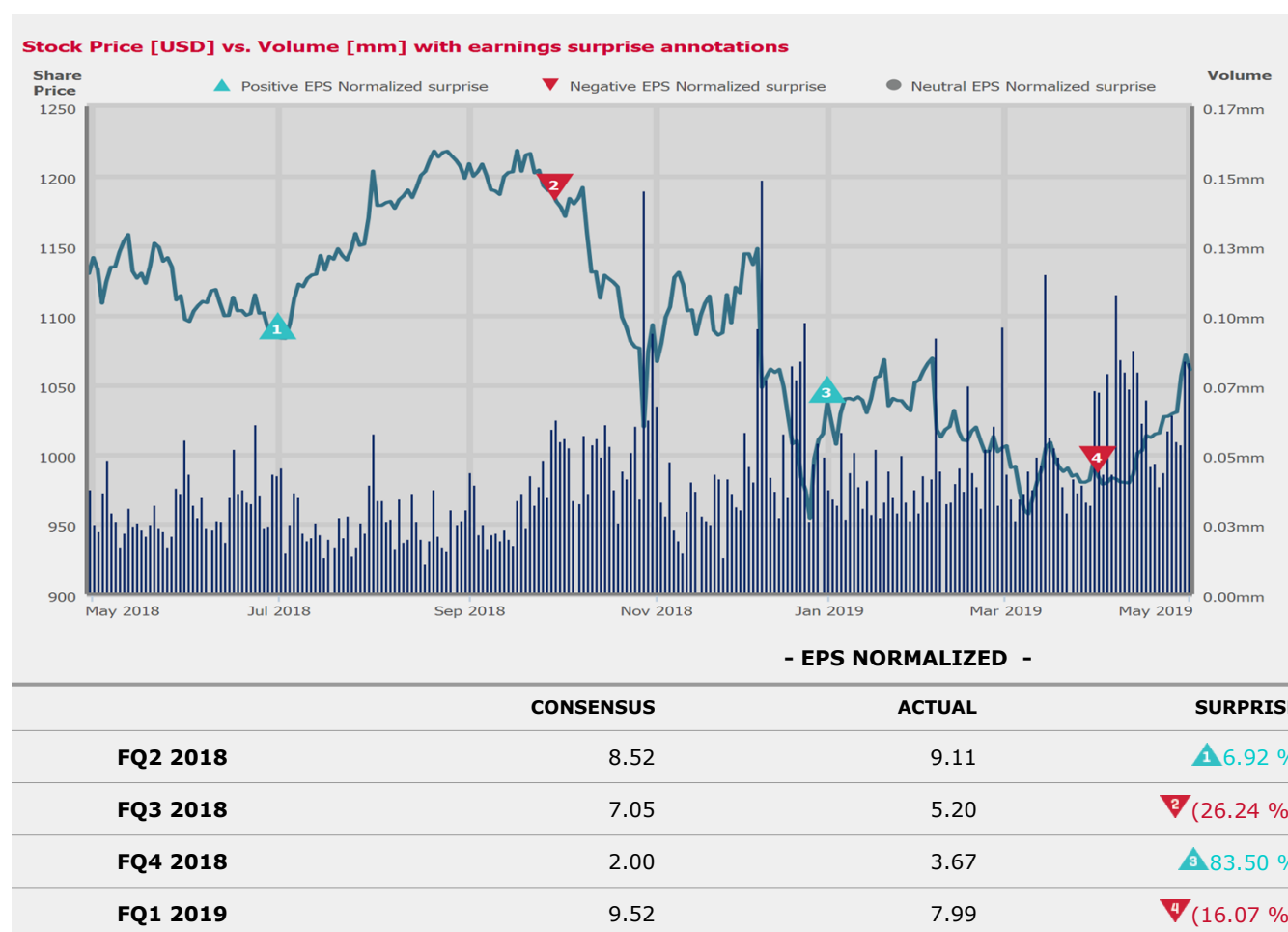


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Call Participants

EXECUTIVES

Jeremy Andrew Noble
Senior VP & CFO

Richard Reeves Whitt
Co-CEO & Director

Thomas Sinnickson Gayner
Co-CEO & Director

ANALYSTS

Jeffrey Paul Schmitt
*William Blair & Company L.L.C.,
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Mark Douglas Hughes
*SunTrust Robinson Humphrey,
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ATTENDEES

Unknown Attendee

Presentation

Operator

Good morning, and welcome to the Markel Corporation First Quarter 2019 Conference Call. [Operator Instructions]

During the call today, we may make forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. They are based on concurrent -- on current assumptions and options concerning a variety of known and unknown risks. Actual results may differ materially from those contained in or suggested by such forward-looking statements. Additional information about factors that could cause actual results to differ materially from those projected in the forward-looking statements is included under the captions, Risk Factors and Safe Harbor and Cautionary Statement in our most recent annual report on the Form 10-K and quarterly report on Form 10-Q.

We may also discuss certain non-GAAP financial measures in the call today. You may find a reconciliation to GAAP of these measures in the Form 10-Q, which can be found on our website at www.markelcorp.com in the Investor Information section. Please note this event is being recorded.

I would now like to turn the conference over to Tom Gayner, Co-Chief Executive Officer. Please go ahead.

Thomas Sinnickson Gayner

Co-CEO & Director

Good morning, and welcome to the Markel Corporation First Quarter 2019 Conference Call. This is Tom Gayner, I'm the Co-CEO of Markel Corporation. And it is my pleasure along with my Co-CEO, Richie Whitt; and our CFO, Jeremy Noble, to welcome you.

These calls are designed to give you a quick report on the current conditions, financial results and our thoughts on the business environment for the Markel Corporation. We appreciate your long-standing partnership and interest, as we continue to build your company over time, and we look forward to answering your questions at the conclusion of this call. The headline is that we're off to a very good start so far in 2019.

Trust me, at this point in the year, we're drinking coffee and going to work as opposed to any celebratory champagne. But I do think the quarter serves as an illustration of what happens around here when all 3 of our economic engines are firing.

Our insurance-related engine achieved underwriting profits and grew in total volume. We also made progress with our insurance services and insurance-linked securities operation, as we continue to learn some tough lessons while we build out those capabilities. Our investment engine produced a new record of recurring interest and dividend income as well as appreciation in the mark-to-market in the portfolio. Finally, our Markel Ventures engine earned record amounts of EBITDA and record revenues, and we ended the quarter with fewer shares outstanding than at the beginning.

Jeremy and Richie will give you more details on the relevant numbers in just a minute. Then I will offer a few comments on our investments in Markel Ventures Group. But I want to take just a moment to pause and reflect on what we continue to build at Markel. We remain dedicated to building one of the world's great company. We define that as the company with a win-win-win architecture for our customers, our associates and our shareholders, all win as we work together to provide products and services that make all of us better off. We're delighted to share a report full of vivid and easy markers that show the financial benefits of this approach.

We've also all been around long enough to have lived through quarters and years where the markers weren't so positive or as obvious as they were during the first quarter of 2019. Rest assured though that our process, our discipline and our values as described by the Markel style remain constant no matter what. Rest assured also that they work. I'd like to thank to more than 17,000 associates, our customers and you, our shareholders for your ongoing commitment and support.

Now I'll turn it over to Jeremy and Richie to review some of the details from the first quarter.

Jeremy Andrew Noble
Senior VP & CFO

Thank you, Tom, and good morning, everyone. As Tom just suggested 2019 is off to a solid start. Our results for the quarter reflect strong performance in our investment portfolio, largely driven by favorable movements in the equity market. We experienced organic growth within both our underwriting and Markel Ventures operations, and our results also reflect contributions from our recent acquisitions of Brahmin within our Markel Ventures operations and Nephila within our insurance-linked securities operation.

Turning to our results for the first quarter of 2019. Total operating revenues grew 57% to approximately \$2.5 billion in 2019. The increase was driven by \$612 million of net investment gains on our equity portfolio in 2019 resulting from favorable market movement. Additionally, revenues for our Markel Ventures segment increased 16% year-over-year.

Looking at our underwriting results, gross written premiums were \$1.7 billion for the first 3 months of 2019 compared to \$1.6 billion in 2018, an increase of 8%, which was attributable to higher gross premium volume in both our insurance and Reinsurance segments. The tentative gross written premiums increased 3 points from 84% in 2018 to 87% in 2019. This increase was driven by higher retention on our property product lines within the Reinsurance segment.

Earned premiums increased 5% to \$1.2 billion for the first 3 months of 2019 due to higher written premiums in our insurance segment, partially offset by lower earnings in our Reinsurance segment. Our consolidated combined ratio for the first quarter of 2019 was a 95% compared to 90% in the first quarter of last year. The increase in the consolidated combined ratio for the quarter was primarily driven to less favorable development on prior year's loss reserves within our insurance segment.

Now I'll cover the results for our Markel Ventures segment. Revenues for Markel Ventures increased to \$455 million compared to \$392 million a year ago. The increase in revenues was primarily attributable to higher revenues across our products businesses as well as fourth quarter 2000 (sic) [2018] acquisition of Brahmin. Operating income for Markel Ventures was \$30 million for the first quarter of 2019 compared to \$24 million last year. EBITDA was \$55 million in 2019 compared to \$47 million last year. The increase in both operating income and EBITDA for the quarter was primarily due to an increase in income attributable to certain investments held within our Markel Ventures segment.

Turning to our investment results. Investment income increased from \$108 million in the first quarter of 2018 to \$114 million this year. The increase was driven by higher yields on our fixed income portfolio and higher dividend income compared to the same period in 2018. Net investment gains included in net income were \$612 million for the first quarter of 2019 compared to net investment losses of \$123 million in 2018. As I mentioned previously, substantially all of our net investment gains in 2019 were attributable to the increase in the fair value of our equity portfolio during the period.

Net unrealized investment gains increased \$152 million net of taxes during the first quarter of 2019, approaching an increase in the fair value of our fixed maturity portfolio. Given our long-term focus, variability in the timing of investment gains and losses is to be expected. Looking at our total results for the year, our effective tax rate was at 21% in 2019 compared to 253% a year ago.

As I've mentioned previously, the impacts on management's decision to elect to treat 2 of our U.K. subsidiaries as U.S. taxpayers beginning in 2018 added \$99 million or 232% of the effective tax rate a year ago. Our estimated annual effective tax rate, which excludes this impact as well as certain other items that are infrequent or unusual in nature, was 19% in both 2019 and 2018.

We reported net income to shareholders of \$576 million for the first quarter of 2019 compared to a net loss to shareholders of \$64 million a year ago. And comprehensive income to shareholders for the period was \$732 million compared to a comprehensive loss to shareholders of \$175 million a year ago. Comprehensive income for the first quarter of 2019 was driven by net income, components of which I just discussed, along with the increase in the fair value of fixed maturity securities at the end of 2018.

Finally, I'll make a few comments on cash flows, capital and our balance sheet. Net cash provided by operating activities was \$19 million for the first 3 months of 2019 compared to \$58 million for the same period of 2018. Operating cash flows for 2019 reflected higher claim settlement activity in '19 and lower cash flows from our Markel Ventures operation. Also reflected in net cash provided by operating activities were net tax refunds received in 2019 compared to net tax payments made in 2018.

Historically, the first quarter is our lowest cash-generating quarter based on the timing associated with incentive compensation payment. Invested assets for the holding company were \$2.7 billion at the end of March versus \$2.6 billion at year end. Total shareholders' equity stayed at \$9.8 billion at the end of March, an increase of 8% from year end. We repurchased 36,000 shares in the first quarter pursuing to our outstanding share repurchase program. And lastly, I'll highlight that in April of this year, we entered into a new revolving credit facility to replace our existing facility, which was expected to mature later this year.

With that, I'll turn it over to Richie to talk more about our underwriting results.

Richard Reeves Whitt
Co-CEO & Director

Thanks, Jeremy, and good morning, everyone. Today, I'll focus my comments on our underwriting operations, and I'll also provide an update of our State National program services business and insurance-linked security operation. The headlines that I would lead off with for our insurance ILS and insurance services results is, we're off to a great start in 2019 with solid results and strong premium growth complemented by the growing benefit of continued incremental improvement in market conditions. So very positive, as we move into the new year.

So first let's talk about the insurance segment. Gross written premiums for the quarter are up roughly \$100 million or 9% compared to the first quarter of 2018. Premium growth for the quarter was driven by strong organic growth across several product lines. Most notably, our general liability, personal lines, professional liability and marine and energy product. Earned premiums for the segment are up 8% for the quarter with similar drivers as the gross written premium increases.

The combined ratio for the insurance segment was 95% for the first quarter of '19 compared to 89% in 2018. The 6-point increase in the combined ratio was driven by less favorable development on prior accident year loss reserves, primarily due to modest adverse development on our marine and energy and professional liability product lines this year versus more favorable development last year.

The favorable development in our marine and energy lines in the first quarter of '18 was largely attributed to favorable development from the 2017 CAT events versus minimal development on catastrophes in the first quarter of 2019. Higher earned premiums this year also impacted the prior year's loss ratio unfavorably. The expense ratio for the segment was flat compared to prior year with higher profit-sharing expenses and a lower benefit from seeding commissions offset by the impact of earned premium growth.

Next, let's talk about our Reinsurance segment. Our gross written premiums for the quarter are up \$21 million or 4% compared to the first quarter of 2018. The increase in gross written premiums was driven by new and renewal premium growth in our professional liability and workers' compensation product line, partially offset by lower premium volumes in our credit and surety and whole account product lines due to nonrenewals and timing of renewals on multiyear contracts.

As mentioned many times previously, significant volatility in gross written premium line can be expected in our Reinsurance segment due to individually significant deals and timing of renewals on multiyear contracts. Premium retention in the Reinsurance segment for the quarter increased by 7% versus last year driven by higher retentions in our Property product line. Earned premiums for the segment decreased by 7% for the quarter due to the runoff of earned premiums from a large specialty quota share treaty entered into in the first quarter of 2017 that was nonrenewed. This was partially offset by growth in earned premiums and professional liability to the increases in gross written premium. The combined ratio for the Reinsurance segment was 99% for the first quarter of '19 compared to 97% in 2018. The 2 point increase in the combined ratio was driven by higher expense ratio, partially offset by a lower current

accident year loss ratio. The increase in the expense ratio was driven by higher profit-sharing expenses and lower benefits from seeding commissions in the current year due to higher retention. The decrease in the current accident year loss ratio was due to favorable premium adjustments on our professional liability and Property product lines this year versus unfavorable premium adjustments in 2018.

Adverse development on prior accident year losses was down slightly in the first quarter of 2019. Both periods included adverse development from CAT events with \$13 million in adverse developments in the first quarter of '19, primarily for the 2018 CAT events and \$12 million in adverse development in the first quarter of 2018 from the 2017 CAT events.

Next, I'll make a few comments about our State National program services business. Gross written premium volume for our State National program services operations was \$527 million for the first quarter of '19, up 14% from the same period last year. This was driven by organic growth across several existing programs.

Just as a reminder, almost all of the gross written premium written by State National is deeded to third-party. Total seeded fee revenue for the -- were up 15% from last year due to the continued growth in program premium volumes over multiple quarters. Amounts for our program services operations are reported in services and other revenues expenses within our operating results. We're very pleased with our State National results, which continue to track very closely with our initial expectation.

Moving to our insurance-linked security operations. With the completion of the Nephila acquisition in November of 2018, we have significantly increased Markel's ILS operation. With our Nephila and Markel CATCo operations, we have approximately \$14.7 billion of net assets under management as of March 31, 2019. Total revenues from our ILS operations were \$53 million for the first quarter of 2019 versus \$17 million in the first quarter of '18, with the contributions in revenues from Nephila offsetting lower revenues from Markel CATCo due to lower assets under management and our decision to reduce management fees charged on sidepocket shares. These are shares which are restricted from redemption.

Operating expenses for the current quarter were impacted by cost associated with the internal review of matters in our CATCo operations, the effects of which were largely offset by lower retention and incentive compensation costs in 2019 compared to 2018. Amounts from our ILS operations are reported within services and other revenues expenses within our operating result.

With regards to CATCo, you are likely aware that on April 14, we issued a press release providing an update on the ongoing inquiries by the U.S. Department of Justice, U.S. Securities and Exchange Commission and Bermuda Monetary Authority into loss reserves recorded at and by our Markel CATCo subsidiary in late 2017 and early 2018. We noted that our internal review by outside counsel recently had been completed and found no evidence that Markel CATCo personnel acted in bad faith in exercising business judgment in the selling reserves and making of related disclosures during late 2017 and early 2018. The governmental inquiries are ongoing, and we continue to fully cooperate. At this time, we're unable to predict the duration, scope or results of these inquiries. At this time, we're also unable to provide any additional commentary on the ongoing investigation or pending or potential legal proceedings.

For more information, I would refer you to the disclosures found in our most recently filed 10-Q under the headings Contingencies, Legal Proceedings and Safe Harbor and Cautionary Statement.

Finally, I'll finish up with some market commentary. And I would say the themes that have been heard on others' calls, we are seeing as well. Market conditions continue to improve in an incremental fashion. While property pricing was somewhat disappointing in terms of increases for the January 1 renewals, pricing has continued to gradually improve throughout April. Japanese wind and quake renewals at April 1 broadly met our expectations for rate increases. The next important test of market discipline will be Florida renewals, which are currently in progress. At this point, it is too early to predict an outcome regarding the Florida renewal.

We are seeing low to mid-single-digit price increases in professional and casualty lines. But I would still categorize most of these areas as competitive. It seems very clear that the market is in transition with carriers reassessing their expectations for CAT frequency and severity, given events of the past 2 years

and professional and casualty results clearly needing rate increases after several years of decreases. About the only major line where pricing is declining at the moment is workers' compensation as a result of the good results over the last several years and its highly regulated nature. We are cautiously optimistic that this incremental rating environment improvement will continue during the rest of the year.

I want to thank you for your time, and now I'll turn it over to Tom.

Thomas Sinnickson Gayner
Co-CEO & Director

Thank you, Richie. My comments today will be quite brief. In our investment operations, we are at 11.3% on our equity investments during the first quarter and 2.4% on our fixed income holdings for a total portfolio return of 5.4%. Needless to say, I'd be happy to annualize those returns. Also needless to say, that will not happen. The good news and the main point is that those results are the results of a repeatable and dependable process. We continue to steadily increase our holdings of equities following our 4 part discipline of seeking good businesses with good returns on capital and not too much leverage with honest and talented management teams with reinvestment opportunities with capital discipline at reasonable prices.

We continue to do our best to execute against that strategy. And in our fourth decade of doing so, my report is, so far so good. In our fixed income operations, we continue to own a portfolio of the highest quality fixed income securities that we can find to hold against our portfolio of insurance liability.

In that process, we match up the duration and currency on both sides of the balance sheet to the best of our ability. We do not engage in exotic trading strategies or purchase exotic securities. There are no changes in policy or execution to report from fixed income.

In our Markel Ventures operations, we earned revenues of \$455 million during the quarter versus \$392 million a year ago and EBITDA of \$55 million versus \$48 million. The majority of this growth was organic with the balance stemming from including Brahmin Leather Works in this year's results. The vast majority of our companies are performing at high level and in keeping with our expectations.

We continue to march our way through the time where purchase accounting treatment can somewhat obscure the underlying economic performance of the businesses themselves. That said, this quarter demonstrates the upward direction of revenues and profitability from the Markel Ventures operations, and I expect to report more of that as time goes on.

To summarize, we are indeed off to a good start at Markel this year. As always, there are challenges and issue to resolve. As always, we remain dedicated to resolving them and continuously learning and improving the performance of your company. Thank you for your ongoing support and interest. And with that, we look forward to answering your questions. Andrea, if you'd be so kind as to open the floor for questions.

Question and Answer

Operator

[Operator Instructions] And our first question comes from Jeff Schmitt of William Blair.

Jeffrey Paul Schmitt

William Blair & Company L.L.C., Research Division

Growth in the U.S., organic growth there looks to be pretty good again at 9%. Could you maybe provide a little more color on the biggest drivers there and touch on what you're seeing in the -- for the E&S business?

Richard Reeves Whitt

Co-CEO & Director

Sure. Yes, like you said, 9% growth at -- very, very satisfying. Areas that we're seeing is in general liability, which is an area that we're very strong in. We're seeing increased demand there as well as some price increasing. In our personal lines operations, seeing some nice growth particularly in the Hagerty program. Professional liability, again, I think similar to others, we're starting to see the pricing environment improved around professional liability, and I think we're also seeing additional submissions. And then our marine and energy products are also continuing to see kind of an improvement in that market. E&S market is vibrant, I would say. I would still -- there is still competition, our people are still having to work hard every day. But obviously, if we're achieving 9% growth, which has some kind of price increases there, we're doing well. We're winning our fair share. So probably one of the more positive environments I've seen in a number of years.

Jeffrey Paul Schmitt

William Blair & Company L.L.C., Research Division

Could you comment on sort of the pullbacks by AIG, in Lloyds now, how that's impacting your business the E&S component?

Richard Reeves Whitt

Co-CEO & Director

It's -- I couldn't tell you how much either of those issues are impacting. But clearly, when market start to firm, it's a result of people reassessing risk that they're taking. So to the extent the competitors such as the 2 you just mentioned are reassessing risk and potentially re-underwriting, that tends to benefit a firming market. So it -- clearly, both those issues are impacting what's going on there. But those are just probably the 2 that get written about the most. That is probably happening in a lot of other places as well.

Jeffrey Paul Schmitt

William Blair & Company L.L.C., Research Division

Okay. And then could you discuss how the M&A environment looks? Or how the pipeline looks for Markel Ventures right now?

Thomas Sinnickson Gayner

Co-CEO & Director

Sure. For the last 3 or 4 years, at least, I lose track of this, I've been saying that prices are too high and private equities are very tough competitor, and we're not really making outbound phone calls, and that has been the case for 3, 4, 5 years, whatever. But in the course of those 3, 4, 5 years, we actually have been able to get a few deals done, and those have been on the account of inbound phone calls where -- because of what we're doing in Markel Ventures and the values involved in that, that is attractive to certain subset of people out there. So we continue to answer the phone when it rings, we continue to have some conversations. We're delighted with what we have and the beauty of the architecture of Markel is that we have organic growth opportunities. We can fund initiatives in the insurance business initiatives.

In the ventures businesses, we can put capital. In publicly traded securities, we can buy new businesses or we can buy back our own stock. We have 360-degree view of what we would do with the capital, and we try to act as rationally as we can to just allocate capital at the highest and best use. So it's a tough environment, but that's okay.

Operator

Our next question comes from Mark Hughes of SunTrust.

Mark Douglas Hughes

SunTrust Robinson Humphrey, Inc., Research Division

Very curious to get -- I know you said it's early on the Florida renewals, but wondering if there's any body language that you can speak at this point? You have had a little bit of an increase last year and some disappointment the prior year that you didn't see much after '17 storms. What's your -- little more on how you think things are shaping up would be appreciated.

Richard Reeves Whitt

Co-CEO & Director

Sure. Like I said, it's still early. A few programs have been completed and have been documented, I think, out in the press that they've been completed at increases, which seemed rational given what's happened in the last 2 years.

But again, it's still early days. I do think as often happens when market start to firm, renewals become later, because conversations are becoming tougher. So that suggests to me that we're probably going to see price increases, it'll still be determined whether people are happy with those price increases or not. It's a market and that's the -- market clearing prices have to be found. I will say that just property in general, if we look at our price increases month by month, and sequentially each month we're seeing improvement in pricing in Property. So we tend to believe the property market as well as other markets, we could continue to see incremental improvement as we go through the year.

Mark Douglas Hughes

SunTrust Robinson Humphrey, Inc., Research Division

In the medical professional liability, there's been some talk about severity, how do you see that?

Richard Reeves Whitt

Co-CEO & Director

Yes. I think absolutely. I mean that -- that was a line of business that was absolutely wonderful for us a number of years ago, and we've had to shrink that business substantially over the last several years. And we've been pretty frustrated that the severity and frequency that we've seen hasn't resulted in correction in that market. It seems like that is starting to get to a point where that could turn. I don't know that we're seeing a whole lot there yet, but clearly, the severity and frequency has been there and has resulted in us having to write a whole lot less of it. And it does appear, it's starting to cause some problems for the market.

Mark Douglas Hughes

SunTrust Robinson Humphrey, Inc., Research Division

You are not jumping in yet but keeping an eye on it?

Richard Reeves Whitt

Co-CEO & Director

We will -- Yes. Absolutely, we'll keep an eye on it, and when we feel like rates are supportive of the margins we need to make, we'll be there.

Mark Douglas Hughes

SunTrust Robinson Humphrey, Inc., Research Division

And then a final question on worker's comp. You think loss trends are still consistent with these pricing declines? Or are you or the market able to still stay ahead in terms of the decline in premium or rate versus the decline in losses?

Richard Reeves Whitt

Co-CEO & Director

Well, very clearly, the results in worker's comp have been very good for last several years. And so as you would expect, given the highly regulated nature of it, some of that margin is being clawed back. I would say at this point, we still believe that is a profitable line, but it doesn't take too many years of sequential declines before you can end up in a different position. I think we still see that being profitable today, but we're watching it carefully, and we're grudgingly giving up rate as we must.

Mark Douglas Hughes

SunTrust Robinson Humphrey, Inc., Research Division

And then in the ILS business, and I -- hopefully, I have this right here, it looks like excluding acquisition-related amortization, you're probably profitable. But with that amortization on a GAAP basis, you're a bit underwater. Can you share with us when -- is that intended to be run on a kind of a cash EPS basis so to speak? Or would we anticipate that within some period of time, that will be profitable on a GAAP basis as well? And that may probably be influenced by maybe some short-term expenses, and I'm sorry, if I missed the discussion of that. But would be curious to get your thought.

Richard Reeves Whitt

Co-CEO & Director

Sure. Sure. Well, I'd have to defer to our finance folks in terms of how the purchase accounting burns off. But the conversations that we've had over the years as it relates to Markel Ventures, it's really the same conversation here. There is the how the underlying business is doing, and then that gets somewhat clouded in the accounting by purchase accounting and things of that sort. And so you do have to sort of go back to an EBITDA concept. And as you stated, if you look at the cash, the business is profitable. It's probably a little bit behind where we would've hoped it would be, when we struck the deal with the guys at Nephila last August because a lot has happened since last August. Obviously, we had the 2018 events, which have created losses in the portfolios and sidepockets in the portfolios. So we're probably coming out of the gate a little bit slower, but we're very pleased with where we are. And we didn't enter that business for what it would do in 2019. We entered that business for what it'll do over the next 10 to 20 years, and we're very excited about what that looks like.

Jeremy Andrew Noble

Senior VP & CFO

Yes, let me add on to Richie's response there about purchase accounting. So in fact, yes, we could go back to Markel Ventures, and we've had numerous examples of how purchase accounting works. Actually, you can go back before that in the early days of Markel as a public company and the acquisition of Shand, and the purchase accounting that was done back in '87 and 1990 and the ongoing sort of confusion that seems to exist in the market between cash, money, earnings and GAAP accounting burns. So let me reiterate and be clear of the long-standing history and policy of Markel Corporation as we want good cash earnings for businesses that we buy and invest in. We underwrite, we think that way, we act that way on a daily basis. And then we follow the rules of GAAP accounting in terms of how we describe that in the financial reports. And the good news is that in the fullness of time, all those differences burn away. But in the early years of it -- of any deal, you'd really do have to slog through the financial statements and see how much amortization is there, see how much depreciation is there, what is real in terms of reinvestment requirements of the business, i.e., the depreciation. Typically, it is real, the amortization, not so much. That's the onetime purchase that affect.

And then the other bit of theory that I would say and why we expect this continue to be something you'll see at Markel going forward is that the insurance-linked securities business, we think, is a really good business. And one of the markers of a really good business is that they tend to produce results that are not tied to physical assets so much. We're in a world where intellectual property and things that are

intangible are becoming more and more of a piece of the total pie than things that are based on tangible assets. So when you buy a really good business like that, you probably have to pay more than what the tangible assets of the business are. And that creates the intangible assets portion, which is amortized and the portion of which is -- what we talked about the purchase accounting, the charges that you'll see. So expect more of that as time goes by from Markel. So expect we as the people running this business are looking at what the cash generated from what we're acquiring and operating continues to produce more good returns on cash that we lay out from the business.

Operator

Our next question comes from Mark Dwelle of RBC Capital Markets.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

Let me build on a couple of Mark's questions there just a second, while we're on the topic. So with respect to amortization, there is around \$40 million in the quarter. Is that a reasonable run rate for the balance of the year? Or is there some cliff to that, but it's going to drop off more quickly?

Richard Reeves Whitt

Co-CEO & Director

Repeating your question just to be able to pass this to Jeremy, the amortization that we're at roughly \$40 million in the first quarter. What's run rate of that?

Jeremy Andrew Noble

Senior VP & CFO

Yes, I think, Mark, it should be pretty consistent with that. There's nothing that comes quickly to mind that kind of sort of change that in the period. Obviously, that's the moved assets for the deals we did last year, most of that amortization.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

And then 2 other kind of, I'll call it, Nephila-accounting-oriented questions. Is there any significant seasonality to that business? Just given the type of things they write and so forth they are involved with writing? And then secondly, when you originally acquired CATCo, you set up an arrangement where any incentive bonus accruals or so forth would occur at the back end of the year depending on how the year unfolds? Is that the same sort of accounting you would use for any comparable arrangements at Nephila?

Richard Reeves Whitt

Co-CEO & Director

So the first thing, I'm not aware of any particular seasonality other than what are the large property renewal dates, which tend to be January 1, April 1 and the June renewals. But I think minimal seasonality, I would say, to the business. Obviously, we've got lower AUM right now as a result of losses last year and some sidepockets. Over time, we would expect that to clear up actually because there is more insurance and Reinsurance at Nephila. Sidepockets should resolve more quickly at Nephila than it would at CATCo, which is a retro product and takes longer to resolve. So that's kind of the -- I guess the first part of your question. Second part of your question, are you asking Nephila would earn -- depending on performance, could earn some performance fees, is that what you're asking about?

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

Correct. Yes, if they are fortunate to earn performance fees, would you accrue those in the fourth quarter to the extent earned or would you do them gradually? At CATCo, you had done it all kind of back ended. I was basically asking, if that's the same accounting practice plan for Nephila?

Richard Reeves Whitt

Co-CEO & Director

Yes, I think so. The year is not over till the year is over. And so I think we would wait until we were certain that any potential fees earned had crystallized, which would be at the stroke of midnight on December 31.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

Got it. Same question also, you mentioned higher property retentions within the Reinsurance unit. And I guess the question I'm going to ask, it's a little bit anomalous to what we're generally seeing. Was that something that resulted from some perhaps particular excess of loss treaty that resulted in that? Or is this a plan change, I suppose, in just general retentions across that segment such that we'd expect to see kind of the sessions be lower for the balance of the year?

Richard Reeves Whitt

Co-CEO & Director

Yes. In this is probably -- thanks for that question. This is probably worth talking about a little bit because I think this is going to be a theme as we go through the year. We at Markel have always been gross line underwriters, and so we expect the gross line we put out to be profitable. And as a result, we've always wanted to retain as much of that profitable businesses we could. We obviously need reinsurance partners to help us with the size of limits that we want to put out and with capacity and to deal with volatility. And so reinsurance partners are always going to be important to us, but we still -- at the same time, we have to balance that against the -- we want to retain as much of the profitable businesses we can.

Over the last several years, we've been moving more and more to enterprise-type covers away from covers that would be specific to lines of business. And as a result of that, it gives us the opportunity we believe to retain more of the premium. And so what you're seeing in Reinsurance this quarter, and you'll continue to see it in Reinsurance and likely to also see it on the insurance side, is where we are changing structures, moving away from quota share programs to some extent, moving more to enterprise covers, which should lead to higher retentions overall for Markel Corporation.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

It's very helpful. Then another question related to -- you mentioned the -- the Qs mentioned it as well, small amount of adverse development within a couple of products in the insurance segment. Can you just elaborate on that? And if possible, maybe size the what you mean by modest?

Richard Reeves Whitt

Co-CEO & Director

Sure. The adverse development, it was in professional liability and marine and energy. And we always trip up over how to discuss these things and when we write them up. Last year we had a pretty nice favorable development in those 2 lines of the business. This year we had a very modest adverse development, marine and energy was for the tune of \$3-or-so million, professional liability to the tune of about \$7 million. If they are pretty isolated areas, the marine and energy is largely related to a claim, 1 large claim. The professional liability is largely related to 1 program. So our process is deadly consistent each quarter. We do our actuarial analysis in our reserve reviews and prior year -- the prior year number falls out of that. I don't get too excited about 1 quarter worth of prior year, either positive or negative to what my expectations might be. It really matters -- we'll know more of a trend as we go through the year.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

Okay, that's really helpful, that's good additional color. Probably something that doesn't lend itself to normal 10-Q disclosures. So I would guess.

Richard Reeves Whitt

Co-CEO & Director

Yes, you guys certainly have so much patience in reading them.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

I am going to attempt one small CATCo question. Let me know if it's something that you can cover. I am really just interested in sort of what the mechanics of the next steps are from here. The shareholders voted to take early redemptions and the Q suggested that, that would commence around June 30. If you just elaborate kind of broadly, how that process would unfold? How -- what I'm trying to get at is how the AUM number might -- would behave, not obviously specifically, just in general, when would funds be disbursed? When would the AUM begin to decline, et cetera?

Richard Reeves Whitt

Co-CEO & Director

So the next date where deals come off risk is in June. And so we would expect some amount of cash and I don't have numbers in front of me, we'd have to talk to the CATCo team. We would expect some amount of cash to start to be returned to investors after those June deals roll off, and that would probably be after all the work is done in everything and probably be sometime in early fall that we would start to see that happen. The rest of cash really will depend on how sidepockets are resolved. One of the things we need to do as the managers work very hard with seeders to try to get them to get as good estimates as they can of their losses and then release capital, go back to the investors as quickly as possible.

So we're going to be working and we are working on that, and we'll continue to work on that as the year progresses and try to move cash back to investors from the sidepockets as quickly as possible. So you saw the number, 91% took advantage of the special redemption, so that will roll off. And then the thing that we're working on is when will we be able to consider raising funds for future investment strategies? And that's a little up in the air right now because we're still working with the government entities on the inquiry.

Operator

Our next question comes from [John Donat,] a private investor.

Unknown Attendee

I am a small time investor. And thank you for all the hard work you guys are doing. Before I ask the question, I'll tell you that as a small investor between Markel and Berkshire Hathaway, you 2 are so much -- the primary point of view touch to my private portfolio, personal portfolio.

And with that the question I would like to ask you, it has to do with State National. And before I ask the questions, let me give you a background. I just learned 2 days ago that Tesla, the company, the car company was starting the insurance business, and it was extremely surprising for me to learn at the same time that State National is the underwriter for this insurance in terms of capital, and I found that very surprising. Let me be honest about it, and so my question is I follow this company Tesla, for all the wrong reasons, unfortunately. And when I learned that State National is going to be an underwriter, assuming that's true, what is the incentive for Markel to get into this insurance business, and especially with Tesla, given the fact that Tesla, though itself want to be a cheap car, they have put up a lot of new technology up there, the things like driving, which hasn't been tested, which hasn't been indulged in water.

And my concern is that even though, there are -- they're still immersed in everything around how that technology is to be used, I have seen videos on the Internet where people are driving the car in the back. They are sitting in the backseat, and there is no driver in the front, and the car is being driven on its own. I have seen cars continuously running in garages and homes in some of videos and posts, so what exactly is the drivers for Markel to take on these type of underwritings? And what is the risk that you are taking on your book for this type of financial?

Richard Reeves Whitt

Co-CEO & Director

Sure. Sure. Thank you, John. Appreciate the question. Yes, State National -- maybe I'll step back just for a second. State National is a company that provides, I'll call it the plumbing to move risk to capital. They have the insurance companies, the ability to file the forms, set the rates and really the thing that attracted to us, to State National is they are quite honestly the best in the business in terms of offering that fronted model. One of the things we were very excited about with State National is we believe that, that plumbing, if you will, to move risk to capital is very important, as we're seeing all this innovation in the insurance industry. Often the people that have these innovative ideas have a hard time navigating the regulatory environment and able -- and being able to execute quite honestly on their innovative ideas. That's where State National can come to the table and help them.

In the case of the partnership with Tesla, State National is providing just that. They are supporting innovative solutions that Tesla has come up with, with risk-taking partners. State National does not retain any business, their model is not to retain any of the business, and so this business is being seeded on to Tesla's risk-taking partner. And I don't want to say any more than that because obviously, Tesla and the risk-taking partner, they have many things they probably want to say about the arrangement. We were just happy that we could step in at State National and assist them in what they were trying to do.

Unknown Attendee

Thank you for the clarification, and actually, you do now reinforce my confidence in your team, as you've stated that -- you are saying that is you're just helping them do the plumbing and get the fronting of it whereas Markel as a entity is not really taking any of the risks on the book. And that was actually, I'll be honest, was the biggest thing that for this particular company, independent of the new technology and the innovation that is coming along, it is not being tested adequately enough for it to be called mainstream and for all autos to go on the full self-driving and in 1 years' time, every auto will be picking up people and stuff. So there were lot of things that were, I think, truly futuristic, which is a good thing but unrealistic at the same time. And I am trying to again confirming that State National primarily is playing the role of helping companies like Tesla and other innovative companies take on the risk on their own or with their other partners but just initiating the products, so much appreciated.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to Tom Gayner for any closing remarks.

Thomas Sinnickson Gayner
Co-CEO & Director

Thank you very much. And we look forward to connecting with you soon. Talk to you next quarter. Bye-bye.

Operator

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

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