S&P Global
Market Intelligence

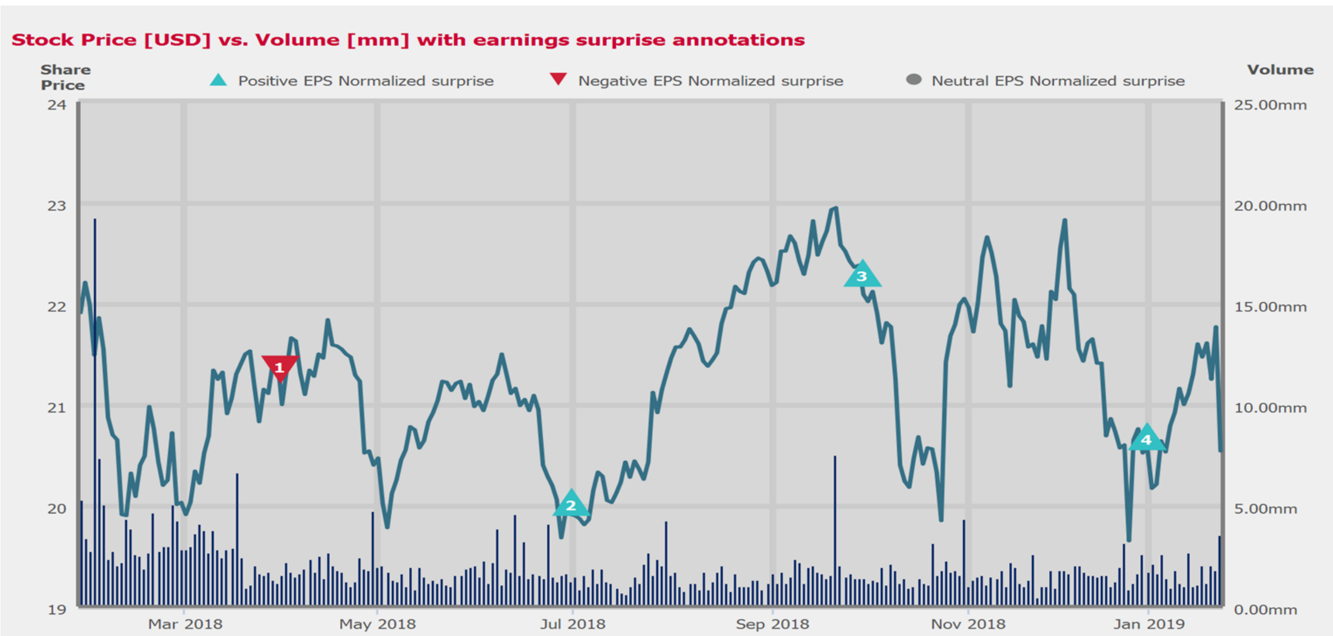
# Old Republic International Corporation
# NYSE:ORI
# FQ4 2018 Earnings Call Transcripts

## Thursday, January 24, 2019 8:00 PM GMT

## S&P Global Market Intelligence Estimates

| | -FQ4 2018- | | | -FQ1 2019- | -FY 2018- | |
|---|---|---|---|---|---|---|
| | CONSENSUS | ACTUAL | SURPRISE | CONSENSUS | CONSENSUS | ACTUAL |
| **EPS Normalized** | 0.44 | 0.45 | 2.27 | 0.38 | 1.88 | 1.86 |
| **Revenue (mm)** | 1574.00 | 1280.90 | (18.62 %) | 1483.00 | 6315.00 | 6021.80 |

Currency: USD
Consensus as of Jan-24-2019 4:40 PM GMT




**- EPS NORMALIZED -**

| | CONSENSUS | ACTUAL | SURPRISE |
|---|---|---|---|
| **FQ1 2018** | 0.41 | 0.40 | (2.44 %) |
| **FQ2 2018** | 0.44 | 0.47 | 6.82 % |
| **FQ3 2018** | 0.46 | 0.56 | 21.74 % |
| **FQ4 2018** | 0.44 | 0.45 | 2.27 % |

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# Call Participants

## EXECUTIVES

**Aldo Charles Zucaro**
*Chairman & CEO*

**Craig Richard Smiddy**
*President & COO*

**Karl William Mueller**
*Senior VP & CFO*

**Marilynn Meek**
*Investor Relations Professional*

**Rande Keith Yeager**
*Chairman & CEO*

## ANALYSTS

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

**Matthew John Carletti**
*JMP Securities LLC, Research Division*

# Presentation

**Operator**

Good day, and welcome to the Old Republic International Fourth Quarter 2018 Earnings Conference Call. [Operator Instructions] I would like to remind everyone that this conference is being recorded.

I would now like to turn the conference over to Marilynn Meek with MWW Group. Please go ahead.

**Marilynn Meek**
*Investor Relations Professional*

Thank you. Good afternoon, everyone, and thank you for joining us for the Old Republic conference call to discuss fourth quarter 2018 results. This morning, we distributed a copy of a press release and posted a separate statistical supplement, which we assume you have seen and/or otherwise have access during the call. Both of the 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 supplements updated January 24, 2019. Risks associated with these statements can be found in the company's latest SEC filings.

This afternoon's conference call will be led by Al Zucaro, Chairman and CEO of Old Republic International Corporation and several other senior executive members as planned for this meeting.

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

**Aldo Charles Zucaro**
*Chairman & CEO*

Okay. Well, thank you. And hello to everyone, and also thank you for participating in this update on Old Republic's business through year-end 2018. And as Marilynn just said, we've got several senior Old Republic executives that will participate in this visit of ours.

First, Craig Smiddy, who is our President, will cover General Insurance segment; Rande Yeager, our Executive Chairman in our Title Insurance business, will cover that part of the discussion; and Karl Mueller, our CFO, who will provide additional color about some of the more important elements of our company's financial situation.

So in approaching today's discussion, we're assuming as always that everyone has seen the earnings release of this morning. And moreover, as in other conference calls we've had over the years, we'll also be referring from time-to-time to some of the statistical information that we include in the financial supplement that we posted concurrently on the Old Republic website this morning.

In addressing our business activities since 2017 and going through all of 2018, it's obviously and abundantly clear that the changes that deal with income tax rates and their impact on our post-tax reported results as well as the changes that have been mandated by accounting rulemakers have had a comparative -- made, I should say, a comparative analysis of our performance a bit more, if not quite a bit, challenging this year.

And this is particularly important when it comes to sifting through so to speak the numbers to get to the fundamentals of our insurance business. So with respect to this year-end review, we thought of having Karl Mueller, our CFO, as I said before, to be first in this discussion and go over the critical highlights of the release from a pure financial perspective before we discuss the business in terms of its key operating components.

Generally speaking, I think that we've done a good job, even though I say so myself, of addressing the key elements of 2018 financial reporting, particularly on Pages 2 and 3 of the news release. And the challenge has been to provide as clear an apples-to-apples comparison of financial performance between similar 2017 and 2018 periods in the light of the changes and I might say aberrations in financial reporting and taxation that have taken place in the past 12 months or so.

So as I say, let me turn the discussion over to you, Karl, and I'm sure you can add color and context as we've discussed to the words and the numbers in the release. Okay. It's all yours.

**Karl William Mueller**
*Senior VP & CFO*

All right. And good afternoon to everyone. So as Al said, let me start by highlighting some of the key factors that affect the year-over-year comparisons of both pre-as well as post-tax income amounts.

First is the new accounting standard set forth by FASB that became effective the 1st of 2018. And that standard now requires the changes in the fair values of the equity portfolio, must be included with revenues in the income statement rather than being recorded directly to shareholders' equity, net of tax, as they have been in prior years.

Second is the lower federal income tax rate of 21% that became effective for 2018. Third is the revaluation of deferred tax assets and liabilities that were recorded to the income statement as of the end of 2017 to reflect the anticipated lower tax rate. And finally, the 2017 comparative results were affected by a number of nonrecurring events and related charges.

So this morning's news release includes additional narrative and some additional tables, in particular, those included on Pages 2 and 3 of the release, as Al mentioned earlier, that quantify the effect of each of these items. And we've done this in an effort to aid the evaluation of operating results on a relatively comparable basis.

As an example, the table on Page 3 provides comparisons of pretax results, which exclude the income statement impact of realized and unrealized investment gains and losses, as well as the effect of the lower tax rate. We believe this measure is most reflective of the business basic operating performance achieved for each of the periods that are presented in the release.

Moving on, elsewhere in the release we show the total cash and invested asset has declined slightly to $13.2 billion at the end of 2018 from the $13.5 billion reported a year earlier. This change was driven most significantly by the decline in net unrealized investment gains during 2018 and the cash dividend payments of $1.78 per share. And that amount includes the special $1 per share dividend that was paid to common shareholders in January of 2018. This decrease was partially offset by investment additions stemming from the positive operating cash flows, which, in fact, totaled $760 million for the year.

Total unrealized market appreciation dropped to $239 million at the end of 2018, compared to $755 million at the end of '17. And this was due, of course, to the overall decline in the stock market valuations that we just mentioned, particularly during the fourth quarter of 2018, as well as the result of the modest rise in market yields on the fixed income security portfolio throughout the year.

The composition of the portfolio remains relatively consistent with year-end 2017 as well as the earlier periods throughout 2018. Fixed maturity and short-term investment portfolio makes up nearly 3 quarters of total investments. Its credit quality rating remains stable, and the portfolio has an average maturity of slightly more than 4 years. And that's remained relatively consistent over a number of periods now.

Investments in high-quality dividend paying equity securities make up the balance of the portfolio. On a year-over-year basis, consolidated net investment income grew by 5.5%, due primarily to a rise in the cost basis of investment balances as well as a higher dividend income amount. On a consolidated basis, claim reserves continue to trend favorably during the final quarter of 2018 and for the full year 2018.

This morning's release, along with Pages 4 and 5 of the financial supplement, that are found on our website disclose the effect of prior claim reserve developments under reported claims ratios for the past several periods for each of our key operating segments.

Old Republic's book value per share declined by 2.8% or $0.49 per share compared to year-end 2017. The primary reasons for these changes are shown on Page 9 of the release. I would simply point out that the 2 most significant contributing factors are the $1.22 per share decline attributable to net realized and unrealized investment losses and a $0.78 per share cash dividends that were declared during the course of the year. These reductions were largely offset by the $1.89 of per share net income that resulted from the operating activities that Craig and Rande will speak to momentarily.

The debt capitalization ratios are also shown on Page 9 of the release. The lower capitalization ratio for debt securities at the end of 2018 reflects the conversion of the remaining outstanding principal balance of convertible notes into roughly 32 million additional common shares of Old Republic common stock, and this conversion occurred last year during the first quarter.

Consolidated pretax operating results for 2018 also benefited by approximately $17 million due to the elimination of the interest charge on the convertible debt. So overall, I'd say, the condition of Old Republic's year-end 2018 balance sheet remains very strong and substantially unchanged from year-end 2017 as well as by comparison to the earlier quarterly periods throughout 2018.

And with that, I'm going to now turn things over to Craig Smiddy for a discussion of the results of our General Insurance group. Craig?

**Craig Richard Smiddy**
*President & COO*

Okay. Thanks, Karl, and good afternoon, everyone. So as the release indicates and as we show in the financial supplement posted on our website this morning, the General Insurance group continues to see year-over-year growth in both revenue and earnings.

Our top line net premiums earned rose by 4.8% when comparing the fourth quarter of 2018 to the fourth quarter of 2017. For the full year 2018, premiums were 5.3% higher than in 2017. Net premiums earned in commercial auto rose by 16% in the fourth quarter of '18 compared to the fourth quarter of '17, mostly reflecting a continued increase in our rates in response to higher severity trends that I'll talk a little bit more about in a moment.

On the other hand, we experienced a 1.6% reduction in workers' compensation writings in the fourth quarter of 2018 compared to the fourth quarter of 2017, reflecting the challenges that we're having in maintaining premiums as rating bureaus continue to push down rates in response to lower frequency trends.

Throughout '18, net premiums earned received a lift from increasing exposure units due to continued economic growth, along with our strong renewal retention ratios and a reasonable amount of new business growth. While the group's overall composite ratio increased to 98.5% in the fourth quarter of 2018, the full year 2018 composite ratio essentially held steady at 97.2% compared to the 97.3% in 2017.

So now turning to the group's expense ratio, which came in at 23.5% for the fourth quarter, well below the 26.8% in the same quarter last year, largely due to the differences we've outlined in the release. The full year 2018 expense ratio of 25% compares to 25.5% last year and is well aligned. Our commercial auto claim ratio increased to 83.2% this quarter, while the full year 2018 claim ratio came in at 79.3% compared to 76.8% last year.

So as we've been reporting now for many consecutive quarters that the severity trends in commercial auto just continued to escalate, and we're recognizing and responding, increasing rates commensurate with the rising systemic claim trends. Even more specifically, the severity that we're continuing to see in commercial auto is emanating both from physical damage and bodily injury claims. Vehicle repair costs continue to rise, mostly due to expensive technology components.

While, bodily injury settlements are also rising, largely due to increasing attorney involvement and often the subsequent litigation that follows. On the other hand, our 2018 fourth quarter workers' compensation claim ratio declined by 6 percentage points from 73.5% in the fourth quarter of 2017 to 67.5% in the fourth quarter of '18. For the full year 2018, we ended at 70.7% compared to 75.5% at the end of 2017, an improvement we're obviously pleased to see.

Our general liability writings are smaller, certainly by comparison to commercial auto and workers' compensation, and we typically provide the 3 coverages together for an account, which is why in the financial supplement, we also show the claim ratio for these 3 coverages combined, which was at 75.9% for the fourth quarter of 2018 compared to 70.3% in the same quarter of last year. This fourth quarter uptick was a result of the higher commercial auto claim ratio for the reasons I've already discussed. However, the full year 2018 claim ratio for these 3 coverages combined came in at 74.8% compared to 75.9% for 2017, another improvement that we're pleased to see.

As the financial supplement also shows, the financial indemnity claim ratio experiences a significant uptick in the fourth quarter of 2018. This uptick is more specifically attributable to higher claim frequency in 2 coverages: Guaranteed Asset Protection, GAP; and Directors and Officers, D&O. Higher incidence of GAP claims are an indirect result of the higher repair costs from expensive technology components that I spoke about a little bit earlier, and a higher incident of D&O claims stems from a greater number of securities class action lawsuits.

As the release indicates, most of the elevated loss ratios we saw in the fourth quarter were result of our response to claim trend evaluations. And the fourth quarter is not necessarily indicative of what we expect to see going forward. Of course, all the claim ratios we report are inclusive of favorable and unfavorable claim development. And in the latest quarter, we saw overall favorable development of 0.9 percentage point, along with a continuation in the improvement of our overall annual trend to a point where we had neither favorable, nor unfavorable development for the full year.

So in the General Insurance group, we'll continue to make investments in people, product, infrastructure, while all of our underwriting units will remain focused on bottom line underwriting profitability. We're cautiously optimistic for 2019, recognizing there could be headwinds if the economies slows or if some of the elevated frequency and severity trends that we spoke about don't level off.

So on this note, I'll turn the discussion over to Rande Yeager for his comments on our Title Insurance group.

**Rande Keith Yeager**
*Chairman & CEO*

Great. Thank you, Craig. So we reported the morning -- this morning that the title group's quarterly and annual results were very good considering in context of a changing market condition, typical of the real estate industry. For the fourth consecutive year, we exceeded the $2 billion mark in premiums and fees, and this past year, we set an all-time high at $2.3 billion. Most importantly, I think, for the third consecutive year, the title group exceeded $200 million in pretax operating earnings, is quite an achievement for us. Quarterly results were also strong as we recorded $61 million in profits in the fourth quarter.

Speaking a little bit about the market. According to the Mortgage Bankers Association, they estimated the total originations were down by about 7% 2018. Most significantly, refinance activity was off about 25%. On the other hand, purchase money transactions were up slightly at about 3.7%. I have to note that the last statistic is good for our business because home sales offer greater opportunities for premiums and fees. So it's always good for us when more houses are selling.

Another contributor, housing price inflation, also enhances our revenues as premiums are based on the value of homes sold. And I think everyone knows that home prices have been going up the last 3 years. So that's good for our premium structure. In 2018, agency premiums were up a bit, about 3%. But in the fourth quarter, they were down slightly about 4%. Because the agency premiums lagged direct operating revenue by about 3 months, the decline is more reflected probably of the total markets fall off late in the year.

Direct operation revenue was basically flat for the year and down a little bit in the fourth quarter, about 4%. Speaking about commercial, about 18% of our premiums and fees are related to title group's commercial for us, which is significant and to a large part our commercial unit. It's not necessarily because of the stronger market, but because of our strong commercial team.

Another factor that's significantly impacted our results is our continuing, favorable loss development. In the insurance business, you can never say that there's a new normal, but we're optimistic that this trend, and it seems to be reflected industrywide, is going to continue.

With the mortgage origination market off and our operating revenues up, it's reasonable to conclude that our market share is up, and it is. In the third quarter of 2017, we recorded a market share of 15.1%, and this year, in the third quarter of 2018, we hit 15.8%. Our latest figure for market share through the first 3 quarters is 15.4%, and last year that number was 14.8%, pretty healthy growth. Bottom line is that if the market isn't going to help our growth, we're going to do our level best to make it happen.

But I would have to say, before concluding, I'd like to bring attention to a couple of senior management changes that augur well for the long-term continuity of our business. I'm referring to important management succession changes that we reported in December of this past year, 2018. As Al announced earlier, I've moved to Executive Chairman. Mark Bilbrey, who was our President, is now become our CEO. And our new President is Carolyn Monroe.

We're very secure in the title group's line of succession. We have qualified and culture-rich candidates throughout the company. And with this, we feel extremely prepared to address any issue that the market or the competition throws our way.

And I guess, with that, any questions that you may have, we can address in the Q&A period. And I'll conclude my remarks by simply saying that I'll turn the call back over to Al Zucaro.

**Aldo Charles Zucaro**
*Chairman & CEO*

Okay. Very good. Let's see. Why don't we take a quick look at the RFIG run-off business? And again, as the release shows, the mortgage guaranty and the consumer credit indemnity parts, we refer to that as MI and CCI, respectively, both of those lines -- types of coverages are reflecting a very stable situation.

And as long as the economy remains we think on a reasonably even keel with good employment and generally accommodative mortgage rates, we should continue to experience this stable situation in this run-off. MI margins, admittedly, will decline as time weighs on because of the important infrastructure maintenance costs that we need to absolutely incur. And as those costs rise or even remain stable, they will become increasingly misaligned with the expected decline in the top line.

Having said this though, we're still anticipating posting positive though declining earnings as this business closes in to the ultimate burn-off of policies in forces, as we said in past conference calls and writings. We think that most of this in force will be off the books by 2022 or thereabouts. So, but until then, the capital account of our mortgage guaranty business should build up, if only because of the increase of the positive earnings we expect. And we're very optimistic that we'll come to a very good end-game so to speak, that we'll have a most beneficial long-term outcome for all of the key stakeholders at ORI or in the mortgage guaranty business itself.

We still think very strongly that the MI business represents a most valuable and viable franchise that can either be activated to advantage in appropriate circumstances or otherwise run-off to similarly great advantage in our good hands. As to the much smaller CCI complement of insurance coverages that rests in the RFIG run-off, we think that it will, as I've said before, just mosey along in a profitable way as that business also experiences a quickening burn-off of policies in force.

This part of the run-off is now totally devoid, I might point out, of the significant claims litigation albatross that it had carried for nearly a decade. And as we announced in late 2017, we had settled one of the largest litigation exposures we had, and that was an exposure with the -- this country's second-largest bank. And it -- as we reported in the fourth quarter or third quarter of 2017, it had been settled at a cost in excess of previously established reserves.

So when you're comparing third quarter, fourth quarter '17 with the same quarters or the year for that matter of 2018, you need to keep in mind those large settlements that we booked in that year and which obviously thankfully would not -- did not occur, again, in 2018. The same time that we announced that settlement, we also said that there were reserves in place at the end of last year, '17 I should say, for the probable settlement of a second, but much smaller piece of litigation we had in the CCI part of the business.

Well, as the year came to a close in 2018, the probable became an actual final settlement around year-end '18, as I say. And it did not necessitate any increase in the reserve provisions that we had set up in earlier times. So that was a good event for us, and that it did not cost us more than we had anticipated. So I think, we're out of the woods in all these regards when it comes to the RFIG run-off, and we think it's likely going to proceed in a very uneventful workout of the remaining contractual obligations we have in the run-off.

So when we join everything together under Old Republic's umbrella, we feel very good about our situation today. Systemwide, our focus continues on the core underwriting and related services disciplines of our business, and that is -- has always been unchanged for us and is likely -- and will most likely remain unchanged.

And if you look at Page 3, in particular, in the release, the consolidated composite ratio of claims and expenses to premiums and fees for the entire book of Old Republic's business came in at 94.7% in 2018. And that number, of course, is obviously within the 95% long-term bogey for the company's long-tailed mix of combined general and title insurance businesses.

We continue -- big picture-wise, we continue to think that the North American economy, in which we are exclusively focused, is likely to remain in a very moderate, though perhaps temporarily slowing growth mode for the foreseeable future. But we think, again, that the very reliable and quality services that we provide to participants in the economy's most important industry sectors should enable us to grow the consolidated business at a faster clip than the economy at large.

And we think we can do this principally on the strength of the very high quality intellectual talents of our people, which are joined to a very strong, we think, world-class balance sheet. So with this, I think, we'll continue to compete on a level playing field, and we can take on all-comers in our specialty areas, no matter how large they may be.
So on this note, we can turn this visit to the planned question-and-answer period. If you will, just address your questions to me, and I'll direct them to one of the 4 of us.

# Question and Answer

**Operator**

[Operator Instructions] We'll take the first question from the line of Greg Peters with Raymond James.

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

I'm going to for the purposes of this Q&A zero-in on mostly the General Insurance business and results. And in the table on Page 4 of your financial supplement where you provide not only detailed by major coverage lines, but you also give us a snapshot of reserve development. I noted in the fourth quarter it looks like favorable development. And yet the current year loss ratio went up noticeably by over 700 basis points. And then, I was trying to flip that in your press release on Page 4. You said substantially all of the increase stemmed from the past decades new books of business. To me, that sounds like it's an adjustment to prior period reserves. And so, I'm just wondering if you bridge the gap or provide further clarification on what has transpired in the fourth quarter.

**Aldo Charles Zucaro**
*Chairman & CEO*

Well, I'll start, and then I'll ask Craig for help on this since he is closer to the details. But anyway, I think, what we meant here is that we did have an uptick in the loss ratio for current year loss costs in the couple of those businesses. And what we also mean to say is that the -- those businesses may have produced unfavorable developments from the past, let's say, but those were more than offset by favorable developments in the other parts of the business. I think that's what we tried to say and show in the news release. Craig, what do you think?

**Craig Richard Smiddy**
*President & COO*

Sure. I guess, I would only add that or underscore that what Al said is, in the current year, we did make some loss ratio adjustments, and that's not going to show up in the prior year development piece of our exhibit, even though an adjustment in the fourth quarter might be for any quarter during the year. And then I would just, again, reiterate that you have different places within our business where you may have favorable or unfavorable. And as Al said, that might not just be different segments of business, but it could be different coverages as well where you have differences in favorable and unfavorable.

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

Okay. And so, if I -- not getting hung up on the quarterly results, but looking at the annual numbers. So the claim ratio on commercial auto for '18 was 79.3%, up from 76.8%. And based on what you saw in the fourth quarter, is it reasonable to assume in that specific coverage areas that the claim ratio is going to be trending closer to the high 70s versus the mid-70s prior?

**Craig Richard Smiddy**
*President & COO*

Al, would you like me to?

**Aldo Charles Zucaro**
*Chairman & CEO*

Yes, please.

**Craig Richard Smiddy**
*President & COO*

Okay. Yes, Greg, I think, we've stated that the mid-70s is where we aim to be, and that continues to be the case. Yes, the severity trends that we're seeing, again, they are compounding quarter-over-quarter and year-over-year. But so are the rate increases that we're getting. And you saw in our growth of premium that I pointed out was largely due to increases in rates, that were also compounding those rates quarter-to-quarter and year-to-year. So I would expect that we will continue to come in, in the mid-70s. An expectation of the high 70s is not one that we have and, certainly, not one that we're targeting.

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

Excellent. I appreciate that. I'm not trying to ask too many questions around this one line, but it is important. And it's worth highlighting and I'm sure you're aware that other companies have signaled similar experiences. Travelers early this week reported some experience in their commercial auto business. If I just -- again, just in commercial auto, I was impressed with the top line growth. I mean, if you just look at the full year numbers, earned premium's up 12%. And Craig, you said a lot of this is rate. It's my impression that there's a ceiling on how much rate you can apply to these accounts in any given year before persistency becomes an issue or competitive threats become an issue. But maybe there's something changed in the environment that would support this higher rate level near term. And I'm just wondering if you could give us some color around that.

**Craig Richard Smiddy**
*President & COO*

Sure, absolutely. I take your point about price elasticity and our ability to continue with our high retention ratios, if rates are increasing as they are. The difference here -- and you asked was there a difference, I think there is a difference. And that is that you pointed to Travelers, but it's the entire industry that is experiencing what I called in my comments these systemic severity trends that -- for the reasons I outlined. So the industry has no choice but to respond to those trends. And therefore, it's helpful when everybody's moving in the same direction and in a very similar magnitude. Our rate increases for the year have been double digit and -- in the commercial auto line and -- which is why I made the comment that a good portion of that growth is coming from rate. But again, it's very helpful when the industry is moving in the same direction. Everyone is experiencing the same systemic issues and responding accordingly.

**Aldo Charles Zucaro**
*Chairman & CEO*

Let me add this to what Craig said before also. And that is the focus on Page 4 of the statistical exhibit should be on the combined results of AL and workers' comp and general liability, which we tend to write in total with respect to most of our accounts. And there, clearly the trends relative to, let's say, the last 10 years are very much positive in 2018 as well as in the fourth quarter of 2018. So I think we need to keep that in mind that we do write these accounts in their totality. And therefore, we know that our pricing or what have you on any part of the 3 lines may be off, but they will tend to get offset over time by the other lines.

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

Great. That's excellent additional color. So probably appropriate for me to let others ask questions around General Insurance. Maybe I can just switch gears quickly. And Rande, maybe the environment, given what's happened in the market recently, would suggest that title could be challenged from a revenue perspective for 2019. And so -- and I know you've provided some comments about this in your prepared remarks. I thought maybe you could expand a little bit on that. And the other piece of the puzzle for title would be just to -- looking at that reserves to paid loss ratio. And that's been drifting downward. And I'm just curious about your perspective of that and when revenue for the industry seems to be -- the outlook seems to be flat to down.

**Rande Keith Yeager**
*Chairman & CEO*

Yes. The market goes up and down, and if you look at the MBA reports on a monthly basis, they'll change their forecast. Interest rates were heading up towards the end of the year and then they kind of declined around the beginning of the year. Housing prices -- there's just -- what is this is a little bit of volatility everywhere, which makes for some uncertainty, and I think people are just waiting. There is government issues with the shutdown of -- was really more the Bureau of Indian Affairs can't approve mortgages for their indigenous clients. And so, as a result, there's just a bunch of uncertainty right now. I more than anything else just tend to believe that it's going to be kind of a wait-and-see for buyers during the first quarter, maybe a little bit longer than that. And then I think things pick up because the basic economy is good. We've got jobs. We've got the lowest unemployment rate in most of our generations that exists today. So I'm not negative about the marketplace. Though it may not be as strong as last year, and last year wasn't as strong as the year before. But I don't think we're seeing any great swings in demand for housing. Commercial market is always going to be there. Where there's money, the lending there appears to be -- developers are going to develop, and so we benefit from that. So yes, it's a wait-and-see year. Yes, let's wait-and-see what happens. But I think, overall, price slightly down from last year, if you just want my guess, but nothing significant and, certainly, nothing that we can't deal with or that we're not prepared to deal with. So I kind of think of that's where the market is. As far as paid losses, are you talking about paid losses to reserves, Greg?

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

Yes. If you look at that line item on Page 5 of your financial supplement, it's the reserves to paid loss ratio. And in 2018, it was 8.3:1 compared with 8.9:1 in 2017 and 9.5:1 in 2016.

**Rande Keith Yeager**
*Chairman & CEO*

I think it's sort of a byproduct. yes, go ahead.

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

No, I think it's historically been lower than its current levels, but I was just looking for your comments around that.

**Rande Keith Yeager**
*Chairman & CEO*

Yes. I mean, it depends on your loss picks and where the reserves were at a certain time and the stability. It shows the stability of the company more than anything else. I mean, how many years are we going to survive if we never had premiums? If we stopped issuing policies, how many years can we pay premiums for or claims for? And low isn't necessarily good. High isn't necessarily good. You want to reach a number or you want that to reflect stability in your financial situation in terms of are we reserving enough and are we prepared for the future? Because the most important thing we have are our policyholders out there, and we have to satisfy those claims that may be presented. We are an insurance company, so we do have them. So is it going to drift higher or lower? It depends on what we do. If we reserve less, that number can go down a little bit. I mean, it only makes sense. It's just the mathematical equation. And so, it's our job to look at these things historically and kind of determine where we should be with reserves and also make sure that those reserves are adequate to fulfill our policy obligations. So it should stay in that range. I think it's going to stay between 7 and 9.

**Operator**

[Operator Instructions] At this time, we have one more question remaining in the queue. [Operator Instructions] We'll take the next question from the line of Matthew Carletti with JMP Securities.

**Matthew John Carletti**
*JMP Securities LLC, Research Division*

Just a couple questions. Maybe starting following on Greg's questions on General Insurance. You talked about the kind of overall impact of prior periods being favorable during the quarter. Can you give us a little of the puts and takes maybe amongst at least the 3 biggest coverages of were there some larger favorables that are offset by some adverses, just trying to help put the movements in the reported line loss ratios into context?

**Karl William Mueller**
*Senior VP & CFO*

Craig, do you want me to take a crack at this?

**Craig Richard Smiddy**
*President & COO*

Sure.

**Karl William Mueller**
*Senior VP & CFO*

All right. Let me answer your question in this fashion. I think, as we've discussed previously, our objective when we close and publish each quarter's financial statements is to record our best estimate of our claim obligations at that particular moment in time. And we follow the same rigorous process each quarter to evaluate our key assumptions, underlying the reserving judgments. And we take into account a wide variety of information, such as claim development trends, changes in frequency and severity, as Craig talked about, so on and so forth. This process guides us on whether we should make any adjustments to our prior estimates as well as evaluating whether the current absent year loss ratios are adequate. So when we speak in terms of that favorable or unfavorable development, it is really just the summation of this quarterly estimation process. And it runs across all insurance coverages and all absent years. So we're headed into to speak [Indiscernible] with various insurance coverages because when you wrap it all up, it's the end result of a lot of judgments. They're made at a very granular basis. So if I might put this in perspective, Greg aptly pointed out earlier that in the fourth quarter of this year, we did have roughly $7.5 million of favorable development and for the year it was breakeven. But if you compare that number to the $5-plus billion of net reserves for the General Insurance group, you can see that the development's not all that significant. So while we strive to set the reserves at an adequate level each balance sheet date, we don't always get it right. But this table on Page 4 shows that we haven't missed it by much for the past several years when you look at things in their entirety. So I don't know if I did response to your question. I think that's the best response we have.

**Matthew John Carletti**
*JMP Securities LLC, Research Division*

Okay. And then maybe just one other if I could, I think, pretty straightforward. The loss ratio in the quarter in the property segment looked a bit elevated both from kind of where it was 9 months and prior quarters. I'm assuming -- I guess, I'll ask if was this some impact there from the wildfires or from Hurricane Michael? And if so, is that -- You could quantify it?

**Craig Richard Smiddy**
*President & COO*

Sure. I can speak to that. Okay. There was some cat activity in there, not from the wildfires. We don't have a lot of California exposure, but there was from Hurricane Michael some exposure there. So there is some component of that in that loss ratio. However, we do secure significant reinsurance for catastrophic property, and our exposure to catastrophic events is pretty minimal, but it will move up a loss ratio by a few points.

**Operator**

We'll now take the next question from the line of Greg Peters with Raymond James.

**Charles Gregory Peters**

*Raymond James & Associates, Inc., Research Division*

Usually, there's a couple more people on the line. So I've been ridiculed in the past for focusing in on asking a question in a public setting around your corporate and other operations because of their immateriality. Yet, the swing in 2018 from 2017 is quite noticeable. I'm referring to the table you put on Page 7 of your earnings release. We've gone from a pretax operating income of $9.9 million to pretax income of $40.4 million in '18 versus '17. So I was wondering if you could spend just a minute and provide us some perspective about what's changed and how we should think about this specific operation or line in your income statement in 2019.

**Aldo Charles Zucaro**
*Chairman & CEO*

Yes, you asked that question the last time, and I didn't answer it. But anyway...

**Karl William Mueller**
*Senior VP & CFO*

Al, I can answer that.

**Aldo Charles Zucaro**
*Chairman & CEO*

I' I'm sorry.

**Karl William Mueller**
*Senior VP & CFO*

I can answer Greg's question.

**Aldo Charles Zucaro**
*Chairman & CEO*

Okay.

**Karl William Mueller**
*Senior VP & CFO*

Very quickly if you -- so, Greg, when you look at -- this line includes our small life business as well as the corporate operations. When you look at the shift full year 2017 to 2018, if you recall some of the charges that occurred back in 2017 included $9.5 million claim expense attributable to the life business. And on top of that, 2018, to my earlier comments, we've eliminated roughly $17 million of interest costs on the convertible debt. So I think those are the 2 driving factors for the change year-over-year.

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

And so '18 would be more of a normalized result as we think about going forward?

**Karl William Mueller**
*Senior VP & CFO*

Well, the life business is continuing to shrink. So yes, it's probably in that neighborhood give or take a little bit.

**Operator**

It appears there are no further questions at this time. Mr. Zucaro, I'd like to turn the conference over to you for any additional comments or closing remarks.

**Aldo Charles Zucaro**
*Chairman & CEO*

Okay. Well, as always, we appreciate the interest from you, Greg, and you, Matt, in particular, since you asked all of the questions. And as I say, we -- so, therefore, we look forward to our next visit, which should be in about 6 months or so since we're doing these calls now on a semiannual basis, and hope for the best. So you all have a good day.

**Operator**

Ladies and gentlemen, this concludes today's call. Thank you for your participation. You may now disconnect your lines.