S&P Capital IQ

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Assurant, Inc. NYSE:AIZ

FQ2 2014 Earnings Call Transcripts

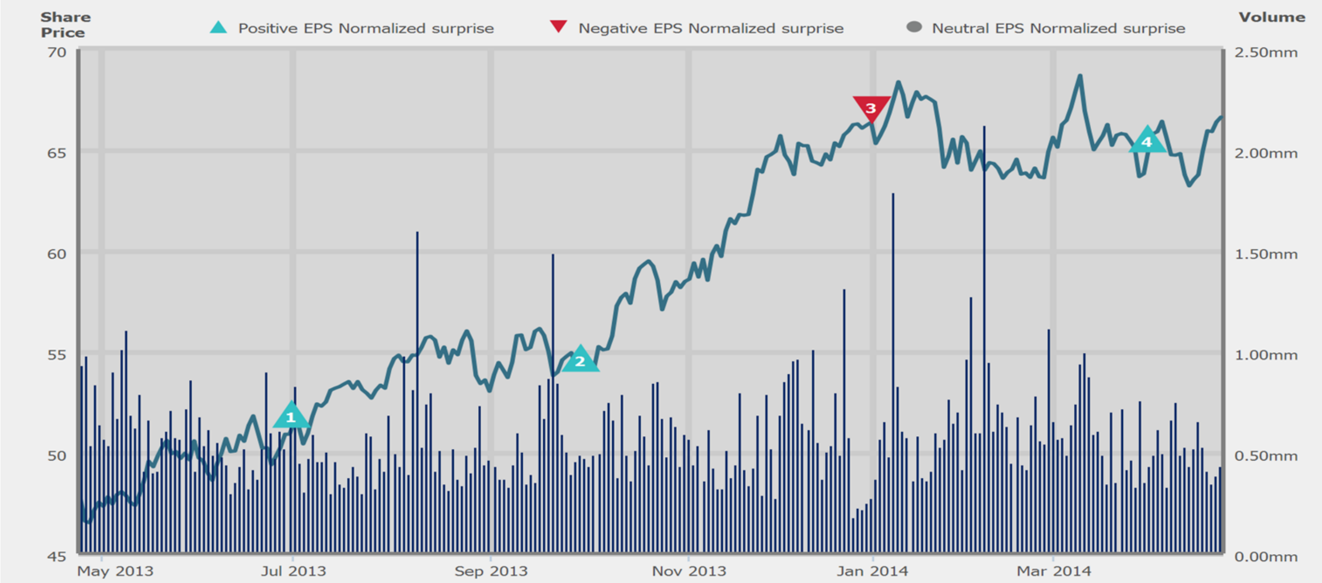
Thursday, July 24, 2014 12:00 PM GMT

S&P Capital IQ Estimates

	-FQ2 2014-			-FQ3 2014-	-FY 2014-	-FY 2015-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.54	1.62	▲5.19	1.39	6.25	6.49
Revenue (mm)	2367.98	2608.10	▲10.14	2370.55	9594.76	9801.94

Currency: USD

Consensus as of Jul-24-2014 9:12 AM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ2 2013	1.43	1.53	▲1 6.99 %
FQ3 2013	1.49	1.71	▲2 14.77 %
FQ4 2013	1.43	1.42	▼3 (0.70 %)
FQ1 2014	1.55	1.68	▲4 8.39 %

Call Participants

EXECUTIVES

Christopher J. Pagano
Executive VP & Chief Risk Officer

Francesca Luthi
Executive VP and Chief Communication & Marketing Officer

Michael John Peninger
Former Chief Financial Officer and Executive Vice President

Robert B. Pollock
Former Chief Executive Officer and Executive Director

ANALYSTS

Christopher Giovanni
Goldman Sachs Group Inc., Research Division

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

Mark Douglas Hughes
SunTrust Robinson Humphrey, Inc., Research Division

Sean Robert Dargan
Macquarie Research

Seth M. Weiss
BofA Merrill Lynch, Research Division

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

Presentation

Operator

Welcome to Assurant's Second Quarter 2014 Earnings Conference Call and Webcast. [Operator Instructions]

It is now my pleasure to turn the floor over to Francesca Luthi, Senior Vice President, Investor Relations. You may begin.

Francesca Luthi
Executive VP and Chief Communication & Marketing Officer

Thank you, Leo, and good morning, everyone. We look forward to discussing our second quarter 2014 results with you today.

Joining me for Assurant's conference call are: Rob Pollock, our President and Chief Executive Officer; Mike Peninger, our Chief Financial Officer; and Chris Pagano, our Chief Investment Officer and Treasurer.

Yesterday afternoon, we issued a news release announcing our second quarter 2014 results. Both the release and the corresponding financial supplement are available at assurant.com.

We'll start today's call with brief remarks from Rob and Mike, with Chris participating in the Q&A session.

Some of the statements we make on today's call may be forward-looking, and actual results may differ materially from those projected in those statements. Additional information on factors that could cause actual results to differ materially from those projected can be found in yesterday's news release, as well as in our SEC reports, including our 2013 Form 10-K.

Today's call will also contain non-GAAP financial measures, which we believe are meaningful in evaluating the company's performance. For more details on these measures, the most comparable GAAP measures, and a reconciliation of the 2, please refer to the news release and financial supplement posted on assurant.com.

Now, I'll turn the call over to Rob.

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Thanks, Francesca, and good morning, everyone. Second quarter results were good, despite higher claims at Specialty Property. We made progress deploying additional resources to the areas targeted for long-term profitable growth.

Let me highlight some examples from the second quarter. Our mobile business drove excellent results for solutions. Specialty Property generated solid fee income growth from our recent acquisitions in the mortgage value chain. Health continued to adapt to the Affordable Care Act, with robust sales outside the ACA open enrollment period, and Employee Benefits grew voluntary sales and revenues.

We measure our performance with 3 key metrics: annualized operating return on equity, excluding AOCI, was 10.8% year-to-date; book value per diluted share, excluding AOCI, has increased 5.3%, since year-end; and revenue, defined as net earned premiums and fees, was up nearly 20% year-over-year, driven by expansion across all 4 business segments and contributions from our recent acquisitions.

Our balance sheet remains strong. We ended the quarter with approximately $560 million of holding company capital. This provides flexibility to make investments in our businesses, pursue select acquisitions, and return capital to shareholders.

Now, I'll provide updates for each of our business segments. Assurance Solutions' delivered record earnings during the quarter, led by Mobile and expense savings from prior restructuring actions. Gains in mobile reflected favorable loss experience and contributions from client marketing programs that exceeded expectations. The number of enrolled devices is up more than 15%, since last year-end. Our program management capabilities provide a broad array of services that clients can tailor to their needs, such as product development, program administration and device management. This expertise allows us to segment mobile consumers and serve their needs.

The mobile industry remains dynamic, as carriers and distributors consider new partnerships and strategies to be successful in the expanding global market. Our progress this year demonstrates our ability to adapt, and we're excited about future opportunities.

In Preneed, we renewed our long-standing relationship with SCI, the leading funeral home provider in North America for another 10 years. This has been a great relationship, and we look forward to continued growth as we benefit from SCI's expanded footprint.

We're pleased with solutions year-to-date results, as the team met performance milestones ahead of schedule. We believe the business is well positioned to deliver 10% average annual growth, and net operating income over the next 3 to 5 years. Contributions from mobile, Preneed and service contracts are expected to offset the clients in our domestic credit and runoff retail businesses.

Assurant Specialty Property's net operating income declined due to a significant increase in non-catastrophe losses, which Mike will discuss in more detail. Underplays revenues continue to be solid. Our growing multifamily housing business, along with our acquisitions in the mortgage value chain are building a more diversified less capital intensive property business going forward.

At Assurant Field Asset Services, we captured additional share of the property preservation market by winning new business. We believe that our strong reputation, rigorous processes and large vendor network were the reasons we were selected.

The StreetLinks integration is well underway and early feedback from clients is positive. We anticipate this property appraisal business will contribute $80 million to $90 million of fee income to Specialty Property's results this year. And we've grown our sales pipeline as a direct result of the acquisition.

While it's still early, both of these acquisitions are exceeding our expectations. Overtime, we anticipate they will generate 15% pretax margins and help sustain attractive returns at Specialty Property.

Let's now turn to Assurant Health. Results reflected the continued impact of health care reform. The new guaranteed issue environment meant that a less healthy population than we traditionally insured would enter the market. The ACA's reinsurance and risk adjusted programs were designed to help mitigate the expected higher claims and were reflected in our pricing. Late changes in ACA rules, however, allowed people to extend coverage under existing plans. This changed the risk pool of ACA enrollees to include fewer healthy lives than we assumed. We expect experience and new enrollees to normalize over the remainder of the year.

The health team is preparing for the next open enrollment period that begins in November. We plan to participate on several public exchanges this year. We expect this new distribution channel will allow us to serve even more consumers with our broad array of products.

Recently, the Department of Health and Human Services announced that fixed indemnity plans, like Assurant Health Access, cannot be sold on a standalone basis beginning in January. Health Access currently accounts for less than 10% of health net earned premiums. While we believe these products meet affordability needs of many buyers, we will discontinue sales as required. Additional business from the public exchanges should more than offset revenue declines from our access products. We're encouraged that our major medical premiums grew in excess of 20% this quarter driven by strong sales, which continued outside of open enrollment. We believe our multichannel distribution, broad network and expense discipline will allow health to deliver attractive returns over the long-term.

Assurant Employee Benefits achieved strong results this quarter, with an ongoing focus on voluntary offerings for the small to mid-sized employer. Voluntary premiums grew by 13% or roughly 2x the rate of the market. We've gained share with our efficient enrollment, communication and billing capabilities combined with our broad product suite. We continue to allocate resources to voluntary, while working to reduce expenses in other nongrowth areas.

Before I turn to Mike, I want to acknowledge the succession plans we announced during the quarter. In addition to my retirement, Mike will retire this year. Chris will succeed him as CFO on August 15. I'd like to thank Mike for his many contributions during his 30-year career at Assurant. He's been a great advisor to me, most recently as our CFO for the past 7 years. I know that Chris will continue to build upon the company's momentum. I look forward to working even more closely with him during my remaining time as CEO.

With that, I'll now turn to Mike for more detailed comments on our second quarter results and outlook for the full year.

Michael John Peninger
Former Chief Financial Officer and Executive Vice President

Thank you, Rob. It's been a privilege to serve as CFO, and I know that Chris will provide strong leadership as the company executes its profitable growth strategy.

Turning now to our quarterly results, I'll begin with Solutions. Second quarter net operating income was just under $60 million, up almost 90% from the prior year. This increase was largely driven by mobile results, which benefited from double-digit growth in covered devices, very favorable domestic loss experience and $10 million of income from client marketing programs, which generated a significantly higher volume of devices than we anticipated.

Total segment net earned premiums increased 13% and fees were up 76%, due to the global success of mobile, which now accounts for roughly 25% of Solutions' revenue. The domestic combined ratio decreased to 91.4%, reflecting favorable loss experience in fee income from our various mobile offerings. Excluding mobile, the domestic combined ratio for our core protection products trended in line with our long-term target.

Adjusting for prior period restructuring charges, our international combined ratio increased 120 basis points year-over-year and reflected changes in our geographic mix of business. European results improved significantly as cost savings from the LSG integration accelerate in the months ahead, European results should continue to improve. We expect the total international combined ratio to approach our target of 100% for the full year.

Based on Solutions' strong performance in the first half of 2014, we believe that full year operating income will exceed our previous expectations. We do, however, expect some moderation in the third and fourth quarters. Client marketing programs contributed substantially to our first half results but future volumes and profitability are difficult to predict in such a fast-changing market.

Similarly, loss experience in our insured products can vary considerably from quarter-to-quarter and will likely increase from the low levels, we saw in the second quarter.

Looking further ahead, fluctuations in foreign exchange and the evolving mobile marketplace may cause results to vary from year-to-year. We remained confident, however, that Solutions' will achieve its 10% annual earnings growth rate target beyond 2014.

Moving to Specialty Property, net operating income declined by $38 million year-over-year, primarily, due to a spike in non-catastrophe losses. Excluding reported catastrophe claims, our loss ratio was higher by 790 basis points versus the second quarter of 2013. Unusually cold weather earlier this year caused a significant jump in water damage claims from burst pipes, including $22 million of adverse development from the first quarter. These losses, along with an uptick in fire claims, accounted for about 500 basis points of the increase. The balance was consistent with our expectations and reflects the impact of lower premium rates and loss trends associated with our new lender placed insurance product.

Our expense ratio increased by 600 basis points in the second quarter. Growth in fee-based businesses, which have higher expense ratios, costs nearly 400 basis points of the increase. Additional cost in our lender placed insurance business drove the remainder of the change. We expect that our long-term initiatives to standardize and streamline our lender placed platform will yield savings beginning in 2015.

Earlier this month, we announced the completion of our 2014 Catastrophe Reinsurance Program with more than $1.8 billion in coverage. Attractive pricing in the reinsurance market allowed us to lower our first event retention to $190 million versus $240 million in 2013. We also expanded multi-event and multiyear coverage. Complete details of the new program are available on our website.

Given continued growth year-to-date, we now expect properties, premiums and fees to increase slightly versus 2013. As we noted on our last call, we are in discussions with the client regarding possible loss of business to another carrier. We have no further update on these discussions at this time. Profitability at Specialty Property for the year will depend on loss experience, and the rate of change in lender placement rates, including the timing and outcome of our client discussions.

At Assurant Health, pretax profits, which we believe are the most appropriate gauge of underlying performance, totaled $7.5 million in the quarter compared with $12.4 million last year. Results included early claim submissions on Affordable Care Act policies. These policies accounted for more than 1/3 of Health's total individual medical net earned premiums in the first half of the year.

As Rob noted, initial claims were somewhat higher than our pricing assumptions, but much of that variance will be offset by the ACA's risk mitigation programs. As of June 30, our estimated recoveries from the reinsurance and risk adjustment programs totaled approximately $140 million, about $80 million of that is from the reinsurance component and is booked as an offset to policyholder benefits. The remaining $60 million is the expected risk adjustment reimbursement and adds to net earned premiums. We anticipate that accruals for both these programs will continue to increase as ACA plans become a larger portion of our business.

It's worth noting that reinsurance recoveries are estimated based on Health's historical claim payment patterns and the projected funds available to the industry under this program. The risk adjustment receivables are entirely a function of how the health of our policyholders compares to that of the market and are thus even harder to estimate. We've carefully reviewed our methodology, and the limited market data that's currently available. We believe our assumptions and methods are sound. Nevertheless, actual reimbursements may vary significantly from our estimates. We will update you as experience develops over the rest of the year.

Health continues to demonstrate strong expense discipline. In the quarter, the expense ratio declined 170 basis points due to prior expense actions and greater scale. Expenses also include $5.3 million related to the annual health insurer fee. We're encouraged by continued sales momentum and revenue growth at Health. As we look to 2015, we believe the individual health market will continue to grow and that Assurant Health will generate profits as we benefit from increased scale, improved experience and our ongoing expense discipline.

Employee benefits delivered a strong quarter, driven by improved disability experience, reflecting lower incidence and targeted pricing actions. In addition, the previously announced increase in the discount rate on new long-term disability claim reserves added nearly $1 million to operating income. Voluntary premiums grew by 13%, while our true group business continued to decline as expected.

Employee benefits remains focused on reducing expenses. In the quarter, the expense ratio declined due to net earned premium growth. As a reminder, expenses in the quarter included $1.5 million related to the ACA annual health insurer fee. We expect additional expense management actions, along with premium growth, to further reduce benefits expense ratio longer-term.

Turning to Corporate matters, we ended June with $310 million in deployable capital. During the quarter, we paid $60 million for StreetLinks, raised our dividend for the 11th consecutive year and bought back $59 million worth of stock. Through the remainder of hurricane season, we'll remain disciplined in deploying our capital. We will continue to balance prudent investments to fuel growth with returning capital to shareholders.

Net segment dividends year-to-date totaled $123 million or 42% of segment earnings. For the whole -- for the full year, they will roughly equal segment earnings, subject to factors such as growth in the business and rating agency requirements.

The second quarter corporate segment operating loss was $14 million, a 35% reduction compared to last year, due to lower benefit plan costs and other operating efficiencies. Overall, we're pleased with the quarter and performance so far this year. We continue to make significant progress against the strategic objectives we announced on Investor Day, as we grow and diversify earnings for the long-term. We're optimistic about our future prospects.
And with that, operator, please open the call for questions.

Question and Answer

Operator

[Operator Instructions] Our first question is coming from Chris Giovanni of Goldman Sachs.

Christopher Giovanni
Goldman Sachs Group Inc., Research Division

Question, I guess for Mike. You've mentioned confidence in achieving the 10% annual growth target in solutions beyond 2014, and you've talked a lot kind of this quarter and last quarter about the favorable experience, but didn't really call them out as disclosed items in the supplement. So I'm wondering if that growth in '15 includes actual year-to-date results? Or if there is some normalization of those client marketing initiatives and favorable loss experience?

Michael John Peninger
Former Chief Financial Officer and Executive Vice President

No, we have not called those out as disclosed unusual items, Chris. I mean, we were very happy with our mobile experience in the quarter of the year. We do talk, as I mentioned, about variability in these things. They're hard to predict in advance. But overall, mobile is very strong for us. And we also like several other areas have solutions too, which are performing very well, on our vehicle services business. We're excited about the new contract with SCI. So mobile definitely is driving our progress this year. But solutions, all solutions lines, are going very well. We got to keep in mind the declining areas too. But the domestic credit business and the retails channel in the U.S. But mobile plus those other areas we feel good about.

Robert B. Pollock
Former Chief Executive Officer and Executive Director

I think, Chris, if we go back and put this in a broader perspective, we're playing that big macro trends that we see going on in mobile. It's growing, it's growing in lots of different places. We're playing the trend of digitization, which is movement away from the big-box. Some of the things Mike talked about towards other ways of distributing product and we still like the growth in the middle market in Latin America. So those are the macro trends we're playing. Recall too that when we entered mobile, we entered that under an idea of ensuring devices. What we found is the much broader program management that Mike's talked about, which offer lots of different opportunities for us to participate. So we're quite excited about the mobile area.

Christopher Giovanni
Goldman Sachs Group Inc., Research Division

Okay. Understood. Around Health, can you talk a little bit about, what you're thinking about regarding the public exchanges? I know at Investor Day you talked about looking to participate. So any updated thoughts in terms of number of states you're going to target, and how we should be thinking about the discontinuation of the access products? That's an area you have had some success selling into over the past few years?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes. So the first thing I think is, if you look at where we were a year ago, we decided to allocate resources toward consumers and agents as they were going through the impacts of health care reform. We also were at the belief that everything we've heard, the exchanges we're going to have, some trouble getting up and operating at the beginning, we didn't think that was the best use of our resources. That turned out to be a pretty good decision. I think things went well. So what are the learnings today. The learnings we found is the exchanges have gotten better, and they're also used by agents as a way to determine who might be eligible for subsidy. So -- although they -- I think the agent will continue to be the guider of the buyer in a lot of these situations, or most of them, they're going to use the exchange as a means to determine if someone can get a subsidy. We're going to make decisions on a state-by-state area based on where we think the best opportunities are, but we do think playing in that arena and demonstrating we can succeed there will be important for us going forward.

Michael John Peninger
Former Chief Financial Officer and Executive Vice President

Yes, and I think access has been a nice growth product to your point, Chris. But with that going away, we think that the exchange will -- be another source of revenue that will definitely offset that.

Christopher Giovanni
Goldman Sachs Group Inc., Research Division

And then last one, and I'll jump back in the queue. Maybe for Chris around capital and M&A. Obviously, the capital position is strong, continues to build and I don't think you've taken kind of all the dividends out here year-to-date. So I guess maybe even better if given the current kind of pace of buybacks here. So wondering, if you still have some debt capacity here, at attractive rates, would there be any consideration for larger M&A and/or change in maybe what you've communicated from a share repurchase standpoint?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Chris, Rob. I'll give this to Chris, because it's really his. But I just want to start with remember, we continue to have businesses that generate a lot of free cash. We think that's a big part of our storyline and what we're trying to do, and it underlies all of our activities around capital management. Chris, why don't you tee that up?

Christopher J. Pagano
Executive VP & Chief Risk Officer

Sure. I mean, it does a couple of things. First, again, this is the approach to M&A hasn't changed. We continue to believe that modest sized deals in targeted growth areas are the best source of value creation. We continue to maintain our discipline around cash based internal rate of return, hurdle rates. We do believe we have some debt capacity, probably $250 million to $300 million, just increases the financial flexibility overall. But as Rob said, cash producing operating companies give us significant amounts of, again, flexibility to deploy capital in targeted growth areas organically or through M&A, and then also to return capital to shareholders. We still believe the stock is attractive, and continue to view share repurchase as a prudent use of deployable capital.

Operator

Our next question comes from Mark Hughes of SunTrust Robinson Humphrey.

Mark Douglas Hughes
SunTrust Robinson Humphrey, Inc., Research Division

The $140 million in accruals, would you assume that the second half accruals would be at about the same level? And can you give us some sense of your confidence in the -- your calculations, given the kind of fluidity of the environment in health care?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Sure, well, the accrual will continue to grow because that the settle up on these things won't take place for a while. But I think it will grow along with our premiums as so-called metallic premiums account for a bigger share of our business, Mark, the accrual will grow along with that. We'll be certainly be reporting out to you in a variety of settings about the progress. To the confidence in these, they're part of the legislation, the ACA legislation. We built them into our pricing. they were designed to make sure that individual carriers were comfortable being in the market. For the most part, well actually, I think they are industry funded. There's money being collected now and then in the case of the risk adjuster, it's sort of a zero-sum industry program. So we're quite confident about that.

Mark Douglas Hughes
SunTrust Robinson Humphrey, Inc., Research Division

Okay. And then you'd -- any update on the savings you'd described when -- the plan to standardize, streamline the platform in specialty property, how meaningful will that be?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Well, we think it will be quite meaningful -- it's a multi-year plan because of the complexity of the property of business, the complexity of the systems environment that's required to serve our lender placed clients and all, it doesn't happen overnight. But as I think we mentioned, we expect savings to start next year and then they'll build over the next year or 2.

Mark Douglas Hughes
SunTrust Robinson Humphrey, Inc., Research Division

Any sense of the magnitude there? Tens of basis points, hundreds of basis points?

Michael John Peninger
Former Chief Financial Officer and Executive Vice President

I think as plans get more firmed up, we'll certainly be updating you about that, Mark. But we expect the savings from these initiatives to be meaningful.

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Right. And you can just think about it as representing a lot of changes that have gone on in the marketplace, where historically having a tailored solution was very important to the servicer, with all the requirements that have come about around the compliance aspects of things, a move towards standardization will make a lot of sense. We've identified things to work on in that area. We've had discussions with a number of our clients. They're very receptive. So now, Mark, it's just a matter of execution on the things that we've identified. But it will take time, as Mike mentioned.

Operator

Our next question comes from John Nadel from Sterne Agee.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

Wanted to go into mobile, maybe in a little bit more detail. And the -- I think you mentioned in prepared remarks, maybe Mike's remarks, that mobile today represents about 25% of Solution's revenues. I just want to make sure, is that of the total segment revenues or should we exclude preneeds? Is that just on premiums and fees?

Michael John Peninger
Former Chief Financial Officer and Executive Vice President

It's the total segment, John.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

Including net investment income as well or just premiums and fees?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

No, premiums and fees.

Michael John Peninger
Former Chief Financial Officer and Executive Vice President

Premiums and fee income.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

And then thinking about -- can you give us a sense for the split of that between domestic and international? Is it 50-50, 75-25, I mean?

Michael John Peninger
Former Chief Financial Officer and Executive Vice President

Yeah, I don't think we've provided that split yet, John. We've got contributions from the domestic clients. Notably, we've talked about T-Mobile, we've got a considerable amount coming in from [indiscernible] and Telefonica.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

Telefonica. Yes. On the marketing programs fees, I think you mentioned $10 million. Is that 100% margin for you guys? Or is there some expense that you put up against that?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes, there's certainly expenses, John. You can think about it as it's a big logistics business. Someone might trade in a phone or send in a phone for repair. We have to work on it, mail it back to them. So there's certainly expenses associated with these things. And the contributions from these programs come in different ways, John. We've talked about the $10 million contribution. But in some cases, because of the different kinds of program we do, sometimes they're accounted for through fees and sometimes they're expense offsets and stuff. So that's why we've tried to help you with that. And we mentioned that the combined ratio on the non-mobile things are trending sort of in line with our historical benchmarks. So I think with this additional disclosure, that can help you sort of figure out how mobile is coming through our financials.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

Okay. And so then -- so $10 million, but it's not entirely $10 million to your pretax income and solutions?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

No, it's a $10 million contribution to NOIs is what we [indiscernible] program. So there's much more combination of things, it's netting to that, John.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

So $10 million after tax impact in Solution. Got it. Then -- just a quick one on health. Just, can you give us a sense for the margin differential between the health access product and the major medical -- individual major medical product?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes, I think at our Investor Day, Adam went through some of this, John, and outlined that. We're feeling much more confident that we can earn good margins in the traditional major medical business. I'd also point out, remember, we're on a journey here in health. And we said that as we developed our strategy over time, the first thing was to demonstrate as the Affordable Care Act went into business or became fully functional, that we could sell in that environment. I think we're proving we can do that. We know we have some higher expenses associated with commissions on new business. We've had to put resources on getting ready for all these things, and we think profitability will improve over time. And over the long term, we think we can earn attractive returns in the business. So step one, we prove we could do things. This year, we're going to go on the exchange, prove we can sell there. Longer term, we know the profits will follow.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

And I'm sorry, I have got 2 more quick ones. Just returning to Solutions real quick. I think this quarter, about $1.7 billion of equity allocated to that business. Obviously some moving parts in terms of what's growing, what's not, how capital intensive that growth is or not. As we look forward, should we expect that, that $1.7 billion is going to grow significantly from here?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

No, I think there's some noise in the inner -- in the quarters, John, because of our complex legal entity structure. So I think if you go back and think about equity as we've got income, we take some dividends out from the segment, there's some growth that's certainly going to drive Solution's equity up. But I don't think it will go up. In fact, it will probably moderate a bit by the end of the year from the $1.7 billion.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

Got it. And then, lastly, just in Specialty Property on the lender-placed side, if you think about the impact of rate reduction, specifically in those couple of states where they were pretty meaningful, about how far in the ballgame are we in terms of seeing that fully reflected in your premiums through renewals and new business?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes, if you think about it on a state-by-state basis for instance, we're done in California. Those changes were put into effect a couple of years ago, we finished. I think what Gene outlined at Investor Day is we'd have about an 8% to 9% impact over the course of '14 and into '15. Obviously, Florida is a big part of our business. We started taking rate actions in Florida beginning in January of this year. And as business renews, that represents about 1/3 of our business, John. So there's a timing impact to how these things come through. And we review the stuff regularly on a state-by-state basis with each of the different insurance departments.

Operator

Our next question comes from Seth Weiss of Bank of America.

Seth M. Weiss
BofA Merrill Lynch, Research Division

Maybe just to return to Solutions real quickly. In the outlook, you removed $50 million target for the 4Q. I just want to make sure I'm reading this right. Is this because you've already basically achieved that? Or could we read that there's maybe upside to quarterly run rate earnings?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes, we feel good about the $50 million in the fourth quarter. We took it out because of the strong quarter we just had. We're sort of already there. We pointed out that you just need to think about a little bit of variance, and we had really good loss experience in the second quarter. Historically, loss ratios have moved around a little bit from quarter-to-quarter. And then we talked about the sort of inherent difficulty in predicting some of these marketing programs because they're really under the control of the carriers. The carriers start and stop them. So we just want you to be aware of those things when we think, but overall, we're very pleased with Solutions results.

Seth M. Weiss
BofA Merrill Lynch, Research Division

Okay. And then thinking about these marketing programs, should we think of the back half of the year where there may be particularly a pressure to what you would otherwise expect that some of those earnings were maybe brought forward due to more accelerated pace of these marketing programs? Or should we just think about a base level there?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Again, we can't predict what will happen. We do have -- I think other things we've talked about, we've got expense savings going on in all the solutions that will continue to take effect, as we go through the year. A lot of the programs are designed around carrier strategies, and also the introduction in new phones, et cetera, those are difficult things to predict.

Seth M. Weiss
BofA Merrill Lynch, Research Division

Okay, great. And if I could just shift quickly to Specialty Property. And I believe in the prepared remarks, you talked about an alternate 15% margin on the Field Asset and StreetLinks. Could you give us a sense of where you are now on margins? And maybe also a sense of -- I assume these are much less capital intensive products. Could you give us any sense of what kind of capital requirements those demand?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes, I think Chris' presentation at Investor Day tried to address some of that Seth. And I'm going to let him tee up kind of where we are on a number of these acquisitions.

Christopher J. Pagano
Executive VP & Chief Risk Officer

Sure. So just one -- a comment, just first about the capital intensity, These are fee-based businesses, so there will be very little additional capital outside of the purchase price. In terms of the investment thesis with these 2 investments, this is mortgage value chain. It's not a market that's growing, but a market where we believe we can gain market share by expanding our product offerings, leveraging our distribution with the -- within the mortgage market and improve the operating margins by efficiencies and synergies by rolling these businesses up into the broader property space. So we feel very good about that. We just keep in mind, though, that we look at these on a cash basis, internal rate of return, hurdle rate basis. There are significant intangibles associated with these 2 purchases. Field Asset Services is roughly $20 million of intangibles that will amortize over the next 5 or so years. The StreetLinks deal is about 75% of that purchase prices intangible. So you're not going to see significant NOI contributions in the early years. But over time, as we assimilate these businesses into Specialty Property, we do believe that they're going to be -- produce long-term profitability and value creation.

Seth M. Weiss
BofA Merrill Lynch, Research Division

So that 15% is looking beyond that amortization period?

Christopher J. Pagano
Executive VP & Chief Risk Officer

No well, again, operating margin and NOI, separate discussions there, so -- which again -- so pretax operating margin will be a function of the synergies and the efficiencies. And then, of course, scale as we expand in the out years. So -- but in terms of NOI, you've got to back out intangible amortization, but that again is not a cash -- will not affect the cash generating potential for these businesses.

Operator

Our next question comes from Steven Schwartz of Raymond James.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

I have a few here, kind of random. The increase in fee income going to Specialty Property. First, the increase in fee income in the quarter, sequentially from 1Q '14, that is both StreetLinks and Field Asset Services?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Correct. StreetLinks was -- it came in during the quarter, so that was a meaningful change from first quarter.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

All right. And then something that I track -- I don't know if you look at it this way or not, but I look at gross premium earned to the homeowners business relative to loans insured and that actually picked up a little bit in the second quarter versus the first quarter. I would expect that to decline. Is there a reason, a geographic mix shift or just?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes. It certainly, I don't know off the top of my head, but the hypothesis you just offered up could well be a reason, Steven. Yes, I think there's lots of -- sort of the loan counts are point in time snapshots, and it's directionally important but it's not a perfect timing match with our premiums. But I think you're thinking about it correctly. But in the loans, the pricing is going down, as we've talked as we roll out our new product.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

Replacement values doing anything?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

I think our average insured values, I'm just trying -- I think they've been pretty level, right.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

And then moving on. Just some more follow-up on these marketing fees. These are monies paid to you and then you go out and boost up your marketing to get people to buy extended service contracts. Is that the deal?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

No. A little bit different than that. So they can be promotional in nature. They might relate to someone sending us a phone, which we repair and get paid a margin on or it could be that we're actually taking a device and selling it into the secondary market. There's a myriad of different things that could go on there.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

But our assumption should be that this $10 million probably goes away?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

No, I just think that it will vary over time. I think that's the big point we're trying to make here is this won't be just a steady state. It will go up some quarters and down others. But, overall, the long-term trend, I think, is this is a positive contributor and demonstrate another place we can participate in profit pools around our overall program management.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

Yes. I realize this is all in the comments, all new, but is this $10 million high?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

It's certainly high given as long as we've been in it, but again, I think you'll see more of these things happening depending on the volumes of our clients being able to attract additional consumers. It may relate to introduction in new phones or devices. A myriad of things can drive it. And I think we'll keep you updated as these things go on. And as Rob said, these are relatively new. So our track -- our history is we have, what, $4 million in the first quarter, $10 million in the second quarter. Over time, there's likely to be some kind of baseline that will develop, but it just takes time for that to come out.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

Okay, great. And then just moving onto Solutions. Firstly, the access product. This is a hospital indemnity product?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

The health access product? It's a product that has fixed indemnity benefits, Steven. It can be a variety of different things. But importantly, not have all the benefit requirements of the ACA plan.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

I guess the question that I want to ask here is, it has not yet been clear to me -- I think I discussed this with Adam. But the HHS decision, does this affect what we would consider to be, I think, ancillary or supplemental health plans like dental or cancer or anything like that?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

No. All those can be sold in conjunction with a qualified plan. So those can continue on.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

Can those be -- can those still be sold in conjunction with the non-ACA compliant plan?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes, but most of our sales are going to be ACA compliant, with our standard major medical site. Again, on Health Access, I believe the in-force will be allowed to remain in effect too. It will be grandfathered as other plans have, for those who have them.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

All right, okay. And then, just one more in Solutions. So the accrual from the reinsurance programs and the risk-adjustment programs was $20 million in the first quarter, $120 million in the second quarter. You wouldn't expect $120 million in the third quarter and fourth quarter?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Well, it's going to grow with the premiums, and the metallic premiums were a much higher percentage of our total premiums in the second quarter than they were in the first quarter, which drove that sort of increase. We're going to tell you, we'll report out regularly on these, Steven, to give you a sense. But they will grow with growth in the premium.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

Well, I guess I'm wondering, was there like some type of catch-up in 2Q as development occurred as you saw what your experience was?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes, we were estimating with no experience at the beginning. We had a little, but still a small amount at the end of the first quarter. We have a bigger, but still small amount at the end of the second quarter. I think, and Mike mentioned this, but I think this is important, we're participating in 2 of the 3 Rs. The health insurance fee is set up to cover the reinsurance recoverable, that's the claims between $45,000 and $250,000. So funded, Mike pointed out what we're paying on those fees, but that's being collected from all health insurers of all sizes to deal with issues in the individual market, okay? The risk adjusters is some companies are going to have worst pool of risks, and some are going to have a better pool of risks. Okay. That's a 0 sum game. If you've got a better pool, you pay in. If you've got a worst pool, you're a receiver. We think we're going to be a receiver.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

One more if I may. Just reminded me of this discussion. Torchmark, yesterday, wound up having to take their guidance down a little bit for this Gilead Hepatitis C drug? Is that an issue for you?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes, it's an expensive drug. I think they may have -- I can't speak to the specifics of what they're offering. But certainly, we pay a lot of attention to just looking at drug cost because they're something that are causing health care costs to go up, obviously.

Operator

Our next question comes from Sean Dargan of Macquarie.

Sean Robert Dargan
Macquarie Research

As we think about the combined ratio in Solutions, domestically, it was the most favorable it's ever been. And I realize there is some favorable loss experience. But can you give us a sense of the seasoning of losses over the life cycle of a handheld device, because you're fairly new to this. When do I guess claims kind of peak?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes. So I think a couple of things first. The movement in that combined ratio has been driven by mobile. But as Mike pointed out, it can report through in the revenue line in the combined ratio. It can also report through as an expense offset in the expense piece. So those will produce slightly different dynamics in terms of just the calculation. Now in terms of the devices themselves, the basic program with the large carriers tends to be reinsured back or can be reinsured back to them. We think we have a long history in understanding the devices that are out there today and how they repair and recognize that in terms of how we look at our results. Could that change on new devices? I suppose it could, but we think we have a good handle on how repairs take place.

Michael John Peninger
Former Chief Financial Officer and Executive Vice President

Yes, and I think losses come in -- there's not like people have a phone for months and then they have more claims going up. I think it's more if there's variability and we see some seasonal variability and losses due to maybe there's more accidental damage claims. There might be a little bit of theft experience that varies differently on the age of the phone or something like that, but I think in general this stuff develops fairly quickly.

Sean Robert Dargan
Macquarie Research

Okay. And if I remember from last year, there's some I guess negative seasonality in the third quarter. And people go to the beach and the pool...

Michael John Peninger
Former Chief Financial Officer and Executive Vice President

Yes, we did see that last year and then we saw very good experience in this quarter that just ended that we talk about. So you do see there's some sort of fluctuations.

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Yes, we've certainly attributed that to kids having phones being outside, dropping them in pools in the summer. I mean those are the anecdotes that get offered up, Sean.

Sean Robert Dargan
Macquarie Research

Okay. That's helpful. And shifting to property, there was a subtle shift in the language of the outlook, which you mentioned another carrier that this portfolio of loans can go to. I know you said at the beginning you don't want to talk too much about this. But does that mean incrementally you feel stronger that -- or you have a better sense that this portfolio is going to leave?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

I don't think we have anything new to report here. I think, again, we've tried to report as quickly as we knew about the issue, and it's going to play out over time. We'll let you know if and when something happens.

Sean Robert Dargan
Macquarie Research

Okay. You still earned the 20% ROE in property in the quarter. Is there any sense that anyone in Bermuda might want to do this at -- priced at 15% ROE? I mean, have you heard anything about new entrants to this market?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Again, not -- I haven't looked at it in particular. Again, we've said that there's always been competition in the business. And really the fact that there's a lot of intricacies around the tracking, the compliance, et cetera, are a big part of our strengths in the process. But there's people who, obviously, have -- we're competing with all the time.

Operator

And our final question comes from John Nadel of Sterne Agee.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

I can't get enough of you guys this morning. It's the first company, first conference call during earnings for me, so I still have energy. A couple of follow-ups on Specialty Property, and I'll follow-up on Sean's question here. I mean is there anything you guys can provide to help us think about the risk to the top or the bottom line if you lose this block of business? Or can you provide any color on why the client is looking to potentially move the business? Is it just a matter of diversifying? Are you seeing some heightened pricing competition? Any color you can provide.

Robert B. Pollock
Former Chief Executive Officer and Executive Director

I think if you go back to Gene's presentation at Investor Day, John. It starts with, "Hey, this business over time is going to normalize," okay? And I think we tried to update all our guidance around what that will look like compared to the prior Investor Day. And I think the things that Gene provided said, is still going to be an attractive business. Probably going to have a little higher placement rate than we had told you last time in the end for a number of reasons. And that we think that we're taking rate actions, et cetera, but we'll still produce attractive but lower returns. I think all of that still is the case. In terms of the particular client, we'll report out if we know anything. But this is normal course action, I think, that can happen at any time within a business. And remember, we've been the net winner of most loan additions over the last couple of years. So again, I don't think this is anything out of ordinary course.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

And this is coming up on the normal expiration of an existing contract?

Christopher J. Pagano
Executive VP & Chief Risk Officer

We don't really talk about terms of anything that way, John.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

So second one for you, and I know this is probably equally as tough to talk about, Rob. But one of the questions I continue to get asked is whether the slower pace of buybacks these last couple of quarters might be related to building up some sort of a cushion in the event of a settlement or something related to the FHFA, who is obviously being at least pushed a little bit here, or at least guided, advised to take some or pursue some legal action against the lender-placed insurers. Do you have any comments there?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Sure. I always have comments. Again, I think, remember, when we go back and we talk about we introduced our new product, okay, we reached out to the Fannie and Freddie at that time. Talked to them about gee, there've been dislocations in the mortgage marketplace. We're going to try and adjust the product to provide more flexibility to servicers to better respond to their individual portfolio needs. So remember, we gave more flexibility around deductible, coverage amounts on seriously delinquent loans. We looked at area ratings. We did all these things, and we sat down with all the state insurance departments and introduced the new product and made rate changes, where we thought they were appropriate. So I think we've responded to all those issues. I think that we've got that new product operating in 45 states today. And our commitment is to our mortgage servicers, which continues. In terms of Capital Management. Chris?

Christopher J. Pagano
Executive VP & Chief Risk Officer

John, I guess I think -- when I think about sort of the pace of buybacks relative to the deployment of capital in organic growth or the acquisition, again, we're focusing on the balance between those 2. We think it's the combination that's going to create value. We still think the stock is attractive. However, as I said at Investor Day, there are other alternatives, both organically and out in the M&A space, that are providing comparable risk return alternatives. If you look at the deployment of capital since the beginning of the year, we've actually returned about $120 million to shareholders via repurchase and/or dividends and done $60 million of acquisitions. So again, it's this balance. How we think about repurchases from this point on, it's again a function of cat season, the capital needs of the operating companies, the M&A pipeline and what's potentially out there and whether or not deals are going to meet our return thresholds. And then also the pace of segment dividends. Again we still -- as you mentioned earlier, we still got a fair amount of segment dividends still at the operating companies, that will come up during the course of the year. And the deployment will be calibrated accordingly.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

Okay. All very helpful. And then final question for you, Rob. So it's been a few months since the announcement of your upcoming retirement. I'm sure the board is taking a really methodical approach here. But should we be interpreting the duration of the process as an indication that you're more likely to bring someone in from the outside, as opposed to promoting someone internally?

Robert B. Pollock
Former Chief Executive Officer and Executive Director

Look, the responsibility on succession is the boards. They've got to process. I think they're following that process carefully. I think, as most of our investors know, we've got a strong talent bench internally here. And the board understands that. They also have a fiduciary responsibility to look outside and what I've kind of pointed out is if they can find a superstar, they're going to bring him in. We've got lots of stars internally. So they're just working through their process, John.

Thanks for joining us this morning. We look forward to updating you on our key milestones in the months ahead. Please reach out to Francesca and Suzanne with any additional questions you might have.

Operator
Thank you. This does conclude today's teleconference. Please disconnect your lines at this time, and have a wonderful day.