S&P Global
Market Intelligence

Arch Capital Group Ltd. NasdaqGS:ACGL FQ3 2018 Earnings Call Transcripts

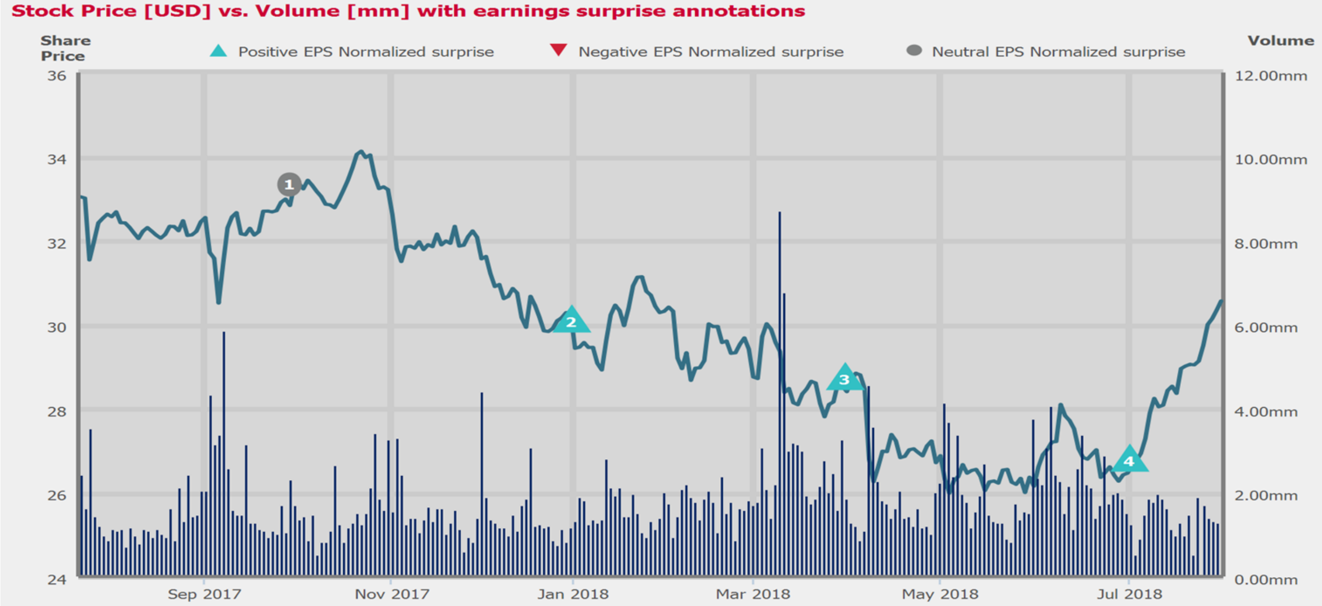
Wednesday, October 31, 2018 3:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2018-			-FQ4 2018-	-FY 2018-	-FY 2019-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.52	0.59	▲13.46	0.55	2.24	2.38
Revenue (mm)	1192.67	1181.88	▲(0.90 %)	1036.97	4610.80	4777.38

Currency: USD
Consensus as of Oct-31-2018 10:00 AM GMT

Stock Price [USD] vs. Volume [mm] with earnings surprise annotations



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ3 2017	(0.21)	(0.26)	NM
FQ4 2017	0.37	0.45	▲1 21.62 %
FQ1 2018	0.52	0.56	▲2 7.69 %
FQ2 2018	0.53	0.59	▲3 11.32 %

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Call Participants

EXECUTIVES

François Morin
Executive VP, CFO & Treasurer

Marc Joseph Roland Grandisson
CEO, President & Director

ANALYSTS

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

Joshua David Shanker
Deutsche Bank AG, Research Division

Kai Pan
Morgan Stanley, Research Division

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

Michael David Zaremski
Crédit Suisse AG, Research Division

Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Q3 2018 Arch Capital Group Earnings Conference Call. [Operator Instructions] As a reminder, this conference call is being recorded.

Before the company gets started with its update, management wants to first remind everyone that certain statements in today's press release and discussed on this call may constitute forward-looking statements under the federal securities laws. These statements are based upon management's current assessments and assumptions and are subject to a number of risks and uncertainties. Consequently, actual results may differ materially from those expressed or implied. For more information on the risks and other factors that may affect future performance, investors should review periodic reports that are filed by the company with the SEC from time to time.

Additionally, certain statements contained in the call that are not based on historical facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The company intends the forward-looking statements in the call to be subject to the safe harbor created thereby. Management also will make reference to some non-GAAP measures of financial performance.

The reconciliation to GAAP and definition of operating income can be found in the company's current report on Form 8-K furnished to the SEC yesterday, which contains the company's earnings press release and is available on the company's website.

I would now like to introduce your host for today's conference, Mr. Marc Grandisson; and Mr. François Morin. Sirs, you may begin.

Marc Joseph Roland Grandisson
CEO, President & Director

Thank you, operator, and good morning to you all. Happy Halloween to all, and best wishes to you, you little ghosts, goblins and princesses. While the stock market has been providing some scares this past week, here at Arch, we had another good quarter despite higher cat activity around the world, as our operating strategy of diversification, cycle management and focus on risk-adjusted returns produced an annualized operating return on equity of 11.4%, and 2.3% increase in book value per share at September 30, 2018. François will provide more commentary on our financial results in a moment, but it's worth noting that our modest exposure to property losses this quarter is not just the result of our good risk selection. It also reflects our ability to remain disciplined in a market where risk-adjusted returns do not meet our return hurdles.

The 2017 and 2018 catastrophes are a reminder that margins in cat-exposed property lines remain thin, and in many cases, are inadequate relative to the severity and frequency of catastrophe events.

With respect to market conditions in our property casualty operations, outside of property, there are just a few specialty areas such as travel accident and European motor, where current market conditions provide opportunities to deploy additional capital. In most of our insurance lines, rate changes are positive and appear to be outpacing claim trends. But as we have discussed in prior quarters, the spread between rate changes and loss trend, claims inflation, if you will, is small, and we remain cautious in establishing our loss picks.

In addition, specialty lines such as those that we write are volatile by their nature, and it is necessary to use a longer assessment period in order to evaluate the ultimate margins.

In summary, overall market conditions in our P&C businesses seem relatively unchanged from last quarter, and we continue to believe that additional rate increases are needed to provide a more adequate margin of safety and broader growth opportunities.

Turning now to MI, where the operating environment remains attractive. I will focus my comments on our U.S. primary business, which represents over 80% of that segment. MI pricing appears to have stabilized in the third quarter after the rate changes announced in the first half of this year. The credit quality of loans insured remained strong, and our key risk barometers are still at benign level relative to historical norms.

If you have a chance, visit our Arch MI website for a full housing and mortgage market report, called the HaMMR report. It will give you a good idea of why we remain confident of the health of the U.S. housing market. In short, due to the factors I just discussed, we like the visibility in the future performance of our U.S. mortgage insurance business.

Our U.S. MI new insurance written or NIW was strong again at $21.4 billion, a 21% increase over the same quarter last year. In the third quarter, higher loan-to-value or LTV mortgages with greater than 95 LTVs grew slightly as a percentage of our NIW to about 15%. Credit quality, as indicated by FICO, remains high across our risk in force with an average score of 743.

We remain underweight relative to the market in the greater than 95 LTV and the higher DTI products. Our single premium policies remain low at 7% of NIW this quarter versus the industry average of roughly 15%.

In the current rising interest rate environment, monthly premium products should continue to produce better risk-adjusted returns over time. The persistency of our monthly policy has increased to 82% in the third quarter and supports the allocation of more capital to the monthly products. In addition, to maintain a credit quality of our in-force book, we increased our protection for mortgage tail risk by completing our second and third Bellemeade risk transfers to the capital market this year, where we have become a regular issuer.

Insurance-linked notes enhanced the level and the predictability of our expected returns. As far as the new MRT programs with the GSE, the IMAGIN and EPMI facilities, they have begun to generate business. Momentum is building slowly as banks develop new systems to handle the programs. More on that later.

Now briefly with respect to our investment operations. Higher yields available in the financial markets and growth in invested assets led to a 21% increase in net investment income in the third quarter. We remain underweight, both credit and interest-rate risk, given the rising rate environment.

Finally, a few words on capital and risk management. Share repurchases by Arch are typically light in the third quarter, and this quarter was no different. While we repurchased some shares this past quarter, we have been working on a few opportunities to deploy our capital into our businesses, and we will let you know if and when these opportunities come to fruition. As to risk management, for the reasons I mentioned earlier, our property cat exposures remained at historically low level with our 1-in-250-year peak zone at 5% of tangible common equity at the end of the third quarter.

For our mortgage segment, as of September 30, our realistic disaster scenario declined, as growth in the insurance in-force was more than offset by the capital relief from the Bellemeade transactions and the continuing runoff of pre-2009 (sic) [pre-2019] business.

With regards to PMIERs, which applies to our primary U.S. mortgage insurance business as of September 30, 2018, Arch was -- Arch MI was at 151% of the current GSE capital requirements. Arch required assets exceeds both the current sufficiency ratio known as PMIER 1.0, and the revised GSE required asset as proposed under PMIERs 2.0, which is to be effective on March 31, 2019.

With that, I will turn it over to François.

François Morin
Executive VP, CFO & Treasurer

Thank you, Marc, and good morning to all. Let me jump right in and give you all some comments and observations on our results for the third quarter. Consistent with prior practice, these comments are on a core basis, which corresponds to Arch's financial results, excluding the other segment, i.e., the operations of Watford Re. In our filings, the term consolidated includes Watford Re. After-tax operating earnings for the quarter were $242.3 million, which translates to an annualized 11.4% operating return on average common equity and $0.59 per share.

On a year-to-date basis, our annualized operating ROE also stands at 11.4%, a solid result in light of challenging conditions in the P&C sector. Book value per share was $21.15 at September 30, a 2.3% increase from last quarter and a 6.4% increase from 1 year ago, despite the impact of higher interest rates on total returns for the quarter and on a year-to-date basis.

Moving on to operations. Losses from 2018 catastrophic events, net of reinsurance recoverables and reinstatement premiums were $58.2 million or 5 combined ratio points. While these losses were predominantly the result of Hurricane Florence hitting the Carolinas, we were also impacted by other events across the globe, including in Typhoon Jebi in Japan. As for Hurricane Michael, while we are still early in the process of reassessing our exposure to this event, we believe the impact to our insurance and reinsurance operations will be in the range of $40 million to $60 million on a pretax basis, given the information available at this time.

As for prior period, net losses are a development. We recognized approximately $77.6 million of favorable development in the third quarter or 6.7 combined ratio points compared to 5.1 combined ratio points in the third quarter of 2017. All segments were favorable, led by the mortgage segment with approximately $38 million favorable, the reinsurance segment at $33 million favorable and the insurance segment contributing $7 million. This level is higher than in recent periods, primarily as a result of the significant favorable development observed in our first lien portfolio in the mortgage segment, where cure rates this year continue to be materially higher than long-term averages and expectations.

The calendar quarter combined ratio on a core basis was 80.1%, while the core accident quarter combined ratio, excluding cats, improved to 81.8%, down 260 basis points from last year's third quarter. The insurance segment's accident quarter combined ratio, excluding cats, was 100% -- 100.2%, slightly higher than the comparable 2017 level as a result of elevated attritional claim activity across a small number of lines, slightly offset by lower operating expenses, resulting primarily from lower compensation costs.

In comparing the quarterly accident year results, it should be noted that the reported results can be subject to noise due to random occurrences that can take place in the lines of business we operate in.

Just as we reported that our results last quarter were enhanced by the lower frequency of large non-cat claims, the opposite result materialized this quarter. In order to detect trends in the performance of our units, we tend to focus on trailing 12-month analyses to remove some of the noise that we see from quarter-to-quarter. The reinsurance segment accident quarter combined ratio, excluding cats, stood at 92.5% compared to 96.9% on the same basis 1 year ago. As we discussed in the prior call, the combined ratio in the quarter 1 year ago was impacted by a large retroactive reinsurance contract. Given the nature of our book and the impact certain large transactions may have, fluctuations of quarterly results are not unusual and should be expected.

The expense ratio benefited from the reduction in federal excise taxes of $2.3 million or 0.8 points, as a result of the cancellation of certain intercompany property casualty quarter share agreements effective January 1, as discussed in prior calls. This item will continue to impact comparisons of 2018 to 2017 results.

The mortgage segment's accident quarter combined ratio improved by 410 basis points from the third quarter of last year as a result of the continued strong underlying performance of the book, particularly within our U.S. primary MI operations. The calendar quarter loss ratio of 3.2% in the third quarter of '18 compares favorably against the 12.8% in the same quarter of 2017 due to substantially lower delinquency rates. 570 basis points of the difference or $17.1 million, is attributable to increased favorable prior development, while an additional 280 basis points of the difference or $8.3 million is attributable to favorable development on 2018 delinquencies, due to very strong cure activity in the period. The expense ratio was at 21.4%, slightly higher than in the same period 1 year ago as a result of a higher level of acquisition expenses due to increased amortization of deferred acquisition costs.

These figures highlight the contribution to our pretax underwriting income from the mortgage segment, which remains strong this quarter. After allocating corporate items such as investment income, interest expense and income taxes to each segment, the mortgage segment's contribution to our 2018 year-to-date net income decreases to approximately 70% of the total after normalizing our results for catastrophic activity.

Total investment returns for the quarter was a positive 31 basis points on a U.S. dollar basis and a positive 37 basis points on a local currency basis. These returns were impacted by the effects of higher interest rates on investment-grade fixed income securities, with marginally higher returns on alternative investments and non-investment grade fixed income.

During the quarter, we continued to shift our allocations away from municipal bonds and into corporates due to relative valuations. The investment duration was substantially unchanged on a sequential basis at 2.94 years.

Operating cash flow on a core basis was a strong $543 million in the quarter, reflecting the solid performance of our units. Lower levels of claim payments and higher levels of investment income received explained most of the increase over the same quarter 1 year ago.

The corporate effective tax rate in the quarter on pretax operating income was 11.8%, and reflects the benefit of the lower U.S. tax rate, the geographic mix of our pretax income and a 190 basis point expense from discrete tax items in the quarter. As a result, the effective tax rate on pretax operating income, excluding discrete items, was 9.9% this quarter, slightly lower than the 10.4% last -- late last quarter.

As we look ahead to year-end 2018, we currently believe it's reasonable to expect that the effective tax rate on operating income will be in the range of 9% to 12%. As always, the effective tax rate could vary, depending on the level and location of income or loss and varying tax rates in each jurisdiction.

With respect to capital management, our debt to total capital ratio was 16.6% at September 30, and debt plus preferred to total capital ratio was 23.5%, down 290 basis points from year-end 2017 and 520 basis points from year-end 2016 when we closed the UGC acquisition.

As for share repurchases, we repurchased 414,000 shares during the third quarter at an average price of $26.48 per share and an aggregate cost of $11 million under our Rule 10b-5 plan that we implemented during our closed window period.

Since the start of the fourth quarter, we have purchased an incremental 575,000 shares at a cost of $15.3 million. Our remaining -- our revision, which expires in December 2019, now stands at $247 million after consideration of the share repurchases made through October 30.
With these introductory comments, we are now prepared to take your questions.

Question and Answer

Operator

[Operator Instructions] Our first question comes from Geoffrey Dunn from Dowling & Partners.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

I guess, first, could you update the RDS number for the MI business? And specifically, can you give us what the gross RDS is, and then the net RDS after all the ILN benefits?

François Morin
Executive VP, CFO & Treasurer

Well, I mean, we don't -- I mean, we do the gross and -- we just -- we focus on the net, because there's a lot of movement there and there's a lot of reinsurance protection, as you know, that comes into play. The current number is just at about $1 billion, net of all the protections we have.

Marc Joseph Roland Grandisson
CEO, President & Director

So, I have 13%, Geoff.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

And is there any way for us to try to back into that gross number?

Marc Joseph Roland Grandisson
CEO, President & Director

Not really. From just talking to you, I guess, at some point, we might want to talk to it through it, but it's not very easily manageable, I guess, on a call like this.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

Okay. And then with respect to managing capital on the MI platform, as you consider both regulatory limitations on dividends and just overall surplus until contingencies starts releasing, is it possible to manage to an efficient cushion on a proforma 2.0 basis, as a recurring ILN assure?

François Morin
Executive VP, CFO & Treasurer

I just want to make sure -- I mean, the question, in a sense -- a cushion, yes, I mean, just to be clear, we certainly want to have a cushion above PMIERs 1.0 or 2.0. We don't think it's prudent to run a business right at PMIERs, whatever that is. So no question that, yes, as you saw, the PMIERs ratio did go up this quarter, driven by the new Bellemeade transaction we closed on in the third quarter. We're in the middle of discussions and planning around how we can extract some of that excess capital from the regulated entity, regulated mortgage entities and see what we can do with that.

Marc Joseph Roland Grandisson
CEO, President & Director

Two things to add to this. Geoff, I think that the Bellemeade transaction, as you know, are, by and large, so far, been backward looking. So you really only know after you've accomplished, or you've realized them. So your question assumes that you're going to have the same level of execution in the market going forward on a guarantee, or somewhat guaranteed basis, which we don't know if that's the case. But having said all of this, you also have opportunities that may develop, over time, in the marketplace that might mean more need for capital. And that also will cause, sometimes, delay or it's not a very immediate release of capital, as you know, with the regulatory entities in the U.S., we have to be careful and it takes a little while to go through the capital management because of all these constituencies out there.

Geoffrey Murray Dunn
Dowling & Partners Securities, LLC

It sounds like maybe it's a little too early to ask the question.

François Morin
Executive VP, CFO & Treasurer

Well, I mean, we're working on it. The answer is, it's a fact, we close on the transactions and as you know, it takes time to get approvals until that's done, and that's really what we're -- the first thing we need to do and then we'll -- once -- if and when we get those, then we'll be -- we'll have more flexibility in what we can do with it.

Operator

Our next version comes from Kai Pan from Morgan Stanley.

Kai Pan
Morgan Stanley, Research Division

My first question, just to follow up with Geoff on the MI business. It looks like last 2 quarters, your underlying combined ratio is running at high 30s, given the strong credit environment, and that's compared with last year, probably in the mid-40s. I just wonder if the credit environment remains stable, will that be a sort of a reasonable run rate for that business or other sort of like a minus/plus, like it could impact that core combined ratio going forward?

Marc Joseph Roland Grandisson
CEO, President & Director

So Kai, all moving parts that are very -- there's a lot of things going on. If anything else change, you're quite right that we should expect to have a very similar combined ratio. That's on a -- just based on the credit quality of the borrowers, it's still extremely good out there. So yes, that we would expect, if everything else being equal, which it never is, right, we still need house price to go up, with still unemployment remaining low and mortgage rates not increasing dramatically or in a significant way. So there's a lot of things that need to happen for this to be -- for the shorter term, yes, we would expect this to be a sustainable combined ratio.

Kai Pan
Morgan Stanley, Research Division

Okay, that's great. And then switch to the reinsurance side. We have heard a lot of sort of new demand in the marketplace in the casualty, as well as this year's cat activity is not quite. It's not like as large as last year, but we have some adverse development from last year's expense as well. So what's your outlook for January renewals? If you can talk both on the property cat side and as well as ongoing, sort of, like pricing on the casualty side as well.

Marc Joseph Roland Grandisson
CEO, President & Director

So let me take the property cat. I mean, it's still early, right? We're a couple of months before the renewal of the January 1s. The market is still flushed with capital. So there's a couple of things going on there that brings a lot of dynamic as we get towards 1/1. Based on our results, the losses that we've seen over the last 2, 3 years, we would expect it to be at least -- there should be at least some price increase to recognize the fact that the long-term average -- the short-term average is probably not going in the favor of the insurance companies and the reinsurance companies. So we would expect that to have an influence on the renewals but however capacity is plentiful and there's a lot of alternative capital that could come and change it. So we'll have to wait and see what happens. It's not a clear-cut answer from that perspective. On the casualty side, it's a very tough place to be. The result from the casualty, we're not a big casualty reinsurance player. What we see -- what you see in our casualty segment is not at all the GL, the general liability or the traditional casualty reinsurance. We still feel this is too competitive for our own taste. The fact that people want to buy more reinsurance might indicate to me that there's a lot -- there are -- there's a willingness and a desire to share or at least to deemphasize the risk that is inherent in their portfolio. So we'll be very cautious in the way we are going about running that business. We're not as optimistic about the casualty market as people would be out there.

Kai Pan
Morgan Stanley, Research Division

Okay. Last one you made the primary insurance side. So you mentioned attrition loss is higher. Could you quantify that for the quarter? And also, you mentioned, the business results have been close to breakeven, and you have mentioned about 95% long-term outlook, and how quickly we can get there?

Marc Joseph Roland Grandisson
CEO, President & Director

Not soon enough, right? I mean, that will be the right answer. I think that we've seen the trailing 12-month combined ratio, hovering around 99% this quarter, yet did have larger attritional losses. I think it's 2 to 2.5 points impact on the quarter, which would have put this quarter in line with the other ones. But on a trailing 12 months, we're pretty much at the 99% number. And this is the one that we tend to focus on. Any one quarter does not make a trend. And as you'll remember, we had large losses on reinsurance last quarter that we didn't have in this quarter. We had it in insurance. So there's a lot of volatility going around those -- given the specialty lines that we write. I think that we also look at this in the sense of the overall market being softer and conditions not strengthening any better, with some rate increase. It just makes us be that much more prudent. When there's a large loss that comes in, most of the time, ID&R would be made up -- would be there to make up for that loss, but we tend to take a more conservative approach to this and maybe not fully take a -- may not take the full impact on the ID&R and remain the -- leave the ID&R at the same level and take the large loss as it comes because we're not sure that the fundamentals are improving as much as we would hope they would be.

Operator

Our next question comes from Mike Zaremski from Crédit Suisse.

Michael David Zaremski
Crédit Suisse AG, Research Division

Starting with mortgage insurance. In the prepared remarks, you mentioned that momentum is building for, I think, you said some of the bigger banks to handle some of the adjustable mortgage insurance pricing. Is that, you think, helping you maintain your market share position? Because I think your market share jumped up a lot in 2Q, and I think it still stayed higher than expectations, which is a good thing, this past quarter.

Marc Joseph Roland Grandisson
CEO, President & Director

I'm not sure what part of my remarks you mentioned -- you referred to, but the thing about our ability to increase market share and being that relevant to our clients is most of the clients that embraced risk-based pricing are actually the ones who are getting market share in the industry. And that's been a phenomena that's been going on for several quarters. So yes, by virtue of us being -- there's much more nimbleness, if you will, the more in the nonbank loan originators than there are in the larger banks out there, and I think that for the first -- for the recent quarters, I think there's been a recognition that the larger banks might be losing market share to those nonbank loan originators and RateStar actually works much better for those loan originators and actually helps them win business. So that's actually helping us grow market share or maintain our market share, at the very least.

Michael David Zaremski
Crédit Suisse AG, Research Division

Okay, that's a good nuance to know. Sticking with mortgage insurance, I know this is probably difficult, but is there any way to -- that we could maybe try to size up how to measure how much could be left in terms of like the pace of reserve releases if the cure rates continue to be significantly lower than historically? I mean, I guess, I don't know if you're using a 2-year average or 3-year or a 10-year historical average. I'm assuming you're not just assuming the rates that we've seen in 2017, '18, kind of overlay on the entire portfolio. But just kind of curious if there's anything we can look at to better understand and size up how that could trend, if things do stay good for the foreseeable future, as you kind of mentioned in your prepared remarks in terms of your outlook for MI?

Marc Joseph Roland Grandisson
CEO, President & Director

Yes, I'll say a couple of things on that. First, I mean, yes, delinquency rates are at very low levels. So we don't think they're going to go much lower than that. But the reality is the performance has been very, very good. As you know, the reserving methodology in the mortgage segment is very much more of a mechanical prescribed exercise. There's a lot less flexibility in the mortgage segment than there might be in the P&C side. So if the delinquencies are there, yes, we can put up reserves for it. And if they're no longer there or they cure, the reserves come down. So it's -- there's no in between. Is it delinquent? Is owned and delinquent? Yes or no. And from there, the models we've built produced the estimates we carry or the reserves we have in the books. So to answer your question, I think maybe there's a bit more to go, but I think to be honest, it's been -- the level that we saw in this quarter have been extremely high and probably higher than any of us here expected. So if it happens again next quarter, well, I'd be surprised. I'm not saying it can't happen, but it would be a, again, a continuation of very favorable trends that the whole industry is seeing. We're not the only ones, as you know, that are seeing these trends and -- but again, I don't think they'll be -- they're sustainable for an extended period.

Michael David Zaremski
Crédit Suisse AG, Research Division

Okay, great. And then lastly, just on capital. You mentioned that, looking on -- looking at some new opportunities, I know you guys are always opportunistic and looking at things. Just curious if you can give us a flavor, whether it's primary insurance or reinsurance, or MI, or all of the above, that you're kind of looking at?

Marc Joseph Roland Grandisson
CEO, President & Director

It's pretty much all of the above that are possibilities. And I think -- and we'll be communicating with the market as and when we find out, if they do find out and come up to fruition. So yes, the answer is all of them.

Operator

Our next question comes from Elyse Greenspan from Wells Fargo.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

My first question is going back to the discussion on your insurance business. So, obviously, the higher non-cat losses drove the increase in the quarter. But I'm just trying, as we think about going forward, and you guys getting to kind of that 95% target, can you just give us a little bit more color on what you're seeing on the -- with inflation? Anything that you guys are watching out for as you think about setting your picks and as we think about the margin outlook for the business for 2019?

Marc Joseph Roland Grandisson
CEO, President & Director

Yes. So the trend is a very interesting and important discussion. The problem is nobody will really know what it looks like until 5 or 6 years from now. Historically, trends in the insurance industry has been outpacing the core CPI increase, and we've seen the CPI at about 1.7% to 1.8% over the last 4 or 5 years. And -- which would mean to me that a trend -- and if you look at the spread over that historically, it was 100 bps above that. So the inflation on claims, for insurance claims is always higher than CPI. I just want to make sure it's clear here. We've seen 250 bps above this over the last 4 or 5 years. So there's a lot of uncertainty on this. We're trying to -- we do 2 things, right? And one of them is portfolio construction. We try to focus on more primary policies because we think that the excess portfolios will have a lot more uncertainty in terms -- if we turn out to be wrong on the trend in the pricing, the trend is going to impact the excess insurance market a lot more than the primary market. And then second, are pricing for those kinds of -- those kinds of trends will give us a range around those trends and putting a cushion that would not wrong -- on the wrong side of the decimals when we actually produce the returns -- the results. There's all sorts of other things, Elyse, that help us. We could buy reinsurance to help us shape around the expected -- the margin. But by and large, it's a give and take and through with the marketplace. And with portfolio

construction, and also focusing on the line of business where -- you heard us talk about travel and property, right? Those 2 lines of business would be lines where inflation is a lot less relevant. Because you're going to tend to find out inflation into a year is much quicker than, let's say, an E&S casualty or high excess workers comp.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Okay, great. And then in terms of the tax rate, I know there's potential for some changes as we get closer to the end of this year. Do you still think your rate will kind of stay in that 9% to 12% range as we think about 2019?

François Morin
Executive VP, CFO & Treasurer

Too early to tell. We think it's not a bad place to start. We're in the middle of planning for 2019, and all I can say is we'll give you more color in -- with the year-end call, I'd say. Once we are into '19, we'll have more visibility on how things are shaping up and the mix of business and what jurisdictions and how we think that'll play out.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Okay, great. And then one last question on mortgage. Your market share seems like it might have grown a little bit this quarter. Could you -- maybe, slightly around 25% or a little bit higher. You had been taking that down after the deal, and then it started to come back up earlier this year. I thought you guys kind of got ahead with RateStar than some of the others in adjusting your pricing. And so others probably kind of caught up this quarter. So I just want to get a full sense of what's really -- do you see kind of that 25% or so as a share that you would expect to maintain? And how should we think about that going forward?

Marc Joseph Roland Grandisson
CEO, President & Director

So first, we don't run the business, as you guys know, on a market share basis. We just provide our rate -- our best foot forward with our rates in our approach to risk-based pricing and try to give good service to our clients and provide them with good products. And at the end of the quarter, we count, then we look at where the chips fell, and we just -- the share is what it is. We have no design for market share. We had -- when we do a UG acquisition, we have thought about, we had indicated, we might be lower 20s, fiber to -- some of it was fiber to the singles being less of a relevance -- relevant product, and we have delivered on this. And we like the monthlies. I guess, there's no answer, basically. I don't know where we're going to be. I just know that what we've done this quarter generated x market share, and we're happy with that. I don't know what the future holds for us.

Operator

Our next question comes from Josh Shanker from Deutsche Bank.

Joshua David Shanker
Deutsche Bank AG, Research Division

There was an earlier call from Genworth who said that they lost a major U.S. customer. I'm wondering how that shapes up in the market, and whether you'll get the same share of a large customer that the rest of the group did or is your market share in such a way that it's harder for you to take a big chunk out of that new opportunity, per se?

Marc Joseph Roland Grandisson
CEO, President & Director

I think we're in the same market as Genworth from that perspective, right? I mean, there are large customers, and that happens all the time, that might decide to reallocate between provider of -- providers of mortgage insurance for various reasons. There's no grand design here. I think that this -- it could happen to us, it's happened to them, and we could -- we might be gaining what they lost and vice versa. There's nothing really magical there, Josh. I can't read much into it, much more than this.

Joshua David Shanker
Deutsche Bank AG, Research Division

Okay. And I saw there's decent amount of growth in property, marine, aviation, that's a pretty big catch all for a lot of things in insurance. What's going on exactly?

Marc Joseph Roland Grandisson
CEO, President & Director

It's really property. A lot of it came out of the, mostly London, cat-exposed business that went through substantial rate changes, rate increases as a result of the 2017 cat events in areas like Texas and the Caribbean. So this is most of where the increase came from on the insurance side. On the reinsurance side, very similar story. You'll see that the property also grew dramatically. We have some growth in marine, but it's largely driven by property. And for the record, it's not aviation, just want to make sure we're clear, it's not aviation.

Joshua David Shanker
Deutsche Bank AG, Research Division

Does this business have a lower normalized combined ratio than the aggregate book? And what I'm getting at is, is this going to cause, 1 year from today, the combined ratio, all things equal, to lower than it is now?

Marc Joseph Roland Grandisson
CEO, President & Director

Everything else being equal, it should. I think that, that property cat-exposed insurance or reinsurance business will have a combined ratio of probably 60 to 70, 75, whereas in more or less property -- that's cat exposed. This is absent in any cat, right? If there's a cat, of course, it could be a lot worse, right? So yes, you're right, it will depend on the cat activity in the year. But, all things being equal, your assumption is right.

Operator

Our next question comes from Meyer Shields from KBW.

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

You talked a little bit about lower other expenses, I guess, you saw that in reinsurance, mortgage, and corporate. I was hoping you could provide a little bit more color, really, in terms of the sustainability of the third quarter versus prior 12 months run rate?

François Morin
Executive VP, CFO & Treasurer

Well, yes. No question that we look at our expenses. I mean, that's something that we watch very closely. And this quarter just turned out, there's always going to be movements from quarter-to-quarter. So on corporate side, yes, a little bit lower, but I wouldn't read too much into it. Sometimes, it's just timing of some cash payments or what-have-you, some expenses that we have throughout the year, so I wouldn't read too much into that. Some -- the reality on the reinsurance side is -- lower compensation, which is the direct result of the performance of the units. No question that as we accrue bonuses throughout the year, they're based on an expected ROE, which this year turns out may not be as good as it has been in prior years, and we're adjusting for that. So certainly, you would -- you think that the operating expenses should adjust over time based on the profitability of the units. And there's, the reality is there's also a couple of miscellaneous payments here and there that will move the needle. But again, the message is, yes, we keep looking at it. We're trying to be as diligent and do as good a job, making sure that we're spending in the money in the right places and making the right investments in our people, in our technology, in our systems. But there's no question, there's going to be some movements from quarter-to-quarter.

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. In terms of mortgage, I guess, were the underlying rates getting better?

Marc Joseph Roland Grandisson
CEO, President & Director

Say it again, Meyer, please. I didn't catch that?

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

I'm sorry. So the other expenses in mortgage insurance declined, I don't know, seems significantly a lot, like $7 million, $7.5 million from the second quarter to the third, and I would naively maybe expect the better cure rate to drive more incentive comps rather than last year?

Marc Joseph Roland Grandisson
CEO, President & Director

That was -- second quarter, we have accrual for a lot of equity-based compensation.

François Morin
Executive VP, CFO & Treasurer

Yes, there's a timing of the second to third quarter. Second quarter is, historically, where we've done are equity grants and there's a spike there across the board for all units. There's also, depending on whether it is retirement-age people or not, there's a different way of accounting for the grants, but that's really why comparing second quarter to third quarter is something that you got to be careful with. And just to give you a bit of a heads-up, as you plan ahead and maybe on a year overall 12-month period, doesn't make a huge difference, but we're contemplating moving the equity-based awards from the second quarter to the first quarter, so -- next year. So that might -- again, we'll give you more color when and if we get there, but that's a possibility we're exploring right now to make those all in the first quarter.

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

Okay, that's very helpful. And then bigger picture question, I guess, for Mark. If you would isolate insurance segment casualty pricing, I guess, what are you seeing in terms of rate increase accelerating, if at all?

Marc Joseph Roland Grandisson
CEO, President & Director

Whether they do or not -- most of the rate increases we've seen in casualty over the last 2 or 3 years were led by commercial auto. And it's still very hard to get significant rate increases outside of that realm. I think, as you know, Meyer, that is slowing down. I'm not judging whether it should or not. But I think that we're seeing that the rate increases are slowing down. And because they're going through 2 or 3 years of significant rate increase, we still are able to push rate increase in some of the E&S casualty that have some auto exposure. But if you don't have auto exposure, it's still not clear that you can get those rate change accelerate or getting higher. And again, I think the rate on the E&S casualty will react and will start to accelerate when and if we see losses emerging. We believe we will, but we've been wrong before so -- but since the downside of being wrong is too painful, we'd rather take a pause and take a step back and just wait for that [audio gap] -- clarity.

Operator

And I am showing no further questions from our phone lines. I'd now like to turn the conference back over to Marc Grandisson for any closing remarks.

Marc Joseph Roland Grandisson
CEO, President & Director

Yes. We understand that there were some technical problems at the start of our webcast, and we apologize for that inconvenience. There'll be a complete replay of the call available on our website within 2 hours by 2:00 p.m. Eastern. Again, happy Halloween. Thank you very much for listening and we'll talk to you next quarter.

Operator
Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program, and you may all disconnect. Everyone, have a wonderful day.