CNA Financial Corporation NYSE:CNA

FQ4 2018 Earnings Call Transcripts

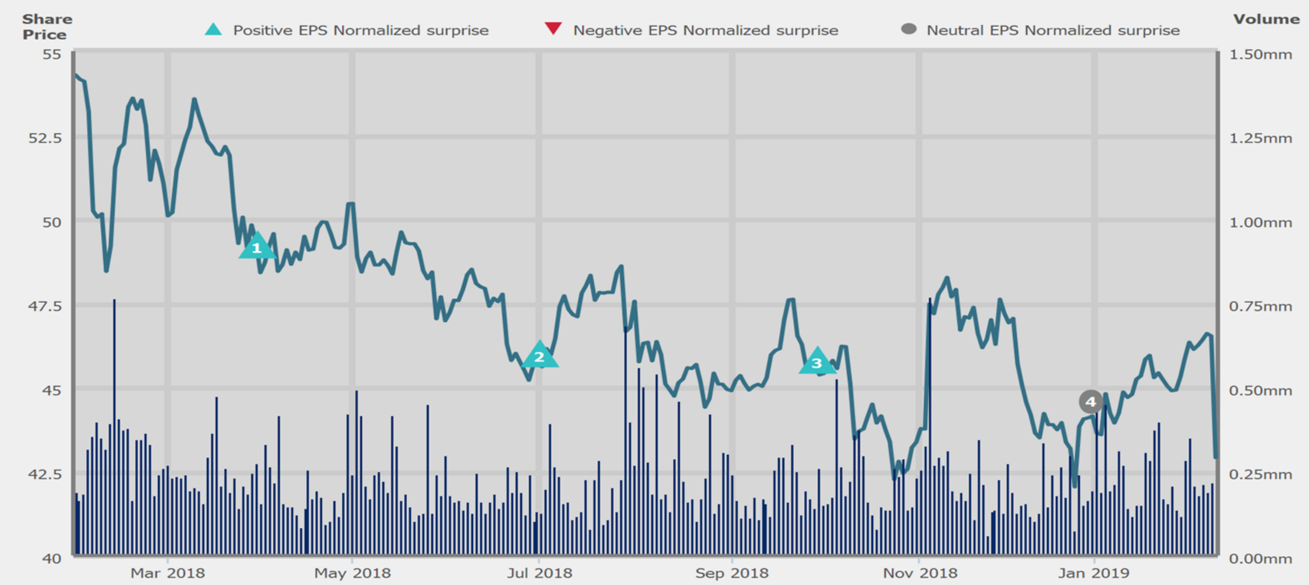
Monday, February 11, 2019 3:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2018-			-FQ1 2019-	-FY 2018-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	0.93	(0.08)	NM	1.05	4.02	3.10
Revenue (mm)	-	1659.00	-	1871.00	-	6822.00

Currency: USD
Consensus as of Feb-11-2019 12:35 PM GMT

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



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2018	0.91	1.03	13.19 %
FQ2 2018	0.98	0.99	1.02 %
FQ3 2018	1.10	1.17	6.36 %
FQ4 2018	0.93	(0.08)	NM

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Call Participants

EXECUTIVES

Dino Ennio Robusto
Chairman of the Board & CEO

James Michael Anderson
Executive VP & CFO

ANALYSTS

Gary Kent Ransom
Dowling & Partners Securities, LLC

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Joshua David Shanker
Deutsche Bank AG, Research Division

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

Samuel Hoffman
Lincoln Square Capital Management

Presentation

Operator

Good morning, and welcome to CNA's discussion of its 2018 fourth quarter financial results. CNA's fourth quarter earnings release, presentation and financial supplement were released this morning and are available via its website, www.cna.com. Speaking today will be Dino Robusto, CNA's Chairman and Chief Executive Officer; and James Anderson, CNA's Chief Financial Officer. Following their prepared remarks, we will open the line for questions.

Today's call may include forward-looking statements and references to non-GAAP financial measures. Any forward-looking statements involve risks and uncertainties that may cause actual results to differ materially from the statements made during the call. Information concerning those risks is contained in the earnings release and CNA's most recent 10-K on file with the SEC. In addition, the forward-looking statements speak only as of today, Monday, February 11, 2019. CNA expressly disclaims any obligation to update or revise any forward-looking statements made during this call. Regarding non-GAAP measures, reconciliations to the most comparable GAAP measures and other information have been provided in the financial supplement. This call is being recorded and webcast. During the next week, the call may be accessed on CNA's website.

With that, I will turn the call over to CNA's Chairman and CEO, Dino Robusto.

Dino Ennio Robusto
Chairman of the Board & CEO

Thank you, Brett. Good morning, everyone. As referenced in our press release and earning slides this morning, our fourth quarter core loss was driven principally by higher catastrophe losses and lower limited partnership investment performance. We also had some pressure on our underlying results. I'll provide some context on each of these drivers in a moment. But first, I want to highlight that for the full year, we continued to make progress towards our goal of top quartile performance. P&C underwriting profit grew 22% to $226 million, an overall combined ratio of 96.7%. And our underlying underwriting profit grew to $315 million, a 12% increase over 2017 as the underlying combined ratio improved slightly to 95.4%. Both Specialty and Commercial improved their underlying combined ratios by approximately 1 point in 2018. As well, we achieved 4% net written premium growth and are continuing to achieve meaningful rate across our P&C portfolio.

Now back to the fourth quarter, where catastrophe losses of $146 million added 8.6 points to the combined ratio. This compares with $38 million in the prior year fourth quarter, driving a $91 million after-tax difference or $0.33 per share. The losses included $88 million from Hurricane Michael and $47 million from the California wildfires. Hurricane Michael's impact was quite unique in that we only had a relatively small number of losses from the event. Indeed, 27 losses generated over 90% of the total. So even when effectively managing exposures in higher cat prone areas as we do, what was essentially a Cat 5 hurricane will cause significant damage. For the full year, the impact was more muted. Catastrophe losses added 3.7 points to the combined ratio, which is only slightly higher than our 5-year average.

The quarter was also materially affected by the investment performance of our limited partnership and common equity portfolios, which generated $138 million pretax loss compared with a $50 million gain in the prior year period, an after-tax difference of $0.52 per share. This loss was big enough to drive the full year results of this portfolio to a loss of $42 million pretax. James will talk more about this in a few minutes. So in the comparison to the prior period, these 2 items alone reduced earnings per share by $0.85. Slide 5 of the earnings presentation provides a detailed walk between the comparative fourth quarters of 2017 and 2018.

Turning to the underlying underwriting results. Our P&C underlying combined ratio for the fourth quarter of 2018 was 98% compared with 95.8% a year earlier. The underlying loss ratio was 64.4%, 3.7 points higher than the prior period, partially offset by improvement in the expense ratio. In the quarter, Commercial's underlying loss ratio was 4 points higher than the fourth quarter of 2017. Half of the increase came from loss activity and half from loss adjustment expense. The increase in loss adjustment expense was driven by severance expense in our claim department. This expense negatively affected the overall P&C loss ratio by 1 point in the quarter.

In terms of loss activity for Commercial in the quarter, we experienced large property losses that were $35 million in excess of our 5-year average, partially offset by some favorable trends in casualty in the quarter. Based on our postmortem analysis, the underwriting on the property accounts was consistent with our guidelines. So we think it is fair to expect some reversion to our longer-term mean much as we experienced following the second quarter of 2017 when I highlighted that large property losses were significantly below the longer-term average and subsequently did revert back.

On the last earnings call, I mentioned that we initiated aggressive reunderwriting in the London operation of our International business, including the full withdrawal from certain underperforming segments in our Lloyds portfolio. In the fourth quarter, International results were negatively affected by elevated property losses and professional liability in our London operations causing the underlying loss ratio to be 14 points higher than the prior year's fourth quarter. A good portion of the losses this quarter come from the areas where we are taking targeted underwriting action, which reinforces the decisions we made earlier in the year. As a result of our reunderwriting and reinsurance actions, we expect our International premium volume in 2019 to be down meaningfully as we return the underperforming operations within International to profitability. Indeed, in January of this year, our International net written premium decreased nearly 15% from January 2018.

Let me now turn to production and give you some detail. In terms of growth, P&C gross written premium, excluding the warranty captive, the large warranty captive grew 6% in the fourth quarter with net written premium up 4%. For the full year, P&C's gross written premium grew 7% and net written premium grew 4%. Rate in the quarter continued to show positive momentum increasing to plus 3% for P&C overall compared with plus 2% in the third quarter. Commercial generated 2 points of rate in the fourth quarter, while Commercial excluding workers' comp was plus 4%, up 1 point compared with the third quarter. Specialty generated 2 points, while International achieved 5 points of rate.

For the full year, rate for P&C overall was plus 2%, up from flat in 2017 with increased rate achievement on all 3 of our business segments. For the year, we had particularly good progress in Commercial ex work comp, in which rate was up 3% compared with 1% in 2017. As we move into 2019, rate in January was slightly better than what we achieved in the fourth quarter with Commercial ex work comp and Specialty overall up more than 4%. Renewal premium change was about approximately 3.5% on an earned basis for both the fourth quarter and the full year 2018, which exceeds our long-run loss cost trends. Retention was 82% in the fourth quarter, down a point from the third quarter.

New business was down 7% in the fourth quarter, coming off a very strong 25% growth in last year's fourth quarter. Despite the fall-off in Q4, on a full year basis, new business was up 13% over the prior year. Importantly, our highly profitable Specialty segment achieved new business growth of 46%. In International, new business was up 12% for the full year with over half of the increase coming from our Canadian operation, which has generated strong profitability over many years. As a result, I continue to be pleased with one of the key tenets of our underwriting strategy, just getting access to high-quality new business.

To summarize, over the past 2 years, I've talked to you extensively about our journey to get our combined ratio to be top quartile on a sustained basis. We have made significant progress in both 2017 and 2018, and our results in each of the past 2 years reflect that progress. As for the fourth quarter performance, we clearly see it as an outlier. Indeed, in the first 3 quarters of 2018, the P&C underlying loss ratio was 60.8%, which is top quartile performance. The full year underlying loss ratio of 61.8% is also a strong result. And as I mentioned, we don't expect property losses to stay at fourth quarter levels. Moreover, our underwriting actions in International, although the smaller part of the business, will have a positive impact going forward. Also, our ability to drive rate increases across our 3 business units should help margin as our long run loss cost trends are still relatively stable and benign.

Combine that with an increasingly disciplined expense culture within the company as evidenced by our 33.2% expense ratio in the fourth quarter, which is 1.5 point better than the prior year's quarter, and we feel very good about our trajectory to top quartile P&C performance. Finally, our long-term care business is on solid footing and continues to perform as expected.

And so with that, we're pleased to announce our regular quarterly dividend of $0.35 per share, along with a $2 per share special dividend. And now I'll turn it over to James.

James Michael Anderson
Executive VP & CFO

Thanks, Dino, and good morning, everyone. Our Property & Casualty operations produced a pretax underwriting loss of $92 million in the fourth quarter, driven by elevated catastrophe activity. For the full year, underwriting profit was 20 -- $226 million, a 22% increase over 2017. Our P&C expense ratio improved to 33.2% in the fourth quarter and is in line with our current run rate. For the full year, our expense ratio was also 33.2% or 1 point lower than 2017 with approximately half of the improvement coming from each of premium growth and reduced expenses.

Prior period development was favorable 1.2 points in the quarter and 2.4 points for the full year. These results reflect the outcomes of the reserve studies completed in the fourth quarter, and our reserve position remains strong. Our Specialty segment had 3.7 points of favorable development in the quarter and 5.5 points for the full year. Both Commercial's and International's prior year development was negligible in both the fourth quarter and the full year.

Moving to each of our individual P&C segments, Specialty's underlying combined ratio for the fourth quarter was 94.3%, a slight improvement from the fourth quarter of 2017. Specialty's overall combined ratio for the quarter was 91.2%, including favorable development, primarily in accident years 2015 and 2016, driven by both surety and professional liability.

For the year, Specialty's underlying combined ratio was 92.7% or more than a full point of improvement compared with 2017.

Specialty's overall combined ratio for the year was 88.2%. While Specialty's fourth quarter rate rounded to 2% as it did in the third quarter, there was actually a slight quarter-over-quarter improvement as we achieved higher rate in both healthcare and in our financial institutions businesses. In January, Specialty's rate is higher than the fourth quarter level.

Our Commercial segment's underlying combined ratio for the fourth quarter was 96.9%. The underlying loss ratio of 63.9% was driven by property losses and loss adjustment expenses, as Dino described. The fourth quarter overall combined ratio in Commercial was 113.3%, including nearly 16 points of catastrophe losses. For the year, Commercial's underlying combined ratio was 95%, nearly a point better than the full year 2017.

Commercial's full year overall combined ratio was 101.1% or more than 1.5 points better than 2017. Commercial's fourth quarter rate ex workers' comp improved to 4% with Commercial Auto getting 7% and Property 4%. In January, these levels were even stronger with Auto at 8% and Property getting 5%.

Our International segment generated a combined ratio of 119.5% in the fourth quarter, driven by large property losses and professional liability in the London market. For the full year, International's combined ratio was 106.5%. And in the fourth quarter, International achieved rate of 5% compared with 4% in the third quarter.

Our Life & Group segment produced $7 million of core income compared with $31 million in the fourth quarter of 2017. The prior year quarter included $27 million after tax from a favorable claim reserve review. You'll recall that this year, the claim reserve review was done in the third quarter and resulted in a favorable $24 million after-tax impact, driving a difference of $0.09 per share compared with the prior year period.

For the full year, Life & Group produced $43 million of core income compared with $50 million in 2017, 2 very good years for this segment. Long-term care morbidity experience continued to be consistent with our reserve assumptions, while persistency remained favorable.

Our Corporate segment produced a core loss of $46 million in the fourth quarter. This loss was driven by our second asbestos and environmental reserve review of 2018. We've historically concluded this review in the first quarter of each year, but as I mentioned on last quarter's call, this now gets us onto a fourth quarter schedule going forward. The result of this review was a noneconomic after-tax charge of $28 million, driving a difference of $0.14 per share compared with the Corporate segment's result in the prior year period. So the year-over-year comparison of Life & Group and the Corporate segment combined was down $0.23 in the fourth quarter due to timing changes of reserve reviews in each.

Pretax net investment income was $334 million in the fourth quarter compared with $505 million in the prior year quarter. This change was driven by our limited partnership and common equity portfolios, which produced a pretax loss of $138 million, a negative 5.7% return compared to a $50 million gain last year. For an LP portfolio constructed with 2/3 of its assets in hedge funds with a long bias, it is not a terribly surprising result in a quarter in which the S&P 500 Index was down 14%. Nonetheless, given this volatility and the fact that some of the funds have not performed as expected over the last several years, we are going to take actions to reduce our hedge fund exposure in 2019.

Pretax income from our fixed income security portfolio was $465 million this quarter, which was slightly higher than the prior year's quarter. The pretax effective yield on the fixed income portfolio was 4.8% in the quarter, again slightly higher than in prior periods.

Fixed income assets that support our P&C liabilities had an effective duration of 4.4 years at quarter end, in line with portfolio targets. The effective duration on our fixed assets -- fixed income assets that support our Life & Group liabilities was 8.4 years at year-end.

Our balance sheet continues to be extremely strong. At December 31, 2018, shareholders' equity was $11.2 billion or $41.32 per share, down from year-end 2017 due to a decrease in our unrealized gain position as investment yields have increased. Shareholders' equity, excluding accumulated other comprehensive income, was $12.1 billion or $44.55 per share, an increase of 6% from year-end 2017 when adjusted for the $3.30 of dividend per share paid during the year.

Our investment portfolio's net unrealized gain was $1.5 billion at year-end.

In the fourth quarter, operating cash flows were $359 million. We continue to maintain a very conservative capital structure, and all our capital adequacy and credit metrics are well above our internal targets and current ratings.

With that, I'll turn it back to Dino.

Dino Ennio Robusto
Chairman of the Board & CEO

Thanks, James. Before we move to the question-and-answer portion of the call, let me leave you with some summary thoughts on the year's performance. The full year underlying combined ratio of 95.4% improved for the second straight year and is the best in a decade. We had net written premium growth of 4% for the year. We had 2.5 points of favorable prior period loss development and remain confident in our reserve position. I'm encouraged by our pricing trajectory in recent quarters. And based on what we have seen in January, I'm optimistic that we can continue to drive rate above our long-run loss cost trends. Our long-term care business maintained positive margin in the active life reserves even as we moved to more conservative reserving assumptions. We increased our regular quarterly dividend during the year to $0.35 per share, and we once again declared a special dividend of $2 per share.
And with that, we'll be glad to take your questions.

Question and Answer

Operator

[Operator Instructions] And first from Deutsche Bank, we'll hear from Josh Shanker.

Joshua David Shanker
Deutsche Bank AG, Research Division

I'd like to hear a little bit -- now you said you're pulling onto some hedge funds and what not. Can we talk a little about what you think the right investment philosophy is with your nontraditional investments? And is the problem that you were invested in hedge funds or that you were invested in the wrong hedge funds? Is there something that is going to change about how you view your strategy for those types of assets?

James Michael Anderson
Executive VP & CFO

Well, Josh, I would say that, as I mentioned, we are going to reduce our exposure to hedge funds. Really, when you look at that portfolio, it is heavily tied to the equity markets for better or worse. And we have 2/3 of it in hedge funds. The 1/3 that's in private equity has performed very well, and it's had much less volatility. It -- I think it's less about the amount -- or the hedge funds that you pick and more about the exposure that you have directly to the equity markets, the way that, that portfolio has been constructed. So we're going to shift that mix going forward to have less of it in hedge funds, more of it in private equity as well as more in our fixed -- parts of our fixed income portfolio.

Joshua David Shanker
Deutsche Bank AG, Research Division

And does that achieve something in relationship to your underwriting? Is there a holistic view about what you should be trying to do on the investment side versus what you should be trying to do on the underwriting side?

James Michael Anderson
Executive VP & CFO

Yes, clearly, we're looking at our risk portfolio across [price], and we want to ensure that we're not taking too much risk on the investment side as we continue to grow our business on the underwriting side. So we are looking across the overall risk tolerance to ensure that we're putting our risk chips where we think we have the best performance.

Joshua David Shanker
Deutsche Bank AG, Research Division

And as we try and model out the volatility associated with the nontraditional assets, obviously, there's been a big rebound quarter-to-date in the markets. I'm not sure how to think about that. And as you pull down from these exposures, is that a 1-year or a 2-year situation? Like, how quickly does that change the volatility associated with the investment portfolio overall?

James Michael Anderson
Executive VP & CFO

It will take -- this reshuffling will take a full year as we do redemptions at different gating time periods for different funds. So it's not something that you do all at once. We had experienced in January the rebound. So we are seeing that in the portfolio. And you'll see, as you monitor it and as we talk, as we go quarter by quarter, how that assets are going to shift over that time period.

Operator

Our next question will come from Jay Cohen with Bank of America Merrill Lynch.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Let's say, starting with the International side. I wanted to hear more about the higher liability costs in the quarter. Was there essentially some current year catch-up in booking that loss ratio?

Dino Ennio Robusto
Chairman of the Board & CEO

Okay. So Jay, it's Dino. Thanks for the question. So the professional liability in the quarter is related to our architects' and engineer and contractors' professional liability portfolio. Based on the loss activity, in the quarter, we did a postmortem, and we're going to adjust some terms and conditions on some of the accounts in the book in International. And if we get it, what we need pricing deductible, so if we get what we need at renewal, that will be good. If we don't, we'll get off of those accounts. And there's really nothing more significant than that. And truthfully, Jay, we should know, and we do know because, as you may know, we have a very large architects and engineer experience and exposure here in the United States. We've had it for decades. We've made a lot of underwriting profit. We've got underwriting talent. We've got claims talent, risk control talent. So we know how to look at this portfolio. We know what we need to do on the accounts on the International. And we've already started. And if we get it, good. And if we don't get it, then we'll not renew those accounts. So that's it. It's not really more significant than that, but it affected the fourth quarter at a time where there was other things that affected the quarter.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

But on this liability business, basically, it was like, your -- for the full year, your booking. In other words, you're kind of restating, to some extent, the first 3 quarters of that business?

Dino Ennio Robusto
Chairman of the Board & CEO

To a certain extent, yes. But clearly, the exposure was something more in the later part of the year, without a doubt.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Got it. Secondly, internationally, if you're cutting the premiums the way you expect to drive profitability, will -- should we expect to see some expense cuts in that business as well?

Dino Ennio Robusto
Chairman of the Board & CEO

Yes, definitely. So listen, I mean, I think, if you take a look at the lines of business that we're exiting and that we talked about in the third quarter, you're probably looking at about it representing somewhere between 10% and 15% of the International premium. So obviously, we're going to deal with expenses accordingly. We're going to continue to grow the rest of it in our target markets, even in the London operation, but clearly, our Canadian operation and other profitable parts of it. It's not going to offset -- we don't expect it to offset the decrease. So we will contend with the expenses, and we already have started to contend with them. So clearly, we would do that.

James Michael Anderson
Executive VP & CFO

And Jay, I'd just add on that. We wouldn't expect that our overall expense ratio in 2019 would be affected by what's happening in International.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

That's helpful. Last question. The expense ratio in the fourth quarter. Did it benefit at all by a lower level of bonus accruals just because of the profit challenges in the fourth quarter?

James Michael Anderson
Executive VP & CFO

It did not, no. And in fact, if you look at our Specialty business as an example, they had an 88% combined ratio for the year and their expense ratio was slightly higher as a result of that.

Operator

And next we'll hear from Meyer Shields with KBW.

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

It looks like we saw bit of a sequential slowdown in reserve releases. And I was wondering whether that is at all connected to, say, the worsening professional liability experience or some other underlying catalyst?

James Michael Anderson
Executive VP & CFO

Meyer, it was actually not. So we have a long history of having favorable reserve development over time, and the quantum varies from time to time. We look at different products every quarter. We make reserve release decisions based on the movements on those quarterly reserves. So you really shouldn't expect any kind of a trend in reserve development, whether it's quarter-to-quarter or year-to-year, just not how it works. We feel very comfortable, as I mentioned, about our reserve position, both -- really in all 3 of the segments. Specialty for the year had 5.5 points of favorable development, that's down from 2017's 7.7 points but still very robust outcome. International was essentially flat for the year. Commercial was essentially flat for the year, both had pluses and minuses inside. So I wouldn't look at any of those trends, no matter what segment you're looking at, and suggest that there's going to be some trend going forward as a result of either the quarter-over-quarter or year-over-year period.

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

Okay. That's very helpful. And I was hoping that you could talk a little bit about planned reinsurance purchases over the course of the year?

James Michael Anderson
Executive VP & CFO

Planned reinsurance.

Dino Ennio Robusto
Chairman of the Board & CEO

Well, yes, right. What I would just say is that, and you can see it, we've talked about it in the quarters. We are purchasing some additional reinsurance, where we think it makes some sense to continue to help with volatility. And we'll continue to take a look at reinsurance through the course of the year. And if we can find something that we think is going to help the risk return profile of the portfolio, then we would continue to consider it, and we will see how that plays out. But clearly, we are using reinsurance more actively than CNA has in the past, clearly, over the last 2 years. And that's the right thing to do based on the reinsurance market and the opportunities and the pricing out there. And the good news is that when we do approach them, they're comfortable with how we look at business and the quality of the underwriting talent and we feel we get access to great terms and conditions. So that's a good thing. So we'll continue to monitor it during the course of the year and then happy to talk about it.

Operator

Next question will come from Gary Ransom with Dowling & Partners.

Gary Kent Ransom
Dowling & Partners Securities, LLC

I believe you said it was $47 million from the California wildfires. Did the losses there change your view on what you need to do and how to underwrite in California and particularly for the wildfire exposure?

Dino Ennio Robusto
Chairman of the Board & CEO

Yes. Gary, it's a -- listen, it's a good question. And we looked at Hurricane Michael, we look at the California wildfires, you're always going to do a postmortem. First of all, I mean, I think, I believe the sort of latest estimates at about somewhere between $15 billion and $20 billion for the California wildfires. So $47 million is not an outsized loss. Having said that, there are a couple of accounts where when you think about it, you say, look, we want to be a little bit more careful or we want to watch our limits profile in certain geographies, in the camp area, et cetera. And so we'll make some tweaks to our underwriting. We should. We always do and -- but there isn't any big sort of wholesale change that we're looking at within -- in the California wildfires both this year and last year. I think relatively not outsized losses for what the industry was. But there's things we learn and we act upon it. We act always upon every catastrophe situation.

Gary Kent Ransom
Dowling & Partners Securities, LLC

I know it was not outsized in the context of the industry, but I'm just thinking in context of you not really writing homeowners insurance where most of the loss was. And so this is all commercial or small commercial. It seems like it was maybe a little bit bigger than you might have thought, but...

Dino Ennio Robusto
Chairman of the Board & CEO

I mean -- we didn't really think -- I mean, listen, Gary, I can understand clearly. I mean, it gets -- the wildfires impact homeowners more. We didn't really look at it as outsized. The postmortem is just a function of something that we did, we always do. And there is some learnings that we've already embedded in our underwriting guidelines. But I didn't want to suggest any wholesale change when you look at our, sort of, market share commercially in California vis-à-vis the overall. Now a wildfire is a little bit trickier to use market share, but nevertheless. So some things there to be learned.

Gary Kent Ransom
Dowling & Partners Securities, LLC

All right. And I wanted to ask about loss trends also. You mentioned a couple of times they remain benign and still get the rate above loss trends. Can you give us any sense of what's going on with the loss trends right now?

James Michael Anderson
Executive VP & CFO

Gary, I would say our loss trends, certainly from the third quarter, really haven't changed much. We're seeing, in many cases, benign certainly, and when we look at workers' comp, we're still seeing benign frequency, although it's not quite as negative as it was a couple of years ago. We're not seeing severity come back into that book yet. So overall, our loss trends are pretty stable.

Dino Ennio Robusto
Chairman of the Board & CEO

And Gary, if the rate increases persist, right, then that's a good thing, Gary. Question is, what are they going to be 12 months from now? And we don't really know that. But what we do know is we're clearly more optimistic today on pricing vis-à-vis the loss cost trends than we were 12 months ago.

Gary Kent Ransom
Dowling & Partners Securities, LLC

All right. If I could just do one more. I believe a lot of your hedge funds are real-time or maybe a large chunk of them. And I just wondered is that true? And is -- are there some that maybe are a month lag where there might be a little bit more to come in the first quarter?

James Michael Anderson
Executive VP & CFO

Yes, Gary, the vast majority of our hedge funds are real-time. We do have a few that are on a 1-month lag. But I'll tell you, even in the January performance, we had a couple come in negative as a result of that. But the vast majority are very positive just with the market movements that we've seen.

Operator

[Operator Instructions] We'll move on to a follow-up with Josh Shanker from Deutsche Bank.

Joshua David Shanker
Deutsche Bank AG, Research Division

Dino, I think it's your 3-year anniversary that's passed recently. I don't know if things are part of a 1-year, 2-year, 3-year plan, but obviously, a lot of improvements have been made. It's hard though for us to see what improvements have been made in International. Are we 3 years into the plan? Is there more work there? What should we look for as evidence that International is turning in the right direction?

Dino Ennio Robusto
Chairman of the Board & CEO

Yes, so Josh, just a point of clarification. I just came up on my 2-year anniversary. I'm not entirely sure what it means, that it felt 3 years to you, hopefully that's a positive. But it's only been 2 years. And you followed CNA over the years. The International portfolio, the London operation, in particular, has had a lot of volatility. And the reality is, it's all over the insurance wires, et cetera, that Lloyd's has continued to be in a tough situation. And the reality is that it became clear to me going into my second year, as we looked at International in 2018, that what I couldn't foresee terms and conditions changing that we were going to be able to turn some of these lines of business that we exited or that we are going to be exiting, be able to turn them around. And so the reality is, we just said, look, let's just make the decision and get rid of them because can't see a turnaround in the foreseeable future. So I think, it does make a difference when you get out of them. So we're getting out of property treaty, we're getting out of marine hull, we're getting out of first-party large construction and engineering, we put our political risk into runoff. And so the way we look at that is, you can see what kind of loss activity those lines were generating, and so you can estimate on a pro forma basis what that can do to your portfolio as it plays out, and it's going to play out in 2019. And truthfully, if it does, it could have as much as a 1 point improvement on the loss ratio in P&C. And so there is a distinction, Josh. I mean, totally fair question. There is a distinction between some trying to change terms and conditions versus exiting the lines of business and just doing what you have to do, taking the hit on the premium [Audio Gap] with the expenses and then moving most of your International operation going forward into those target segments where we do make a little bit more margin. And so you just have to take the tough decision. We took it in the third quarter, we had done a very thoughtful analysis in the 2 quarters before that going into 2018, and you're going to see it play out in 2019. So I hope that gives you a little bit of clarity on the International.

Joshua David Shanker
Deutsche Bank AG, Research Division

What does that mean for premium volume?

Dino Ennio Robusto
Chairman of the Board & CEO

So it's going to be -- those are going to represent somewhere between about 10% and 15% of the International premium. And as I said in my prepared remarks that the reality is, if you exit that, we are going to continue to write in our target market segments, even in the London operation, but clearly, we're going to continue to grow Canada, we're going to continue to grow parts of Europe and the U.K. that have traditionally been more profitable for us. So it will offset some of the 10% to 15%. I just -- as I indicated, Josh, I don't think it's going to offset the full amount, so that the expectation would be a negative growth number, less than, obviously, what we are exiting for 2019. And look, every quarter that goes by, we'll know more and we'll see how it's impacting it. And we'll talk more about it.

Operator

And moving on, from Lincoln Square we have Sam Hoffman.

Samuel Hoffman
Lincoln Square Capital Management

I just had one question. Can you explain the causes of the large property losses that affected the underlying loss ratio in the quarter?

Dino Ennio Robusto
Chairman of the Board & CEO

So -- I mean, the -- as I indicated, right, the large property losses, we quantified them for you, we look at sort of a longer-term average, it's about $35 million, mainly fire losses and -- so what we do is a postmortem on them, make sure that there is nothing within the guideline -- anything we have to change from in the guidelines. And in these particular activity, there wasn't anything. And so hence why I think it is fair, at some level to assume some reversion to a mean, as I said in my prepared remarks. Second quarter of '17, I was in the opposite position. And I clearly said on the call that some of that's luck [Audio Gap] revert back the other way. So the fire losses are what happens, and there was nothing more significant than that.

Samuel Hoffman
Lincoln Square Capital Management

Great. It seems like this is something that's been affecting the entire industry over the course of the last year or so and that you can't pinpoint anything that's unusual, it sounds like.

Dino Ennio Robusto
Chairman of the Board & CEO

No, I mean, I think, all I can say is that when you start to see things that are a little bit broader across the industry, what you're to a certain extent looking at is, you probably just need more pricing also in that line of business. And notwithstanding my comments about a reversion to some mean, the reality is, we got to push for more pricing on property. So if you look at the second quarter, we were getting 2 points of rate. In the third quarter, we got 3 points of rate. In the fourth quarter, we got 4 points of rate. In January so far, we are at 5 points of rate. And to a certain extent, that is part of a solution also going forward. When you see it broader, then one company as you have seen it affecting multiple companies, if you understand the point I'm making there.

Samuel Hoffman
Lincoln Square Capital Management

Yes. But there's no way to pinpoint the underlying cause, that it just happens to be happening at this point, for whatever reason.

Dino Ennio Robusto
Chairman of the Board & CEO

Yes. And so you try to mitigate it going forward with pricing.

Operator

All right. And it looks like that does conclude today's Q&A session. I'd like to turn the floor back to CNA's Chairman and CEO, Dino Robusto, for any additional or closing remarks.

Dino Ennio Robusto

Chairman of the Board & CEO

Again, thank you, everyone, and thank you for your questions. And we will talk to you in a quarter.

Operator

And once again, ladies and gentlemen, that concludes our call for today. We thank you for joining us. You may now disconnect.