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Call Participants

EXECUTIVES

Beth A. Costello
Executive VP & CFO

Christopher Jerome Swift
Chairman & CEO

ANALYSTS

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

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Presentation

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Good morning, and welcome. We are kicking off day 1 of the Wells Fargo Financial Services Investor Conference with The Hartford. Joining us from The Hartford are Chris Swift, Chairman and CEO; and Beth Costello, CFO; and Susan Spivak, Head of Investor Relations. If you have questions you would like me to ask during this session. You can send them to me via e-mail.

Before we get started with the Q&A, I'm going to turn it over to Chris for some introductory comments. Chris?

Christopher Jerome Swift
Chairman & CEO

Thank you, Elyse. Beth and I are really excited to be with you here today virtually. We'll get back to in person soon. But I just thought I'd start with some of the comments I have made before publicly of just how excited we are for our strategic direction at The Hartford and our ability to continue to generate superior returns for our shareholders. If I look at the macroeconomic conditions, they favor The Hartford in our employment-centric firms. You know what we've been doing to improve our underwriting and expand margins.

I would say also that excess mortality trends are beginning to return to normal. Second quarter, we're still going to be a little elevated, as we alluded to. And our Hartford Next program is really going to make us a leaner, more efficient organization for the long term.

So as we sit here today, I'm really excited about our ability to continue to expand margins, to grow organically and generate excess capital that we've committed to returning to shareholders over our 2-year period of time. And as we said in our first quarter earnings call, we are going to start to buy back shares, and we have been executing buybacks. We could talk about that further.
So -- and you put all that together, Elyse, and that's why we'd felt investors were really owed more of a forward look through '22 and into '23. We really are confident we could generate a 13% to 14% ROE. So that's all I'd say real quick as an opening and look forward to the dialogue with you.

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Question and Answer

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Yes. So maybe kicking off from there, you highlighted the 13% to 14% ROE target you guys rolled out with earnings for 2022 and 2023. So if we dissect that metric, in your mind, what are the biggest swing variables in terms of The Hartford's ability to hit that target? And what do you see as needing to happen for you guys to come in at the high end of that target range?

Christopher Jerome Swift
Chairman & CEO

Yes. I would say -- and I'll let Beth add her color. When we talk about forward views, and like we have in this particular case, I mean, we're very confident in our ability to hit it, primarily driven by the robust rate increases and some of the reunderwriting we've done in the book. So that our core performance, I think, is going to greatly improve in our Commercial Lines business and, obviously, in our Group Benefits business get a little bit back to normal. So just really bullish about what we could do and generate.

When you talk about sort of variability in outcomes and potentially at the higher end, I mean, you know our P&C business. The wind blows, the earth shakes, we have traumatic events that can change reported ROEs. I would also say that, look, if there is a little bit of lift in our investment portfolio, that can contribute to an outperformance or conversely. But again, as we look at all the variables we think we can control, we do believe we could generate that 13% to 14% ROE. Beth, would you add anything?

Beth A. Costello
Executive VP & CFO

The only other item that I would add that is contemplated in that, and Chris touched on this in his opening remarks, is all the things that we're doing with our Hartford Next program. And we've indicated before that this program is a very detailed program. We have line of sight into the various initiatives that will deliver the value that we've laid out. We just recently laid out our expectation going into 2023. And that obviously is also providing us a lift.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

That's helpful. And now maybe touching on another part of your opening remarks, Chris, you mentioned the buyback authorization, which you guys did take up with earnings. And so in terms of just thinking about buybacks, would you guys consider front-loading or taking advantage depending upon where the stock price is, to bring -- buy back more stock sooner perhaps than later? And can you just give us a sense of kind of any thoughts surrounding that and the level, I guess, that we could expect as we move through the different quarters of 2021?

Christopher Jerome Swift
Chairman & CEO

Yes. I would share and then Beth will -- she can give you more of the details, is that I think it is front-loaded. We talked about a $2.5 billion program, $1.5 billion this year, which really when we announced it was, in essence, 3 quarters of the year. So I think you're right. It is front-loaded. We think our shares are still attractive to buy in and create value for shareholders. We think it's the highest and best use of excess capital at this time.

So yes, it is front-loaded and next 15, 18 months, a lot of things can happen. And if things continue to favor positive in development, there's always the upside -- the ability to upsize the program. But I think the context of a $2.5 billion program for The Hartford over 2 years is pretty robust at least. But Beth, what would you add?

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Beth A. Costello
Executive VP & CFO

Yes, I agree with that. And I agree with your point that we did message that we were front-loading it by saying that we plan to do $1.5 billion this year. We had repurchased $123 million in Q1. We started repurchasing again after our earnings were announced in April. And through yesterday, in Q2, we repurchased about $258 million worth of shares.

So I think we're on a good pace, and we do obviously look at market conditions as well. We typically use a combination of just program, sort of trading plans just to make sure that we can always be in the market. But then we also do opportunistic repurchases as market conditions change.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

And then sticking on capital. It sounds like given the ROE that you guys have laid out and kind of the conviction in the business plan that M&A -- and Chris, I know you and Beth have addressed this in the past, is kind of very low on the list right now. But can you just kind of give us your current thoughts just how M&A fits into hitting kind of that 13% to 14% ROE target?

Christopher Jerome Swift
Chairman & CEO

Yes. You got it right. I mean it's a lower priority. Again, we think using our excess capital to continue to buy in shares at this point makes the most sense. I mean we have a robust M&A function that is always in tune with market conditions. But M&A is just a low priority for us, at least for the next couple of years, primarily because I think we've done 2 large, successful deals, integrated them.

We're fully realizing the benefits of all the product potential. We're focused on cross-selling. We're focused on organic growth. We're focused on more of our products' lines per account, as we would say internally. We want to have multiple lines with more of our clients. We're aggressively marketing ourselves to our distribution partners and making them fully aware of all our capabilities that we've built over the last 4 or 5 years, particularly. So yes, it's an organic focus and it's using our excess capital to buying shares.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

And then moving on. Another component, main driver of your guidance is just your margin outlook within your Commercial Lines business. So you guys are looking for around 5 points of underlying margin improvement over the next couple of years, that is excluding your COVID-19 losses. And you guys have said around 3 points of that is going to come from the underlying loss ratio we can get into Hartford Next in the expense side as well. But when we think about just that underlying loss ratio component, can you give us a sense of just within your different segments, so small, middle, large and specialty, where you see the drivers just of that kind of good amount of improvement that we should expect over the next couple of years?

Christopher Jerome Swift
Chairman & CEO

Sure. Well, I mean I think as you said, it's Commercial Lines focused. And if I look at our 3 major segments, I'll just provide just a little color for you. Yes, Small Commercial, as you know and you've written about, is really just a first-class operation. It's innovative, it's growth-orientated. We've rolled out our new Business Owner's Policy that really changes the customer experience from a buying side to an administrative side. And it's just a growth-orientated business that, of late, I mean, we've been producing sub-90% underlying combined ratio. So that business will continue to perform with a growth orientation and still produce strong margins and strong ROEs for us.

I think the real action is in middle and large and our Global Specialty businesses that through a variety of initiatives, from reunderwriting, portfolio steering, changing attachment points, terms and conditions as we go through the cycle, as you would say, that's where the greatest lift in our margins is going to

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come from. I think a lot of the heavy lifting has been done in both those businesses, but particularly in middle and large. And middle and large right now is really focused on taking advantage of the market opportunities and cross-selling Global Specialty products into middle and vice versa. So that is an additional growth-orientated business for us.

And as we've been foreshadowing with Global Specialty for the last 2 years since we've acquired it, we knew there was some self-help that we needed to provide that book. And I would say Vince Tizzio and the team at Navigators, along with Doug have just done an outstanding job in repositioning that book where we have a profitable book of business and that the margins are going to continue to grow from there, coupled with the robust rate environment, both in the specialty markets here in the U.S. and in London. I think all those components point to that 3 points of margin lift from loss ratios over this 2-year period of time.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

And Chris, when you -- kind of highlighting these 3 points, and we kind of just went through the segments. But within your workers' comp book, within that outlook, are you guys assuming any inflection there in terms of just the pricing environment? Or just big picture, would you expect workers' comp to just be a headwind to margins over the next couple of years?

Christopher Jerome Swift
Chairman & CEO

Yes. I think as we said in the first quarter, as Doug said, I mean, we don't expect any big shifts, up or down, at this point in time. It's still going to be a little bit of a headwind, less and less every quarter. But our outlook is not forecasting through '22 a major shift, a major inflection on margins in workers' comp.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Okay. And then in terms of another hot topic, we hear about social inflation. Courts have been closed, starting to reopen as we kind of come through the pandemic. Is a pickup within inflationary trends embedded within the margin target as we think about those 3 points over the next couple of years?

Christopher Jerome Swift
Chairman & CEO

Yes. From our loss cost trend side, I think we're really comfortable with our process and our ability to get our arms around the different components of loss cost trends and inflation is one. Social inflation is in another. So yes, I would say, again, through '21 into '22, we've appropriately picked a loss trend reflective of what we think is going to be a market environment.

Sometimes -- and I'm not picking on you, Elyse, but when you guys talk about why can't margins grow faster, I mean, that's because we're still picking conservative trends and making sure that nothing surprises us on the down side and the seasoning process we go through with reserves. So I would ask Beth to comment. But Beth, I think we got our arms around a good process to project where inflationary pressures are coming from.

Beth A. Costello
Executive VP & CFO

Yes, I agree. I mean we take those -- all of those factors into consideration in establishing our loss picks. The point around courts being closed as it relate to the pandemic -- and obviously, you saw some slowdown in loss payments because of that, we didn't reflect that in our loss picks. We knew that, that was sort of temporal and that it would start to pick up again. So we look at things over a longer period, and we don't adjust for things like that on a short-term basis.

So we always have a starting point of what happened the previous year. But again, we look then more historically at what trends have been and establish loss picks that take all of those things into

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consideration and don't try too heavily weigh what could be seen as sort of short-term good news to affect our loss picks going forward.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

That's helpful. And then another big topic is just the pricing environment. Chris, I think in your introductory comments you said something about -- referred to the rate increases as robust. So when we think about just the pricing environment, can you just kind of give us your views? Where we are today? How you guys expect that to trend kind of this year and next? And which lines in your view are still in need of a good amount of rate increases?

Christopher Jerome Swift
Chairman & CEO

Sure. Well, I think you framed it well. Yes, the rate environment has been strong, robust, particularly over, I would say, the last 6 to 8 quarters. And the simple reason for that is because it needed to be. It needed to be, given the inflationary factors that we just talked about, whether it be goods and services or social or otherwise, we needed to make up for some years of pricing being below loss cost trends. So the rate on rate environment that we're getting and hopefully will continue to come is positive, again, for our margin expansion story.

But if I look at the environment a year ago compared to where we are today, nothing's really changed, right? We're still in a lower interest rate environment. There is inflationary pressures out there. Competition is steep. There is new capital coming into the businesses more and more each day.

But I still think there is a relative discipline about the market and knowing that rate is still needed over -- or at least I think over the next 18 months. And we're still pretty bullish that the rate environment will moderate a little bit. Again, you've written about it. Some of your peers have written about it. But I mean, you put it in the context of where we've come from with rate on rate on rate in certain cases, it's still strong and will contribute to the overall margin expansion story, I think, over the next 18 months.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

And then another part as you think about your commercial business, it's just top line growth, right? We've seen some pressures over the past year across the industry just from the impact, the economic contraction due to the pandemic. So as we think about coming out of the pandemic, vaccines being broadly rolled out, how could we think about just from a top line growth perspective, just the rebound there in exposure levels? And how that could benefit you guys as we go through the rest of the year?

Christopher Jerome Swift
Chairman & CEO

Well, I think you got the components again. I'm just going to sit back and listen to you because you've got all this stuff figured out. No, I think in our -- I'll call it our forward look into '21 and '22, we did provide high-level top line guidance. But you're right, exposures are coming back, whether it be in physical exposures or, I'll call it, human bodies exposure, where we ensure a lot of workers, both through our workers' comp business and our Group Benefits business. You could see payrolls expanding. There is some, I would say, slight payroll pressure also beginning to exert itself, which should be a positive for our employment-centric businesses.

I think people's confidence to be able to spend, particularly spend on bigger-ticket items, you couple that with Washington policy potentially on additional stimulus, additional support for our infrastructure, I think we're entering a period of just a great environment to operate it within where exposures and insured values are going up. And the government is going to try to build -- rebuild our infrastructure, which, again, would be positive to the private sector.

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I'm not going to repeat the guidance that we provided, but I think we were realistic in all the major businesses from benefits to Personal Lines, given what we're trying to do with our new products and our new platform. And then obviously, we see the biggest growth potential in our Commercial Lines.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

That's helpful. And then one question that came in on Hartford Next. You guys have been successful since that was launched with that program in terms of both being able to realize expenses sooner than you expected and also raising the saves from the program. So what's led to the success, I guess, right off of the bat? And then ultimately, over time, do you see perhaps raising the level of saves again?

Beth A. Costello
Executive VP & CFO

Maybe I'll start and, Chris, you can add. But I think that from the beginning, this program got off with a lot of energy and a lot of focus. And to some extent, it sort of has built on itself. So as we achieve savings in certain areas, it's opened the door to other things that we can look at. And I think it is a very robust program when you look at what we're going to do over the next couple of years. And we've talked in the past that we -- for several years, we're very invested in growth capabilities and putting our invest dollars there.

And as we were approaching the end of 2019 going into 2020, we felt that it was the appropriate time to relook at some of those invest dollars, and can we start to invest more for efficiency gains. And so have a little bit more of a balanced portfolio of initiatives that are equally focused on growth and efficiency.

And so putting some dollars to work that allow us to expand some of our digital capabilities, use of robotics and things like that, that really help elevate from an efficiency perspective, have really started to accelerate and is part of the reason why we've been able to outperform, both in terms of timing, to your point, Elyse, and that some of the expense savings have come in sooner than we originally anticipated. And I think it's also important to remember that when we announced this program last July, we were still right in the middle of the pandemic. And so we did have a little bit of hesitancy as to how effectively could we execute on some of these initiatives given the environment that we were working in. And I think we've shown that you can work very effectively in this type of environment, and that also helped to contribute to the outperformance.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

And maybe moving on to Group Benefits. You guys laid out an outlook there for the margin next year to be stable with this year, kind of excluding the COVID-19 losses. And so when we think about the Group Benefits business, what we haven't seen yet is an impact on disability results from the pandemic. Because obviously, this economic contraction is different than any that we've seen before. So I guess we could ultimately not see an impact on disability results. It could come later. Do you guys kind of, when you put out your guidance, what were you guys kind of expecting from the disability side of the business?

Christopher Jerome Swift
Chairman & CEO

Sure. Well, I would just clarify, the short-term disability business has been impacted by COVID in a fairly meaningful way from just a claims volume side. Frequency and severity are pretty moderate there, or I should say severity is pretty moderate. People are generally out 3 weeks. But the level of activity that we've had in STD has been very, very meaningful from overall claim volume side. So I give our claims team and benefits team a lot of kudos for taking care of our customers during this particular time.

But you're right, we have not seen many claims migrate into the LTD status. There are some, but it's relatively modest, given a book of business of our size. So we continue to watch it. We are on alert to see if there's any new trends, particularly coming out of COVID, whether it be long haulers or more -- just more long-term disability. But as of right now, we haven't seen it.

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So when we look forward, and we provided that 6 to 7 margin guidance, that is our best views of where long-term trends will settle out. I think we've experienced a period of time, at least in '18 -- '17, '18, '19, where we really had robust results, particularly as prior year development was strong in LTD. We do envision a little bit of a reversion to the mean.

So we do think that 6% to 7% is still a good double-digit ROE, low double-digit ROE that will contribute into the overall value creation proposition. But the ability to earn 9 to 10 points of margin in this business is not realistic, at least in what we see in the short term.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

That's helpful. And then one of your other businesses that we haven't addressed on is the Mutual Funds business. Chris, on your last conference call, you spoke about this business as an investment for Hartford. So just as we think about the long term and just how that fits within the organization, any kind of thoughts you can add in reference to that business?

Christopher Jerome Swift
Chairman & CEO

Yes. We've always thought of it as an investment because it's sort of self-contained and it's not part of the insurance operations. It's based in Philadelphia. That is a major hub for the mutual funds industry as you know.

So -- and if I look over the, say, at the 10-year period of time, it's been really growth-orientated. It's been innovative. It's expanded it's sub-adviser relationships to complement Wellington with Schroders over the last, I think, 3 years. We've built an ETF platform or smart beta platform. So I'm trying to paint a picture of -- that's a growth-orientated and an innovative business, and that's exactly the type of investments we'd like to have.

So as long as they continue to remain development -- remain relevant in a very competitive marketplace, as you know, we're happy to own it because I think it is contributing to our value creation, long term. And if the world changes and it is not, I'll call it, accretive, we'll take another decision at that time.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

And maybe to round out the conversation because we have a couple of minutes left. We haven't touched on your Personal Lines business, right. That's a business for the industry that's really been a winner during the pandemic, just due to the lack of driving. You obviously have seen driving pick up, but different types of driving, right, less to work and just more for other types of trips. Your business, obviously, skews towards the AARP with that relationship. So just how are you guys thinking, I guess, about margins and just driving levels on the Personal Lines side just as we come out of the pandemic?

Christopher Jerome Swift
Chairman & CEO

Yes. Well, I would just say on just one bigger-picture item. That business is going through its own transformation, right? As you know, we've expanded our AARP contractual relationship for another 10-year period through 2032, I believe. We've just basically refreshed the program with them from a marketing side, the features and benefits side. We're using a cloud-based technology with Duck Creek, and we're rolling out new class plans for auto and home with embedded telematics. So it is a complete makeover, as I would say, and a really exciting time, I think, for both organizations to serve more of their members, both the youthful side of AARP members at say, 50 to 65, and then well as continued sweet spot of 65 and up.

We've always talked about, Elyse, that the driving patterns of our group is a little different than the mass market. And you would say that right now, driving is beginning to revert more towards normal. And whether it be miles driven or summertime activities coming up with, obviously, the pandemic beginning to recede and people taking more of the vaccine, people are going to, I think, travel a little bit more this

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summer. So we do expect a reversion to the mean. But I think the profile of our drivers is still going to be a little less than a mass market player. So we continue to, at least in the near term, expect a level of favorability here. But in the second half of '21, I think there is that reversion to normal, will occur more in the second half of '21 for us.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

That's helpful. And it does bring us to the end of the session. But we did -- we were able to kind of address all of your businesses, so it worked out pretty well. So I do want to thank Chris Swift and Beth Costello from The Hartford for joining us today and helping us to kick off our financials conference. Thank you.

Beth A. Costello
Executive VP & CFO

Thank you.

Christopher Jerome Swift
Chairman & CEO
Thank you for having us.

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