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Beth A. Costello
Executive VP & CFO

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ANALYSTS

Alexander Scott
Goldman Sachs Group, Inc., Research Division

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Presentation

Alexander Scott
Goldman Sachs Group, Inc., Research Division
All right. So we will get going here with the next session. Yes. First, I'd like to say welcome, thanks for being here. I have Chris Swift, Chairman and CEO; Beth Costello, CFO.

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Question and Answer

Alexander Scott
Goldman Sachs Group, Inc., Research Division

And I'm going to start with just a high-level question. In mid-2021, you put forth some financial projections. Can you talk about some of the things you've executed on, some of the things you're still making progress towards -- and what are the areas of focus here over the next year?

Christopher Jerome Swift
Chairman & CEO

Sure. Well, I would say, first, it's always good to be here with you at your global headquarters.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

We make it very convenient for ourselves.

Christopher Jerome Swift
Chairman & CEO

Yes as you should. But no, it's good to be with everyone and trying to get back to as much normalcy as we can. But I would say, over the last, say, 18 months, 2 years, I'm really pleased with the overall performance of the organization, really top to bottom. And I'll just summarize some of the stats I provided during the third quarter earnings call that I think evidence is the fact that we're performing at a high level. We've been able to grow core earnings 18%, 27% on an EPS basis given our share buyback program.

We've been able to grow our commercial top line about 1%, commercial underlying combined ratios are 88.5. If you look at what we've done with our capital, we've returned about $1.6 billion to shareholders. We raised the dividend for the tenth consecutive year. And you put that all together on a cumulative basis, we earned a 14.1% ROE for the first 9 months of the year. So I think, by any measure, we're performing exceptionally well.

But then if I take back even a further step and say, strategically, we've gotten 2 deals integrated. We've finished sort of restructuring the firm over the last 3 years. We've been investing both in our technology, digital capabilities our product sets, as I like to call it, we knew we needed to expand some of our underwriting capabilities and product breadth.

We had the distribution. We still have wonderful distribution, but we always felt we could put more through it. So we've done all that. And I'd just like to always remind investors that I think our peak performance is still to come. There's a compounding effect of all the activities and improvements and investments that we have been making and continue to do that. And if I look over the next 6 to 8 quarters, I'm still very confident in our ability to perform at this high level and continue to generate superior returns. If you really say what's the real focus, I wouldn't tell you all our detailed, really, focuses, but I would give you themes associated with -- there's still a technology journey we want to complete and that ultimately involves moving to the cloud.

There are major investments in one of our businesses, group benefits from a platform side that we needed to modernize the 40-odd year old platform. I think we're going to continue to maximize the benefit of our full product breadth, but there are go-to-market strategies that we're refining, in essence, to capture more market share. So those are just a couple of them that come to mind. And -- but first and foremost is every day, every week, every month, I mean, we got to have our hands around the levers that produce the superior results that we're generating, whether it be pricing, returns -- or excuse me, retention, new business discounts, just managing the nuts and bolts of what we are asking our underwriters to do every day is critical.

And Beth and I and the team feel very, very confident and we get our arms around all the metrics and all the data we should be seeing to make those good risk return trade-off.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

Got it. That's very helpful. Next, I wanted to get your perspective on the environment sort of more generally for commercial property and casualty insurance. We've obviously gone through a period of prolonged price increases. We have inflationary pressures on

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loss costs. When we think through all these things, how do you feel about your price adequacy at this point in your positioning and willingness to grow.

Christopher Jerome Swift
Chairman & CEO

Well, at a macro level, we feel good. We still think it is a good time to think about expanding margins from a portfolio side. As you know, everything then becomes then a trade-off by line of business and where specific lines of businesses are in sort of a cyclical nature. But you put it all together, I still feel good. And I'll tell you why specifically, generally, in an inflationary environment, P&C companies perform pretty well.

I'm sure Beth will talk about the investment portfolio, what that means. But generally, as exposures rise or values rise, there's opportunities to expand margins. So feel very comfortable that we have our arms around that environment. But then if you go sort of top to bottom on a product line basis, we still see the need to be disciplined. And I think the smart management companies and teams will continue to be very disciplined on pricing because whether there's social inflation coming out of the court system, whether they be supply chain lingering inflation, whether there be climate change, if you really want to get specific on the property market and the reinsurers are driving price there.

And then just sort of inflationary trends, I'd like to describe it on a secondary effect from all the social inflation activity. So we have to keep up with loss cost trends. I think we will, as in the industry because, one, it's needed; and two, I think everyone generally has pretty good insights into what's happening with their books. But I'll spare you by product line, some are going to enjoy double-digit price increases, I think in casualty lines and other lines like D&O are going to give back some rate. But if you put it all together, the books of businesses at least that we manage are highly profitable. And I believe they won't stay that way, again, over the next 6 to 8 quarters.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

So one of the things companies have talked about is we've discussed margin expansion has been this concept of unit exposure, and it's not just economic growth, it's also the inflation aspect, higher insured values and so forth. And I was hoping you could help us think through how impactful that's been for your margin improvement? And do we need to consider anything about that potentially becoming less of a tailwind. I mean who knows whether we get that recession and so forth. But I would think even just with some moderating of inflation, you would expect that maybe that becomes a little less of a tailwind as we look into '23?

Christopher Jerome Swift
Chairman & CEO

I'll start, and I'll ask Beth to add her commentary. Clearly, it's been beneficial. And that's part of -- if we're in a hopefully becoming a mild inflationary environment after inflation sort of spiked. Generally, that's positive. There's people at this conferences that I'm sure you've interviewed. We've talked about it on our earnings call.

I mean when you talk about units of risk, units of risk have been expanding, but that's new risk. And then conversely, if you have existing risk profiles that are getting paid more, or if insured values are going up because equipment or property values are going up, that is the component that sort of acts as rate going forward. who knows really what's going to happen in the future and where the Fed is trying to land the gross economy. But generally, I still think it's going to be helpful to us in our ability to maintain or expand margins in the future. But Beth, what would you add?

Beth A. Costello
Executive VP & CFO

Yes. The only thing I'd add to this conversation because I think it's -- definitely, as you look at the rates that we post, obviously, that has been a benefit. But the inflationary pressures have also put pressure on our loss costs. So to some extent, that rate that we're getting that is manifesting itself and that the inflation trends is offsetting some of that loss trend. So if inflationary pressures start to dissipate, we also see loss cost trends would change a little bit, too. So there's a little bit of a buffer there. So we look at it, it's provided us some protection on the loss cost piece. It's not as if all of that additional rate just goes into margin because you have to think about the cost of the goods that we're selling.

Christopher Jerome Swift
Chairman & CEO

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And I think the key point in sort of the aggregate as we sit here today and we said it in our third quarter call, we still think we're in aggregate, making about 100 basis point spread on a written basis between our cost of goods sold estimated and our total rate access price.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

That's helpful. Next one, I have views on property pricing. There's obviously been a ton of focus following Hurricane Ian, and I think some of the issues leading up to Hurricane Ian. A lot of focus on repricing of catastrophe insurance and to what degree you expose into other areas? And I guess, I'm just interested in your perspective on what do you see in terms of as a primary pricing for property, what kind of increases do you think the industry will need to make in response to all of that?

Christopher Jerome Swift
Chairman & CEO

Yes, yes, it's probably -- it's obvious to everyone here in the room. It's the most dynamic part of the market these days, particularly in the last 2 weeks of the year. I would say just again, the context of our commentary in this area is going to be we have property capabilities in small, middle, large and E&S. From a portfolio side, the Hartford is underweight property risk today. It's actually one of our growth areas. And we think it's actually a pretty decent time to sort of lean in, in a thoughtful way, but you've got to make sure that we're getting -- not on a widespread cat basis, but just wide spread property. But again, you've got to be very disciplined in making sure that you're making adequate risk-adjusted returns.

I would say, again, observations more than anything, Alex, is that those that that've had high leverage to reinsurance in their business model are probably most at risk. Those organizations that use reinsurance as a capital management tool or in some cases to manage some volatility should be fine. Prices are going up. I can look at Beth to share her point of view, but we're in the market right now and. But as we sit here today, we've already made projections on where we see our reinsurance sauce going in 2023 because we're quoting business in January 1, February 1, March 1 and April 1 right now. And our mechanism that is the true up to our final reinsurance costs once they become known and once we sort of lock in our firm order terms. But Beth, what would you add?

Beth A. Costello
Executive VP & CFO

Yes. So our cat renewals, our cat treaties have a 1/1 renewal, so that both are per occurrence, treaties. And then also, we have an aggregate, as Chris said, we're in the market now. Just to sort of size, I mean our premium associated with those programs in 2022 was a little under $100 million. So again, it's not a significant spend for us. As Chris said, we are anticipating to see increases and going through that process now. One thing that we've done to structure our program for many years is our top 2 layers that are $300 million of coverage each.

We renew 1/3 of that every year. So when we've been renewing in the past, we renew it for 3 years. And so there's always 1/3 of the contract that's coming up for -- so that helps us a little bit too, as we think about going out to the market. And our performance on our treaties has been very good for our reinsurers. I think they recognize us as a very good underwriters. So as I said, we're managing through the process. We're not looking at making any wholesale changes in our program. We'll obviously look at where the costs come in by layer and make our final judgments and share that with all of you when we report our fourth quarter earnings.

Christopher Jerome Swift
Chairman & CEO

One last point is just to remind investors, we do have an assumed reinsurance business, relatively modest, maybe about $450 million, $500 million of premium. So it will benefit from the hardening market. We consider it more of a specialty reinsurer. It's not a heavy cat-exposed type of reinsurers. So I think in terms of specialty risk, casualty risk, a little bit of surety, a little bit of trade credit, political violence and excess casualty here in the U.S., but it does have some property exposures coming from various parts of the world, including the U.S.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

So there's been some talk recently of competitive differences between the standard lines versus the E&S lines. And I thought I'd get your perspective on that. I mean, are you finding standard lines market is getting more competitive is your positioning in small business, in particular, allow you to be a little insulated from what's going on?

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Christopher Jerome Swift
Chairman & CEO

Well, I think the competitive positioning in both markets is increasing, right? It's -- they're both highly competitive markets, but still fairly rational. And when you think of us as a standard line carriers and now with the Navigators acquisition on E&S capability, where we've got over $1 billion of E&S premiums coming through the new distribution channels that the new relationships that we've had or inherited from Navigators, I'd like our positioning to be able to play in both markets. I think structurally, the E&S market is going through change and will become a larger percentage of a commercial line pool going forward just because of the great flexibility in terms and conditions and pricing that you get, particularly for property risk and maybe certain elements of excess casualty risk going forward.

So we like our positioning. We play in both, obviously. We manage both on a separate basis. So there's no conflicts. But I think we picked the right time to purchase navigators to be in the E&S marketplace, and we like our positioning.

One specific point I would just share with you maybe a little bit deeper on some of the go-to-market strategies. We do have a strategy to become a larger player in the E&S market and small commercial. So you'll see us using our industry-leading tools, which is ICON and our data and analytics capabilities to be more of a major player in the E&S side of small commercial. That's mostly a casualty play in a property play. But we think, again, with the capabilities that we have, the distribution we have, that's a logical extension of our marketplace to capture more market share.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

The next one I have is a little bit of a high-level question on your small and medium targeted market, that you really seem to have a bit of a differentiated franchise and -- what are some of the things you do that differentiate the way you distribute product? What allowed you to be successful in that part of the market that may show you from the discussion of some of the larger competitors that are talking about trying to get bigger in that area?

Christopher Jerome Swift
Chairman & CEO

I'd boil it down just simply, it's an area that we've consistently invested in over 40 years. And we've committed ourselves to the small end of business. We have great insights, great data, great tools. And it really comes down to -- and if Stephanie Buscher were here, who leads this business, he would say it's just really simply 3 things: speed, accuracy and just reliability and speed matters when you're dealing with agents and brokers that are dealing with small large volumes, but small premium values that you've got to be quick, you got to be accurate to give them a bindable quote.

And once you commit to it, you've got to press the button and it basically goes through the issuance and that's sort of the certainty side. So we've built, I think, a wonderful machine. We continue to invest in it to always be differentiated. But if you look at any outside in view, Keynova is one of those readers of firm's capabilities. We've been #1 4 years in a row. There's a 20-point difference between us and our nearest competitors. And our aim and our goal is to maintain that differentiation. Also part of it is, though, the innovation in our product sets too.

We've reinvented the BOP, our Spectrum product one is going to go through another reinvention and how we interact with that agent that is producing business for their customers. is centered to our thinking. We'll always have some experiments in other areas, Alex, but we're still committed to the agency and broker channel because that's where 95-plus percent of the premiums are these days.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

Got it. I can't do one of these sessions about me asking about social inflation. Is the course more fully reopened. I mean if you gotten enough clarity from the pipes being cleared out from the pandemic and getting through a lot of the delayed settlements and so forth, do you have enough visibility at this point to sort of know where things stand and feel like you're fully priced for that kind of an environment?

Christopher Jerome Swift
Chairman & CEO

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Yes. I mean, the nature of this area is complex, right? So point of views, and Beth will add her point -- or color, too, the court systems are fully opened but there's still a backlog, right? So most people are getting back or continuing to work in a hybrid environment. But I wouldn't say the backlogs that have cleared in any material meaningful way. There's still backlogs.

Two, all our data shows either on an aggregate basis, by region, by product line. The effects of social inflation is dramatic, meaning that awards settlements are just getting more costly to settle. And that's not even dealing then with the frequency of nuclear verdicts that everyone is exposed to. And that's sort of that halo effect or secondary effect that I talked about in our litigious society, everyone thinks they're owed more or whatever injury or event happened. And look, that's what insurance is for. It is sort of protect the businesses and individuals from liability. But I would say that the expectation of higher settlement values is real, and that's why you got to continue to be disciplined on pricing and anticipate that 6, 7, 8, maybe even 10 points of trend, that you need to get into your cost of goods sold and then you need to charge your customers the appropriate rate, work with the agents to explain them why that is needed, and it sort of becomes that cycle that you got to manage, but you got to be on top of your data first and foremost. And I think we are very much...

Beth A. Costello
Executive VP & CFO

Yes, I would agree. I mean I think you touched on all the components and how we talk about it from watching actual loss trends how we incorporate our views of that into our pricing models to stay on top of trend, and there's a very tight connection between where our claims folks are seeing, what our actuarial team is seeing, what our business partners are seeing, so we can put all that together because you don't want to get behind. And I agree with Chris that although core cave reopened, there's still -- you still sort of feel a little bit of a backlog, which we take into consideration as we make our loss for their cost

Christopher Jerome Swift
Chairman & CEO

If I could share just personally with you. I hope I don't offend anyone in the room or the firms, but the #1 invention in this area that's been absolutely terrible for American Society is litigation financing. It's fundamentally backwards, fundamentally. I mean, if you think about a system to, again, fairly compensate people are injured and then you're trying to put a profit margin on top of that for capital providers. That's b*******.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

All right. We'll pivot over to personal auto with that. So I wanted to I want to touch on is, obviously, the industry is pressured. You have a little bit of a unique business focused a bit more on the AARP group. What is your experience so far? And what do you need to do to sort of restore full profitability in that business?

Christopher Jerome Swift
Chairman & CEO

Well, it's challenging, right? And I think it's the macro environment, all personal lines carriers are facing today. So we're not immune from it. I would say that our book of business tends to be a little bit more preferred, a little bit more stable, and it's probably has a basis difference of performance compared to a national book of business, both on the auto and home. So I think the simple strategy that we laid out at the end of the third quarter is that the book just needs more rate on auto -- we've been actually fairly disciplined in keeping up with rate on the homeowner side, if you look at a 12-quarter trend. But we're going to try to get about 8 to 9 points of rate in the book in the fourth quarter. And then by mid-2023, hope to get about 14, 15 points of rate in the book so that at least on a written basis as we close out '24 -- excuse me, '23 and head into in '24, I think we have a shot to make our targeted profitabilities by the second half of '24. As things earn in, as we still expect inflation to be high but moderating. And the moderation is occurring today.

I look at used car prices quite a bit, I look at other supply chains, I look at cargo shipment all around the world. So I mean, there is a coming slowdown and I hope it continues to come and maybe even accelerate. But that's one still the great variables in terms that we're just going to have to manage. I think the only again, positive thing, particularly about our platform is -- we're rolling out a new platform that gives us greater flexibility with 6 months policies as opposed to 12-month policies and greater flexibility, particularly in auto and home, where we don't have lifetime renewability agreements.

That is important, particularly as we roll out that platform we call Prevail to about 45, 46 states in 2023, new business only, the in-force is going to stay where it is, at least for the time being. But at least the new business we're putting on our books, we could be much more reactive and responsive to the trends.

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Alexander Scott
Goldman Sachs Group, Inc., Research Division

Got it. And as we've looked across some of the mutuals and even one of the stock companies, there's been some reserve refinements over the last couple of quarters that have been sizable. So I'd just be interested in like your approach to reserving, if you've seen anything as you've kind of gone through your reserve reviewing process?

Beth A. Costello
Executive VP & CFO

Yes, I'll start. You can add anything you want, Chris. So when we look at the majority of our lines every quarter and specifically on personal lines, obviously, has been a focus. As I look at we first addressing prior years, then feel very comfortable with where we put our loss pick for '21, continue to monitor, obviously, those reserves. But things, for the most part, in line with what we expected. We had a little bit of actually favorable releases in the third quarter that related to, I think, the 2018 year in auto.

As it relates to the '22 accident year, obviously touching that very closely. And as shared previously, our loss picks for the auto line have been higher than what we would have anticipated at the beginning of the year. That's why we said in our second quarter earnings call that we anticipate it to be 1 to 2 points above the high end of the underlying combined ratio guidance that we had provided for personal lines, and I'd expect we'll be pretty close to that 2 points above.

I mean we're very focused on getting our 2022 accident year pick appropriate watching lots of trends in the third quarter has seen some increases in frequency, some impacts in bodily injury that we reacted to. And would anticipate we'll see more of that in the fourth quarter. But I feel our process is very tight. It's always difficult when trends are changing underneath, which is why we're so connected with our claims folks and really understanding what they're seeing and being able to react to that and ensure that we're providing appropriate provisions that allow us to feel good about the accident year.

So it's really just a lot of analysis, so a lot of back and forth and making our best call.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

Got it. Next topic I had was workers' comp. We've seen some of these NCCI price decreases that have come out in certain states recently. And I know that doesn't always translate exactly to your pricing a little like any given state. But could you talk high level about what are you seeing in workers' comp pricing? Are you able to achieve the kind of rate you need to hold up margins on an accident year basis there?

Christopher Jerome Swift
Chairman & CEO

Yes, I would say, again, just context for everyone. It's a line of business we know extremely well. We're the second largest provider. If you look back at the historical results and if you look at things in an aggregate standard lines, small and middle. We're operating with accident year combined ratios in the 91, 92 range. So again, still highly profitable. Generally, trends, frequency and severity have been behaving.

I would say frequency is -- we always keep a watchful eye on it and generally within expectations in aggregate. And then severity probably is outperforming our long-term assumptions at this point, but it's one of those areas you just got to really, really watch. And as Beth and I -- Beth, she talks about from a reserving side, you got to be very cautious to let the reserve season so that you're not releasing excess reserves too quickly. So I think we have our arms around that line of business very tightly, and we still like it.

We'll still try to grow it where it makes sense. But it is increasingly more challenged given the rate environment and the rollbacks of rates that we anticipate in '23. So we do anticipate aggregate rate price decreases. We'll have to see what happens with exposures, both new and higher wages to see how that might offset some of that pure rate decline. We'll have to continue to watch, obviously, frequencies and severities very closely and react appropriately. But I think we got a proven track record we know how to react and manage in various cycles in this line of business. Would you add anything else?

Beth A. Costello
Executive VP & CFO

No, I think you covered off on it all, and we usually like to start and end with what you said was it's a very profitable line for us. So even going into the year, we expected to see a small amount of margin compression in small commercial. But given overall how small proportional performs and how that book performs and the growth that we have, that for us is a good trade-off. And in middle market,

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Obviously, they feel that pressure too, but they also have been reunderwriting the book and so they've been able to compensate for some of that compression. But again, a very profitable line and we know how to manage it.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

So before we end, I want to make sure we touch on net investment income. Rates are obviously a lot higher. Could you talk about the benefit that you're getting from that? Any kind of color on where new money yields are relative to what's rolling off and how that will flow into your earnings part?

Beth A. Costello
Executive VP & CFO

Yes. So yes, we are seeing the benefit in our earnings from rising interest rates on our investment portfolio. And we talked about on our third quarter call that looking to the fourth quarter, we'd expect to see about a 10 to 20 basis point increase in the yield ex limited partnership. And probably sitting here today, we're probably closer to the high end of that than that range. And then next year, we'd expect to be another 50 to 60. So it definitely is providing a tailwind. And we've also talked about the fact that as we look at those earnings and the benefit we're seeing there, our objective with our underwriters is that we want to hold on to that benefit.

So not looking incorporate that from a pricing perspective because I think there's still some uncertainty to know where exactly rates are going to go after we get through 2023. So we're very mindful of that. The other component of our portfolio that has performed really well with our limited partnership portfolio. Again, that's comprised of about half of private equity and half of real estate funds. And on the real estate side, just had very strong performance. And when we talked about our expectations going into fourth quarter -- on our third quarter call, we're expecting for the full year to be kind of at the high end of our 8% to 10% range that we typically talk about with LPs.

I would just say fourth quarter is turning out to be another strong quarter on the real estate side. So I think from a full year perspective, we'll be above that. And the question of that then does bring up is what does that mean for 2023? And we'll have to see because there obviously can be some volatility there, especially as you pull forward sales and so forth that remains to be seen. So overall, when we look at our investment portfolio, how we've allocated the various asset classes to feel very good about how it's performed. Overall credit quality is still looking very strong. We obviously monitor that very, very closely.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

And maybe the last question that I have for you is just as we think through next year, looking into 2023, what are some of the biggest opportunities and challenges that you see for The Hartford?

Christopher Jerome Swift
Chairman & CEO

Well, as I hopefully made clear, I'm optimistic about '23 and '24 in just the platform and all the capabilities that we've built enhanced or created here. So -- but I mean, the real opportunities that I see is just competing in the marketplace with what I think is pretty good capabilities. I think I made it clear that we do want to grow our property and general liability capabilities or lines of business after we've invested or acquired some of those capabilities. So that diversification to our portfolio. We didn't talk too much about group benefits, but group benefits, I would just share with the group is back to normal, always subject to change on any mortality trends. But as we called this time last year, we thought the first half of the year would have more severe mortality trends and then the second half of the year would lighten up a little bit, and that's played out well.

But that business is a steady contributor with good tangible returns on equity in that 14% to 15% range. It's the #3 provider of core capabilities, and we've really built some other voluntary capabilities that are high margin that will continue to gain traction. And then as I said, there's other go-to-market strategies that we want to continue to maximize our distribution capabilities. So there's a lot of opportunity, I think, for us to be thoughtful providers and lean in to expanding our market share as a national company.

Alexander Scott
Goldman Sachs Group, Inc., Research Division

Great. I think we're out of time. So I'll leave it there. Thank you very much for being here with us.

Christopher Jerome Swift
Chairman & CEO

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