United Fire Group, Inc.

2024 Third Quarter Conference Call

November 6, 2024, at 8:30 a.m. Eastern

CORPORATE PARTICIPANTS

Tim Borst – *Vice President, Investor Relations*

Kevin Leidwinger – *President and Chief Executive Officer*

Julie Stephenson – *Executive Vice President and Chief Operating Officer*

Eric Martin – *Executive Vice President and Chief Financial Officer*

PRESENTATION

Operator
Good day and welcome to the United Fire Group Insurance 2024 Third Quarter Conference call. All participants will be in a listen-only mode. Should you need assistance, please signal a conference specialist by pressing star then zero.

After today's presentation, there will be an opportunity to ask questions, to ask a question, you may press star then one on a touchstone phone. To withdraw your question, please press star then two. Please note this event is being recorded.

I would now like to turn the conference over to Tim Borst.

Tim Borst
Good morning and thank you for joining this call. Yesterday afternoon, we issued a press release on our results. To find a copy of this document, please visit our website at UFGinsurance.com. Press releases and slides are located under the investors tab.

Joining me today on the call are UFG President and Chief Executive Officer, Kevin Leidwinger, Executive Vice President and Chief Operating Officer, Julie Stephenson and Executive Vice President and Chief Financial Officer, Eric Martin.

Before I turn the call over to Kevin, a couple of reminders. First, please note that our presentation today may include forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. Such forward-looking statements are based on current expectations, estimates, forecasts and projections about the company, the industry in which we operate and beliefs and assumptions made by management. The company cautions investors that any forward-looking statements include risks and uncertainties and are not a guarantee of future performance.

Any forward-looking statement made by us in this presentation is based only on information currently available to us and speaks only as of the date on which it is made. These forward-looking statements are based on management's current expectations and the actual results may differ materially due to a variety of factors, which are described in our press release and SEC filings discussed specifically in our most recent annual report on Form 10K.

Also please note that in our discussion today, we may use some non-GAAP financial measures. Reconciliations of these measures to the most comparable GAAP measures are also available in our press release and SEC filings.

At this time, I will turn the call over to Mr. Kevin Leidwinger, CEO of UFG Insurance.

Kevin Leidwinger
Thank you, Tim. Good morning, everyone and welcome to our third quarter conference call. I'll begin this morning by providing a high level overview of our results. Following my comments, Julie Stephenson will discuss our underwriting results and Eric Martin will discuss our financial results in more detail. But first, we would like to take a moment to extend our deepest sympathies to those impacted by Hurricanes Helene and Milton in recent weeks. It's been a devastating hurricane season and we wish a swift recovery to the people and communities who were in the path of these storms.

Turning to our results, the third quarter reflects our ongoing efforts to improve performance through the execution of our strategic business plan. We generated the highest quarterly net income and operating income in the past 10 quarters, demonstrating our progress in improving underwriting and investment returns by engaging with distribution partners to profitably grow our business, deepening expertise across the company, enhancing our capabilities and leveraging technology to improve efficiency, all while upholding the personal relationships and responsive service our partners and policyholders value.

Net written premiums grew 23% at $305.6 million with growth led by our core commercial and alternative distribution businesses. Core commercial growth remains steady, with average renewal premium increases exceeding 12%, stable retention and strong new business production. Rate increases accelerated to 11.2% exceeding loss trends, with all liability lines near or above double-digit rate increases.

The third quarter GAAP combined ratio improved 3.8 points to 98.2% from ongoing actions to improve core margins, stable prior period reserve development and catastrophe losses below prior year and historical averages. The third quarter underlying loss ratio of 57.9% improved 2.6 points from prior year, reflecting strong earned rate achievement exceeding loss trends, continued underwriting discipline and lower than expected property large loss experience. The third quarter catastrophe loss ratio was 4.4% and below prior year, as well as both 5 year and 10 year historical averages. This quarter's results directly reflect our ongoing efforts to optimize our property catastrophe risk profile, including targeted actions in hurricane exposed geographies over the past year that reduced our exposure to events like Hurricane Helene, Debbie and Beryl in the third quarter and Milton in the fourth quarter. At this time, we expect Hurricane Milton to have no material impact on the fourth quarter catastrophe loss ratio.

Prior period reserve development was neutral overall in the third quarter. The pattern of stable to favorable loss emergence allows us to continue reinforcing our position against the future inflationary uncertainty challenging our industry in certain liability lines. The underwriting expense ratio in the third quarter was 35.9%, slightly higher than prior year as a result of stronger business performance during the current quarter and increase technology costs as we invest in continued growth.

Third quarter net investment income of $24.4 million increased 49% or $8 million above prior year. Recent actions to reposition portions of our fixed income portfolio resulted in a strong and sustainable increase in fixed maturity investment income to $18.7 million in the third quarter and $78 million on an annualized basis going forward.

New purchase yields remain strongly above total portfolio yields, creating potential for further improvement. Improved valuations on our limited partnership portfolio contributed $5.4 million in pretax investment income in the third quarter. Eric will provide more color on these investment portfolio management actions and results in his remarks.

We continue to make progress in resolving the rating errors in our core commercial business that were identified in the last quarter. At this time, in the last quarter, we were in the early stages of investigating this matter and recorded a contingent liability based on information available at the time. We have since completed our investigation and based upon an evaluation of our findings, the IO [ph 6:06] insurance division elected to take no action nor require refunds. Through the IO insurance division, we continue to work with regulators in other states to achieve resolution that have not changed the amount of the pretax charge reported last quarter.

In conclusion, I'm pleased with our third quarter results and the cumulative progress we've made over the past nine months. Our strategic actions continue to materialize in our results and we remain committed to driving ongoing improvements through the strategic execution of our business plan.

I'll now hand it over to Julie Stephenson, our Chief Operating Officer, to discuss our underwriting results in more detail.

Julie Stephenson
Thank you. Kevin. Net written premium in our core commercial business, which includes small business, middle market and construction, grew 13% to $186 million in the third quarter compared to prior year. Renewal premium change in our core commercial business accelerated to 12.4% with rates up 11.2% and exceeding loss trends. Commercial property premium change remains strong at nearly 20% with pricing accelerating from the second quarter for commercial auto and general liability. Retention remained consistent and within expectations at 81%.

Loss severity trends remain elevated but are consistent with our expectations and showing signs of stabilization. We continue to see ongoing frequency improvement across the portfolio. Core commercial new business production was strong and well above prior for the quarter, with small business, middle marketing and construction adding quality accounts delivered through improved alignment with our distribution partners. Alternative distribution, surety and specialty all contributed diversifying and measured growth for the quarter,

The third quarter underlying loss ratio of 57.9% improved 2.6 points from third quarter of 2023 continuing the momentum reflected in our first and second quarter results. We saw favorable results across all major lines of business this quarter. Earned rate achievement is impacting the loss ratio to a larger extent than previous quarters and continues to exceed loss trends, while lower than expected large property loss experience seen in the second quarter continued into the third quarter.

Prior period reserve development was neutral overall in the third quarter. Consistent with the first two quarters of 2024, loss emergence was neutral to favorable across the portfolio. These positive indications enable us to continue to reinforce our position against the future inflationary uncertainty challenging our industry in certain liability lines. We are pleased with the progress made in our reserve position and will prudently maintain a solid foundation for future success.

Our third quarter catastrophe loss ratio of 4.4% was 1.5 points below prior year and below our 5-year and 10-year historical averages by 8 points and 5.5 points, respectively. Hurricane Helene had a small impact on our quarterly catastrophe loss ratio, while our non-hurricane catastrophe losses were well below expectations. We continue to execute multi-faceted strategies to improve our property catastrophe risk profile, leveraging advanced analytical tools to manage and monitor our exposure to severe convective storm and hurricane risks. Specifically, we're more closely managing our geographic concentration and improving risk quality by focusing our risk improvement and deductible actions on roof quality, building age and construction type.

I will now turn the call over to Eric Martin to discuss the rest of our financial results.

Eric Martin
Thank you, Julie. Starting with the investment portfolio, total invested assets in cash ended the third quarter at $2.2 billion, a high quality portfolio with an overall credit rating of AA- and a duration of approximately 4 years. Total net investment income was $24.4 million in the third quarter, up $8 million or 49% compared to the third quarter of 2023 due to strong improvement in both fixed income and alternative asset portfolio returns. These third quarter results show how the actions taken since transitioning management of our fixed income portfolio to our partners at New England Asset Management are delivering increasing benefits. Continued repositioning out of tax exempt municipals into high quality assets offering more attractive tax equivalent yields in order to take advantage of the current elevated interest rate environment are significantly and sustainably increasing investment income.

As you may recall, in the second quarter, we invested over 20% of the fixed income portfolio at an average yield of 5.6%. In the third quarter, these actions continued, but to a lesser degree, as we invested over 10% of the portfolio at an average yield of approximately 5.2%, which continues to outpace portfolio yield by more than 100 basis points. The benefits of reinvesting over one-third of our fixed maturity portfolio in the last 2 quarters contributed to third quarter fixed maturity income increasing 29% or $4.3 million over prior year to $19 million. This high volume of asset purchases at attractive yields will enhance shareholder returns for years to come.

Our third quarter fixed maturity portfolio is expected to generate $78 million of fixed maturity income on a prospective annualized basis, with additional increases possible from future reinvestment at higher rates. In addition to the improvements in our fixed income portfolio, we also saw increased valuation on limited partnerships and alternative assets. This part of the portfolio contributed $4.3 million of the increase in investment income from prior year.

Turning to the expense ratio, we continue to make good progress in reducing our overall cost structure while also investing in the business. We've seen some geography shifts impacting our underwriting expense ratio. Since the beginning of 2023, we have made meaningful changes to the size and composition of the UFG team, with total headcount down approximately 20% in that time. A larger reduction in the size of the claims team, combined with significant investments and capabilities supporting long term profitable growth has resulted in a shift in the geography of our overall expense. This shift has contributed to an increase in underwriting expenses but a larger decrease in claims, which benefits our loss ratio. However, our expense ratio remains too high and we'll continue to focus on bringing this down over time. This quarter was impacted by improved business performance that drove slightly higher expenses, as well as an increase in technology spending compared to the same quarter last year.

Third quarter net income was $0.76 per diluted share with the non-GAAP adjusted operating gain of $0.81 per diluted share. These results, along with a significant decrease in the unrealized loss position, resulted in book value per common share increasing to $31.01. Adjusted book value per share, which excludes the impact of unrealized investment losses, increased to $32.42. From a capital management perspective, during the third quarter, we declared and paid a $0.16 per share cash dividend to shareholders of record as of August 30, 2024.

This concludes our prepared remarks. I will now have the operator open the line for questions.

QUESTION AND ANSWER

Operator
we will now begin the question and answer session. To ask a question, you may press star then one on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. If at any time your question has been addressed and you would like to withdraw your question, please press star then two. At this time, we will pause momentarily to assemble our roster.

Our first question today comes from Paul Newsome with Piper Sandler.

Paul Newsome
I got a few quick questions here, I think. First, I wanted to ask you about the sustainability of the combined ratio excluding catastrophe losses and reserve developments. It looked like you had some good guys, at least in the catastrophe loss ratio. Were there any sort of good or bad guys that you would like to call out as we think about the current level being the proper run rate?

Julie Stephenson
Of course. I think we see overall improvement across all lines of business. I think as we continue to drive strong rate achievement and that rate achievement earns through, we believe that the loss ratio that we're seeing on these lines will continue to be favorable. We also have continued to see frequency decline and it looks as if severity is showing some signs of stabilization. So, all of those things suggest that the loss ratio improvement we've seen is sustainable over time. Of course, we are continuing to take measures to continually improve the risk profile of the business we're putting on the books.

Paul Newsome
Then maybe turning to top line growth, maybe some additional color on what's happening there. I was hoping you could kind of slice it maybe two different ways. One, looking at sort of rate versus exposure versus unit growth and then maybe some thoughts about sort of specifically where you're growing from a product perspective as well and where you think the opportunities are.

Kevin Leidwinger
We missed the first part of the question. Could you just clarify the intro? We need the context to be able to answer your question.

Paul Newsome
I'd like you to talk about your premium revenue line, the top line and I'd like you to hopefully talk about it in two different ways. One would be rate versus exposure versus unit growth and the other way I was hoping you could talk about it would be from a product perspective and where you think the best advantages are.

Julie Stephenson
Certainly, and I'll take that, Paul. Thank you for the clarification. I think we were really pleased this quarter to see growth across all of our business units. It had been a while since we were able to do that. As you know, we took a chance to rebuild our surety organization, rebuild our specialty organization under a new leader and certainly have taken measures to bring a higher degree of specialization to core commercial. So, I think all those things you're beginning to see the result of in this favorable growth.

As an account solution provider in core commercial, getting the business mix and line of business mix right is a priority. We think that we're heading in the right direction and that we're well poised to grow. Also taking a lot of opportunity to reinforce our relevance with our distribution partners and as they understand more about where we're headed, we feel very confident that we'll continue to see a nice flow of the quality of new business that we want.

From a rate perspective, as I mentioned before, we still are seeing some rate acceleration. We hope that will continue. We saw the leveling off in property but acceleration well above trend in auto, which we think will continue and solid rate achievement in GL. In the current conditions, we hope that that will continue into future quarters.

From a count perspective, policy counts are remaining relatively stable. The profile of our business is changing a little bit as we are looking to write more sophisticated insureds. We may see a slight decrease in the number of clients that we're adding, but nothing material and it would all be based on the fact that we're just writing larger accounts.

CONCLUSION

Operator
This concludes our question and answer session. I would like to turn the conference back over to Kevin

Leidwinger for any closing remarks.

Kevin Leidwinger
Thanks for joining us this morning and we'll see you next quarter.

Operator
The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.