U.S. Insurance

Insurers in the wake of the Silicon Valley and Signature closures

Price Objective Change

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Credit concerns rise following bank failures

In response to closures of Silicon Valley Bank and Signature Bank, financials have sold off with the S&P 500 financials ETF down 9.5% over the past three trading days. Life insurers are down 6-21% with a median decline of 14% and P&C insurers are down 3-10% with a median of 7%. Insurance brokers have been more resilient as investors exit balance sheet intensive financials for the perceived security of balance sheet light businesses. During financial instability, investors are increasingly concerned about credit risk associated with securities held by financial institutions. Recessions are a natural part of the economic cycle, and while pushing out the imminence of the recession seems a recurring theme, fears of recession and credit losses become heightened after the failure of major banks. Investors are particularly concerned with credit losses stemming from commercial properties in the form of structured mortgage-backed securities, mortgage loans and real estate on balance sheets. While we believe these concerns are overly broad, that does not mean that they cannot weigh on valuations and investor appetite near-term.

Risk of associated insurance claims likely manageable

It should likely be expected that these bank failures will trigger claims for in directors & officers (D&O) liability and there may be some tangential errors & omissions (E&O) claims, but we believe that such losses likely total in the hundreds of millions of dollars, such that when spread across many insurers' balance sheets via syndication, any one company's expose is merely modest. Losses could actually serve to arrest current pricing declines in professional liability classes.

Yield curve sees a downward phase shift

Just three trading days earlier 2-Year U.S. Treasuries closed at 5.05% compared with 4.02% after Monday's trading. Below where the yield curve perched at year-end 2022, we are reining in our expectations for rising investment yields, now considering 4.00-4.25% as the ceiling where P&C investment portfolio yields will go regardless of duration. An inverted short end of the curve and a flattish trajectory for longer bonds, we expect that investment returns will rise into year-end 2023 and stabilize thereafter. This leads us to trim our EPS forecasts for a number of P&C insurers.

Broadly lowering our price objectives

On the following page we detail changes in our price objectives (and EPS forecasts, where relevant). As most of our coverage universe is valued on a relative price-to-earnings multiple, the revaluation of the group downward causes us to reduce the average multiples of the peer group, triggering declines among most of the names. All companies mentioned below are seeing a downward revision in their price objective with the exception of AXIS, which rises, as its PO is based upon year-ahead book value, which we now forecast to materially rise as mark-to-market losses on its investment portfolio get increasingly amortized to par as they move to maturity,

Refer to important disclosures on page 14 to 17. Analyst Certification on page 13. Price Objective Basis/Risk on page 9.
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Exhibit 1: Summary of changes to BofA EPS forecasts and price objectives

Recent multiple contraction for the group broadly causes us to lower our price objectives broadly. Lower investment yields and market performance causes a modest reduction in EPS forecasts.

	Rating	New				Old			
		2023	2024	2025	PO	2023	2024	2025	PO
Allstate	Buy	$7.50	$12.95	$16.45	$131	$7.70	$13.20	$17.05	$142
Arch Capital	Buy	$6.60	$7.75	$8.60	$78	no change	no change	no change	$84
AXIS	Underperform	$7.45	$8.45	$8.65	$56	$7.55	$8.20	$8.85	$49
Chubb	Underperform	$16.25	$17.35	$18.25	$185	$16.25	$17.45	$18.40	$205
CNA Fin'l	Underperform	$4.35	$4.50	$4.79	$39	$4.40	$4.60	$4.90	$42
Everest Re	Buy	$46.45	$53.80	$59.95	$435	$48.05	$54.75	$61.00	$481
Hartford	Buy	$8.45	$9.50	$10.65	$86	$8.60	$9.60	$10.85	$94
Lincoln Fin'l	Neutral	$8.80	$9.95	$10.95	$28	$8.70	$9.85	$10.85	$34
MetLife	Buy	$8.50	$9.25	$9.95	$71	$8.40	$9.15	$9.85	$88
Principal	Buy	$7.20	$8.05	$8.45	$81	$7.10	$7.75	$8.15	$100
Progressive	Buy	$7.25	$9.90	$11.65	$175	no change	no change	no change	$179
Prudential	Neutral	$12.50	$12.75	$13.55	$88	no change	no change	no change	$106
RenaissanceRe	Buy	$31.40	$34.85	$39.05	$283	$30.85	$35.20	$40.05	$307
Travelers	Underperform	$14.45	$17.55	$19.60	$183	$14.25	$16.55	$17.55	$200
Unum	Neutral	$6.85	$7.20	$7.65	$40	$6.70	$6.60	$7.10	$48
Voya	Buy	$8.25	$9.65	$11.25	$84	$8.30	$9.70	$11.30	$83
W.R. Berkley	Neutral	$4.85	$5.10	$5.40	$77	$5.00	$5.25	$5.65	$85

Source: BofA Global Research estimates

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Following the failure of three banking institutions—Silvergate Capital on March 8, SVB Financial (Silicon Valley Bank) on March 10 and Signature Bank on March 12—investors have been selling balance sheet-heavy financial institutions. In the three days since Silicon Valley Bank experienced a "run on the bank," shares of the popular S&P 500 Financials ETF ("the XLF") are down 9.5% compared with the S&P 500 being down 3.4% over the same three days of trading. One cannot regard this trading action as impacting the banking sector only as insurance companies have also traded down in response to the news flow. Over the past three days, shares of U.S. life insurance stocks have traded down 6-21% with a median of 14%, while P&C (property & casualty) stocks have traded down 3-10% with a median of 7%. Insurance brokers, which are not balance sheet intensive the way banks and insurance underwriters are, have fallen 2-9% with a median of 5%. Arguably investors may be seeking them out as a "port in a storm" of perceived balance sheet intensive risk.

Exhibit 2: March 3 to March 13 Underperformance of U.S.-Traded Life Insurers Ranked

The U.S. life sector has performed poorly against the backdrop of bank closures, credit concerns and commercial property investment inquiries

March 3 to March 8		March 8 to March 13		March 3 to March 13	
LNC	-6.9%	LNC	-21.0%	LNC	-26.4%
BHF	-5.9%	AEL	-19.2%	BHF	-22.8%
EQH	-5.2%	BHF	-18.0%	EQH	-22.0%
PFG	-4.9%	APO	-17.9%	AEL	-21.7%
CNO	-4.6%	EQH	-17.7%	APO	-20.0%
PRU	-4.4%	UNM	-16.7%	UNM	-19.3%
MET	-4.0%	AMP	-14.9%	PFG	-17.6%
AFL	-3.4%	JXN	-14.1%	CNO	-17.2%
AEL	-3.1%	PFG	-13.3%	PRU	-17.1%
UNM	-3.1%	CNO	-13.3%	AMP	-16.8%
APO	-2.6%	PRU	-13.2%	MET	-16.2%
VOYA	-2.4%	MET	-12.7%	JXN	-15.2%
AMP	-2.3%	VOYA	-11.2%	VOYA	-13.3%
GL	-1.8%	GL	-9.8%	GL	-11.4%
JXN	-1.3%	AFL	-6.0%	AFL	-9.2%

Source: Bloomberg

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Exhibit 3: March 3 to March 13 Underperformance of U.S.-Traded P&C Insurers Ranked
While the declines have not been as harsh as among the life insurer, P&C insurers are also down materially during the current market turmoil.

March 3 to March 8		March 8 to March 13		March 3 to March 13	
CNA	-5.2%	RNR	-10.2%	HIG	-13.6%
HIG	-5.0%	RE	-9.4%	CNA	-13.4%
AXS	-4.8%	KMPR	-9.1%	KMPR	-11.8%
ALL	-4.5%	HIG	-9.0%	AFG	-11.3%
AFG	-4.2%	CNA	-8.7%	RNR	-11.0%
WRB	-3.4%	WRB	-7.5%	ALL	-10.9%
CINF	-3.4%	AFG	-7.4%	AXS	-10.9%
TRV	-3.2%	ACGL	-7.3%	WRB	-10.7%
KMPR	-2.9%	CINF	-7.0%	CINF	-10.2%
THG	-2.6%	ALL	-6.7%	RE	-9.6%
SIGI	-2.1%	AXS	-6.4%	ACGL	-8.6%
MKL	-2.1%	MKL	-6.2%	MKL	-8.2%
CB	-1.8%	SIGI	-5.7%	SIGI	-7.8%
ACGL	-1.4%	CB	-5.6%	THG	-7.7%
PGR	-1.3%	THG	-5.2%	CB	-7.3%
RNR	-0.9%	PGR	-2.9%	TRV	-5.7%
RE	-0.2%	TRV	-2.6%	PGR	-4.2%

Source: Bloomberg

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Exhibit 4: March 3 to March 13 Underperformance of U.S.-Traded Insurance Brokers Ranked
Insurance brokers are not balance sheet-intensive businesses, which likely goes to explain some of the recent outperformance relative to Life and P&C underwriters.

March 3 to March 8		March 8 to March 13		March 3 to March 13	
RYAN	-3.6%	RYAN	-9.4%	RYAN	-12.6%
AON	-1.1%	BRO	-4.9%	WTW	-5.5%
MMC	-0.9%	WTW	-4.8%	MMC	-5.1%
WTW	-0.7%	AJG	-4.8%	AJG	-4.8%
AJG	0.0%	MMC	-4.3%	BRO	-4.7%
BRO	0.2%	AON	-2.4%	AON	-3.5%

Source: Bloomberg

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With the failure of a number of banks and fears of recession looming in the distance, sometimes near sometimes far, concerns over credit risk become amplified, even if difficult to pinpoint. It would not be unexpected that this level of financials stock volatility persists. As investors redeploy into relatively less exposed companies, it is possible that the perceived-as-less-risky stocks will become more expensive while the perceived-as-more-risky stocks will become cheaper. It is not clear that the underlying value of the enterprise is changing, but volatility will cause investors to reorient their portfolios defensively until deciding that more aggressive tactics are warranted.

The difference between an insurance carrier and a bank

Caution is always a wise investment strategy, though we believe it is important to remember how a bank and an insurance company differ on the most basic of levels. Commonly, a depositor places money (called a "deposit") within a bank, and a bank can loan that money out or invest it. Essentially, the depositor has a right to request that deposit returned at will, and it is important for a bank to maintain a high level of liquidity to meet those demands.

For an insurance carrier, the role of the depositor is replaced with a policyholder who pays the insurer a premium. These premiums, in part, form a reserve that supports the future claims of the policyholder collectively, but not individually. The policyholder may or may not see cash returned. The cash is only returned in the event of a "claim," a triggering event where the protection for which the premium was paid has occurred. A claim may be the death of a policyholder, a repair to an automobile, a court judgement against the policyholder, etc. The policyholder cannot demand the premium returned without a triggering claim. Unlike a "run on the bank" where too many policyholders demand their deposits returned simultaneously, there is no "run on the insurer." It only pays claims as they arise. Even failed insurers exist for many, many years in a state of run-off. Policyholders cannot accelerate the return on policyholder funds faster than claims emerge. This is a "first principals" difference between an insurance carrier and a bank.

There is no "run on an insurance company" the way we commonly understand a "run on a bank." Policyholders cannot demand their funds returned to them.

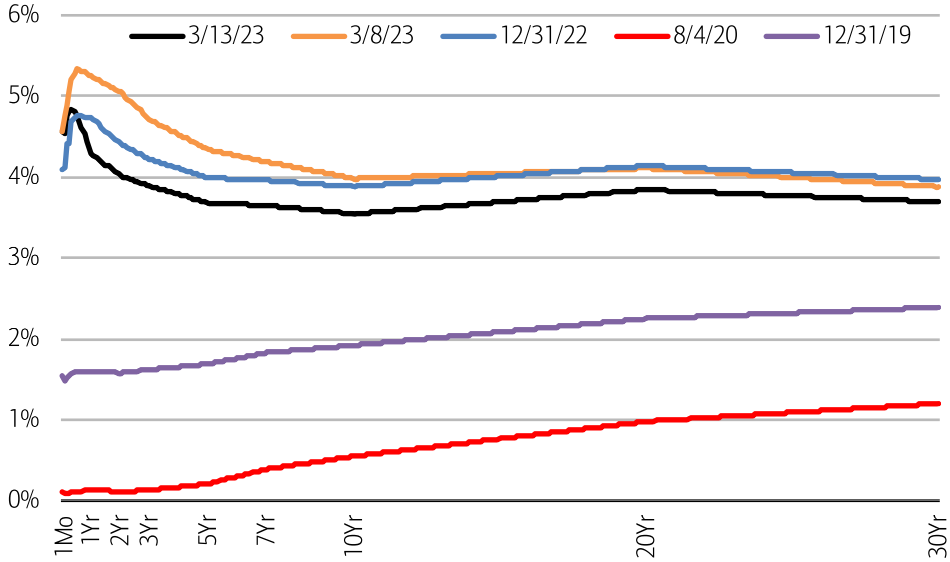
This is not to say that insurers cannot make poor investment decisions or undercharge policyholders for coverage, eventually leading to insolvency. These things have indeed happened in the past. The difference is that it all happens incredibly slowly. Oftentimes, an insurance carrier that has made material investment or pricing decisions will have an opportunity to correct course as the cash outflows from yesteryear's business: increase pricing materially and grow while yesteryear's claims are slowly paid. In the case of an illiquid investment, the insurer may have an opportunity to wait many years into the future where the once illiquid investment becomes liquid.

Mark-to-market losses in an insurance company

On August 4, 2020, during the peak of the COVID19 pandemic, short-term U.S. Treasury yields for 1-3 Months were a mere 9bps. 2-Year Treasuries weren't much higher: 11bps. The 5-Year? 13bps. Only the 30-Year was above 1% (at 1.20%). That was the bottom. Fast-forward to the end of last year. The yield curve was flattish across most maturities at around 4%, albeit inverted with the shorter maturities of the yield curve around 4.40-4.80%. The significant rise in the yield curve took companies from ending 2Q20 with a material mark-to-market gain on the portfolio and transforming it into a material mark-to-market loss over the next 10 quarters. As examples that might serve as metonymies for the industry subgroups more broadly, P&C underwriter Travelers went from having a mark-to-market after-tax gain of $3.6 billion on its $86 billion investment portfolio at June 30, 2020 to having a mark-to-market after-tax loss of $4.9 billion on the portfolio at year-end 2022. By comparison, a life company like Prudential went from a $31 billion unrealized gain (on $569 billion of investments) at June 30, 2020 to an unrealized loss of $20 billion at December 31, 2022.

Exhibit 5: Shape of the U.S. Treasury yield curve at various maturities

While the yield curve has been shifting upward for the past 18 months, over the past three trading days, it materially retraced some previous steps with most maturities now below where they were at year-end 2022.



Source: Bloomberg

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Insurance companies typically hold the investments on their balance sheets as available for sale, and these unrealized gains and losses are well documented quarterly. However, insurance companies do not anticipate that they will realize these investment losses (or investment gains where applicable). They will slowly pay out claims as the bonds that make up the investment losses pull to maturity where the unrealized losses (and former unrealized gains) will be zero. There are some cases where a bond is sold in an unrealized loss position, but this is usually sold in conjunction with another security in a gain position, thereby neutralizing the tax consequence, and then those proceeds are redeployed at a higher yield. While true, it is the exception. Most everything is held to maturity,

While insurance balance sheets often bear investment gains and losses, in most cases, the marks will amortize to zero upon a bond's maturity. The slow and steady payment of claims renders the need to prematurely liquidate the security unlikely.

There is nothing hidden in the disclosure. The insurers aim to match the duration of the assets and the liabilities such that the investments liquify into cash at approximately the same time as the liabilities come due. That said, sometimes P&C insurers have run their investment portfolios shorter than their reserves for losses, but the life insurers aim to match very carefully. As such, the companies generate the cash they need in a timely manner to fund the claims.

The impact of lower yields

For the past 18 months U.S. Treasury yields, particularly on the shorter end of the curve, have generally only risen. The past three days saw a retrenchment that ran contrary to the prevailing trend. Not since being mired in the pandemic have yields dropped so viciously. Referring back to Exhibit 5, one can see that the shorter end of the U.S. Treasury yield curve fell materially in the past three trading days. Two-year U.S. Treasury yields fell by 103bps (to 4.02%). Five-year yields fell by 66bps (to 3.68%). P&C insurers tend to run investment portfolios with durations ranging from 2-5 years. A week ago, we would have assumed portfolio yields were headed north of 5% over the next couple years. Following the rate moves of the past three days, over 4% seems like a better forecast. The flatness of the yield curve argues that the yield on the portfolio will be little different across one- to five-year maturities.

> The notable retrenchment in U.S. Treasury yields over the past three trading days leads us to expect lower terminal investment yields for most of the P&C underwriters in our coverage universe.

Below we list some relevant statistics that guide how we think about investment yields for our P&C insurance coverage companies. Companies that are already earning above 4% on their investment portfolios are likely already approaching the terminal yield on their investment portfolios. That said, some companies hold a material amount of cash and short-term investments that can be deployed into higher yields typically, although not currently with the yield curve inverted as it is. We are generally lowering the investment yield forecast for most companies we cover. The exceptions would be Arch Capital and Progressive, both of which have low investment yields relative to peers as well as low investment portfolio durations relative to peers.

Exhibit 6: Comparing construction and yield characteristics among P&C insurers

We believe, given where interest rates are today, some insurers are already nearing the yield they will enjoy in the future years.

	Portfolio		% portfolio allocation			4Q22 investment yield		
	Duration (years)	Credit quality	cash/ short-term	CMBS/ mortgage loans	real estate	overall	fixed maturities, cash and short-term	fixed maturities
Allstate	3.4		7.8%	1.2%	1.7%	3.58%	3.68%	3.55%
Arch Capital	2.89	AA-/Aa3	8.0%	3.8%		2.63%	2.94%	3.34%
AXIS	2.8	AA-	8.0%	13.2%	1.9%	3.78%	3.47%	3.65%
Chubb	4.5	A/A	6.0%	2.0%		3.90%	4.12%	4.33%
CNA Fin'l	6.6	A	5.3%	3.7%		4.66%	4.78%	
Everest Re	3.1	A+	8.1%	3.1%		2.88%	3.80%	4.26%
Hartford	4.0		7.7%	17.6%		4.91%	4.12%	
Progressive	2.9	AA	5.8%	8.7%		2.95%	2.90%	2.99%
RenaissanceRe	3.2		14.5%	0.9%		3.71%	3.78%	4.04%
Travelers	4.6	Aa2/AA	5.3%	1.4%	1.2%	3.12%	3.24%	3.22%
W.R. Berkley	2.4			2.6%	5.5%	3.84%	3.77%	

Source: Company reports

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For the life insurers, the 10-Year Treasury is a better benchmark, and it has fallen only 44bps (to 3.55%) over the past three trading days. Also, earned yield matters less for life insurers, given that there is also a crediting yield, making the gap between the two more important for future earnings than the earned yield alone. However, it is worth noting that life insurers tend to be material investors in the commercial mortgage-backed securities, whole mortgage loans and real estate markets. In the days leading up to the Silicon Valley and Signature closures, life insurers had already been selling off.

> Life insurance earnings are less dictated by changes in yield at the shorted end of the yield curve.

At a widely attended industry investor conference on March 6-7, investors became increasingly focused on the commercial property market. There are concerns regarding the credit quality of some of these securities as well as increasing concerns that owners might not refinance their mortgages as they become due in a higher rate environment. In this case, insurers might have to move mortgaged properties from a loan to an owned real estate holding. The life companies already are significant real estate investors, so this would not be foreign to them, but there are questions about the value of these properties and the capital charges associated with illiquid real estate. We believe the concerns are overbroad, and, as mentioned at the outset, the pace of insurance companies claim payments are very slow and regular. The illiquidity of real estate today does not likely present the company with impediments to generating cash flow to pay claims. However, that doesn't mean it won't weigh on valuations.

Exhibit 7: Allocation of life insurer investments to commercial real estate interests

Even before the sell-off related to the bank closures, investors seemed to be becoming increasingly cautious regarding commercial real estate exposures among life insurers.

	Investments ($mn)				As a % of investments			
	CMBS	Mortgage Loans	Real Estate	Total	CMBS	Mortgage Loans	Real Estate	Total
Lincoln Fin'l	1,674	18,301	0	131,796	1.3%	13.9%	0.0%	15.2%
MetLife	10,063	83,763	13,137	433,293	2.3%	19.3%	3.0%	24.7%
Principal Fin'l	3,862	20,630	2,240	95,089	4.1%	21.7%	2.4%	28.1%
Prudential Fin'l	10,655	56,176	1,617	417,489	2.6%	13.5%	0.4%	16.4%
Unum	573	2,435	434	43,712	1.3%	5.6%	1.0%	7.9%
Voya	3,883	5,427	346	43,091	9.0%	12.6%	0.8%	22.4%

Source: S&P Capital IQ; company filings, BofA Global Research estimates

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Above, one can see the relative size of commercial real estate exposure (CMBS, whole loans and real estate) as a proportion of the various investment portfolios. We would note that real estate is often marked at cost as there is no reliable way to get a market quote for illiquid property. When speaking to company managements, they tend to speak much of the Class A nature of their holdings and their confidence that the cost at which they sit on the balance sheet is almost certainly lower than the value of the asset. There is no way to corroborate this argument, but it is nonetheless worth mentioning.

Looking back at Exhibit 2, we believe these concerns over commercial property investment exposure preceded the market jitters associated with the bank closures, and these two issues have cross-pollinated to create the material underperformance of the past six trading days. Is there a correlation between the underperformance and the exposure to the commercial real estate market? It is difficult to determine, but we expect little can assuage the concerns of investors focused on this risk until after the economy comes through a recession that may or may not be imminent.

Litigation related to bank failures

P&C insurers sell professional liability coverages. So-called D&O insurance (director's and officer's liability) protects the executives and board members of corporations from litigation related to alleged mismanagement of a company. Suits can be brought by just about anyone—customers, investors, employees, etc. When a stock goes to zero, shareholder suits are often brought against the board and the company management. So-called E&O insurance (errors and omissions liability) protects professionals from litigation related to a counterparty alleging that a job was performed negligently or with mistakes. For example when an accountant fails to file one's taxes on time or a lawyer failed to give its client the best defense or a banker invests a client in a clearly unsuitable investment.

Given that the equity holders of SVB Financial and Signature Bank have been wiped out. one would expect that it is likely there will be associated litigation in the future, and as such it seems reasonable to assume the plaintiffs, at minimum, will try to claim the proceeds of the protection provided by any D&O insurance that these companies may have purchased on behalf of their board and management. Insurers understand how sizable a bank failure can be and are generally uncomfortable extending significant protection to banks for this reason. The media is currently reporting that Silicon Valley Bank's D&O tower totals $180 million. We don't have any reason to dispute or confirm that figure, but it is worthwhile to understand that D&O insurance towers are highly syndicated. Most participant typically want no more than $10 million dollars of exposure from any one D&O risk. As such, whether it is $180 million or $100 million or $250 million that risk is materially spread across many counterparties. Therefore, we believe it is reasonable to assume most companies participating in the public D&O market are likely to have a small piece of Silicon Valley's program, and it would probably be prudent to think of it as a complete, but small loss for analytical purposes. One should probably regard the Signature Bank D&O exposure the same way.

> It is not unreasonable to think of Silicon Bank's D&O litigation exposure as a $150-200 million risk for the P&C insurance industry, but that risk would generally be spread widely with few participants having more than a $10 million share of the loss.

The E&O risk is a bit trickier to analyze. One must consider what might have been a negligent act with mistakes that could result in litigation. Prior to the joint announcement from the U.S. Treasury, the Federal Reserve and the FDIC that depositors would be made whole, this seemed like it could be a big risk as professionals associated with the bank's decisions come under scrutiny. Hundreds of these kinds of cases could prove a material exposure for insurers. However, now as depositors have access to their money, it would be more difficult to identify an identifiable harm. This likely reduces the risk of a multitude of E&O claims, but it would be foolish to ignore the potential for E&O claims entirely.

It may even be the case that the potential for D&O and E&O claims might curtail or reverse a recent trend for the commercial P&C group. Professional liability insurance pricing was up materially in 2020 and 2021, but has materially retrenched downward in the past six months. It is a possible scenario that the potential for losses creates the type of catalyst that forestalls the continued slippage in pricing and maybe the beginning of reversing those declines.

Exhibit 8: Stocks mentioned

Prices and ratings for stocks mentioned in this report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
ALL	ALL US	Allstate Corp.	US$ 114.18	B-1-7
ACGL	ACGL US	Arch Capital	US$ 65.18	B-1-9
AXS	AXS US	Axis Capital	US$ 54	B-3-7
CB	CB US	Chubb Ltd	US$ 191.98	B-3-7
CNA	CNA US	CNA Financial	US$ 38.06	B-3-8
RE	RE US	Everest Re	US$ 346.14	B-1-7
LNC	LNC US	Lincoln National	US$ 23.11	C-2-7
MET	MET US	MetLife	US$ 58.96	B-1-7
PFG	PFG US	Principal	US$ 72.13	B-1-7
PGR	PGR US	Progressive Corp	US$ 139.53	B-1-8
PRU	PRU US	Prudential Financial	US$ 82.18	B-2-7
RNR	RNR US	RenaissanceRe	US$ 189.45	B-1-7
HIG	HIG US	The Hartford	US$ 67	B-1-7
TRV	TRV US	Travelers Cos	US$ 172.22	B-3-7
UNM	UNM US	Unum	US$ 36.64	B-2-7
VOYA	VOYA US	Voya	US$ 65.83	B-1-7
WRB	WRB US	W.R. Berkley	US$ 60.23	B-2-7

Source: BofA Global Research

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Price objective basis & risk

Allstate Corp. (ALL)

Our $131 PO is based on parity with the peer group 2024E P/E multiple of 10.1x. The life insurance divestiture should drive a higher relative valuation compared to the past, and, given our view that personal lines is a better business, there could be upside potential should the market shift to valuing personal lines at a premium. We would believe this valuation seems more than supported by our forecast for a high-teens ROE (on tangible).

Downside risk is presented by the pressure from lower interest rates causing a decline in earnings power and potentially leading the company to miss our EPS expectations. The race to reprice business following the new wave of auto accident frequency and severity could take longer that we forecast. The volatility associated with catastrophes also creates the risk of missing or exceeding our EPS outlook. Another risk: revenue and earnings uncertainty looms in the distance with the eventual adoption of autonomous vehicles.

Arch Capital (ACGL)

Our price objective is $78 in line with the large-cap P&C peer year-ahead P/E multiple (10.1x) on our 2024 EPS forecast. This is a modest premium to the historical trading range (90% of the peer group P/E) given Arch's above-average growth and margin outlook.

Downside risks are depression-like scenarios leading to a collapse in homeownership rates, however, Arch does have $3 billion of collateralized reinsurance protection, partly mitigating this material risk. While Arch had been generally under-exposed to natural catastrophe losses in recent years, the company has been recently increasing its exposure to such events as the price of underwriting that risk has been increasing.

Axis Capital (AXS)

Our price objective of $56 represents parity with our forecast for year-ahead BVPS, which is likely consistent with our forecast for an ROE of 10-11%. However, we do believe underwriting income is peaking. Historically, book value has served as a valuation floor for companies within the peer group given potential for utilization of strategic alternatives.

Upside risks are an acquisition of AXIS at a premium valuation, lower-than-expected catastrophe losses, and favorable prior-year reserve development.
Downside risks are higher-than-expected catastrophe losses, reserve charges, and further elevation in casualty loss cost trends.

Chubb Ltd (CB)

We arrive at a price objective of $185 based on 10.1x 2024E P/E, which is in-line with large-cap commercial lines peers, reflecting the historical trading range.

Upside risk is posed by a material improvement in underwriting margins. The company has been experiencing meaningful price increases in 2020, but these have not translated into meaningfully improving margins so far. Downside risk is presented by the pressure from lower interest rates causing a decline in earnings power and potentially leading the company to miss our EPS expectations. The volatility associated with catastrophes also creates risk of missing or exceeding our EPS outlook. Likewise, reserve adequacy is a bi-directional risk to our price objective.

CNA Financial (CNA)

Our price objective of $39 is based on 85% of the average consensus large-cap P&C peer P/E multiple (10.1x), compared with a 75-100% range where it has traded in the past. We think the discount is appropriate given the overhang associated with its closed-block long-term care book and its general inability/aversion to repurchasing its own shares, even when trading at a discount to perceived fair value. Trading history around a range validates this relative multiple.

Downside risk presented by the pressure from lower interest rates causing a decline in earnings power and potentially leading the company to miss our EPS expectations. The volatility associated with catastrophes also created the risk of missing and exceeding our EPS outlook. Upside risk comes in the form of a steep rise in interest rates, which would ameliorate the reserve pressures on the LTCi book. This particularly could be a tailwind if COVID19 mortality serves to materially reduce the future utilization of nursing care for owners of LTCi policies. Additional upside risk could come from majority owner Loews buying in the limited float trading today.

Everest Re (RE)

Our price objective of $435 is based on 80% of the year-ahead multiple for large cap property and casualty (P&C) peers (10.1x). The 15% discount is based on a reversion to the relative multiple where RE has traded in the past, which we also find likely/appropriate given the greater earnings volatility associated with the reinsurance subsector.

Downside risks are pressure from lower interest rates causing a decline in earnings power and potentially leading the company to miss our EPS expectations, volatility associated with catastrophes also creates the risk of missing or exceeding our EPS outlook, and lawmakers enacting what the industry sees as a retrospective change in coverage to insurance contracts, enfranchising virus-triggered business interruption.

Lincoln National (LNC)
Our PO of $28 is based on 40% of the U.S .large-cap life peer year-ahead (2024) P/E multiple of 7x and our 2024 EPS estimate. The discount is in line with the stock's more recent historical relative valuation likely due to the higher capital intensivity of Lincoln's businesses. The recent 3Q22 assumption review charge leaves it less able to execute on capital return initiatives relative to peers, and for this we believe the discount justified.

Downside risks to achieving our PO are a severe equity market decline, persistently low interest rates, lower than expected flows and sales, and lower than anticipated capital deployment. There is also upside risk, as noted in our PO, which its not insignificantly above the current price. However, we believe current risks justify a higher requirement to recommend ownership. However, a strong rally in equity markets will likely accrue to higher fee income and diminished concerns around capital, which could push the stock higher. A resumption in share repurchases and dividend increases would also be reflected positively in the stock.

MetLife (MET)
Considering our 2024E EPS forecast, we arrive at a price objective of $71, based on 110% of the U.S. large-cap life peer year-ahead P/E multiple of 7x. The premium reflects a transformation at MetLife away from capital intensive businesses and increasing focus on core capabilities by selling the P&C business.

Downside risks to achieving our PO are weaker equity markets and persistent low interest rates, additional charges or reserve issues, failure to achieve net expense initiatives, and lower-than-expected capital deployment.

Principal Financial Group (PFG)
Our price objective of $81 is based on 130% of the U.S. large-cap life peer year-ahead (2024) P/E multiple of 7x applied to our 2024E EPS forecast. The premium multiple reflects PFG's higher free cash flow generating business mix and lower exposure to long-dated guaranteed policies.

Downside risks to our PO are an equity market decline, a decline in core business margins, a deterioration in fund flows, and inefficient deployment of capital (i.e., unprofitable M&A). Upside risks to our PO are stronger than expected equity market returns, better than projected core business margins, stronger fund flows, and higher-than-anticipated capital deployment.

Progressive (PGR)
Our $175 price objective is based on a 10% premium to the current S&P 500 P/E multiple for 2024, currently 16.1x, on our 2024E EPS forecast. Due to quickly accelerating EPS ahead of the market rate of growth, as in 2016-2019, Progressive shares should trade at a premium to market as its earnings accelerate.

Downside risks to our PO are 1) presented by the pressure from lower interest rates, causing a decline in earnings power and potentially leading the company to miss our EPS expectations, 2) the volatility associated with catastrophes, which also creates the risk of missing and exceeding our EPS outlook, 3) the impact of material pricing changes by major competitors, 4) the long-term impact of emergent technologies, such as ride-sharing applications and autonomously driven automobiles.

Prudential Financial (PRU)

Our $88 price objective for PRU is based on a 5% discount to the current year-ahead life insurance P/E multiple (7x) on our 2024E EPS forecast. Prudential has de-risked its businesses, however it is still sensitive to changes in interest rates and equity markets.

Downside risks to the achievement of our PO are a weakness in credit and equity markets, lower than expected interest rates, and lower growth and returns in U.S. and international businesses, and lower than anticipated capital deployment. Upside risks to our PO are better than expected equity market returns and higher interest rates, higher than estimated growth and returns in U.S. and international businesses, and higher than anticipated capital deployment.

RenaissanceRe (RNR)

Our $283 PO is based on 80% of the large cap P&C year-ahead P/E multiple (10.1x) on our 2024E EPS forecast. We believe that RenaissanceRe, because it is uniquely constrained to reinsurance markets, may be disadvantaged from a valuation standpoint. Once it traded at a premium, but currently reinsurance is viewed as a derivative market with less upside in an improving market for P&C underwriting margins.

Downside risk is presented by the pressure from lower interest rates causing a decline in earnings power and potentially leading the company to miss our EPS expectations. The volatility associated with catastrophes also creates the risk of missing or exceeding our EPS outlook.

The Hartford (HIG)

Considering our 2023E EPS estimate, we arrive at a price objective of $86, based on HIG's P/E at 90% of the large-cap P&C peers (10.1x). We continue to value Hartford's earnings at a 10% discount to the peer group, noting its sub-scale personal lines business..

Risk to our PO comes from the risk of loss cost inflation in years to come. Further, given many claims against it for COVID19, Hartford seeks greater clarity as to whether or not the industry receives court assurance that it is not responsible for many categories of virus claims. Additionally, catastrophe losses remain a key factor in earnings volatility and, in a low catastrophe year, could cause the EPS results to exceed our forecasts. Prior year reserve adequacy risk is also bidirectional. Currently, spiking auto accident frequency and broad personal lines severity could put pressure on this segment.

Travelers Cos (TRV)

Our $183 price objective is based on 105% of the large-cap P&C peer group's next-year P/E multiple (currently 2024E), which currently stands at 10.1x. The modest premium in the multiple is due to our view of Travelers as the benchmark in terms of quality and scope of disclosure among commercial P&C insurers. The company's transparency aids in establishing investor confidence in its reserving methodology and underwriting discipline.

Upside risks to our price objective are the potential that commercial loss reserves established during the COVID19 period do not evolve into paid claims and instead create earnings in the form of net prior-year favorable reserve development. Additionally, high loss cost trend has muted the impact of rate improvements. Should loss costs decelerate, the company's underlying margins would expand more quickly. Downside risks are workers' comp claims could accelerate as back-to-work trends post-pandemic trend toward full employment. Catastrophe losses remain a key factor in earnings volatility and could prevent the company from achieving our price objective. The risk of inflation remains a longer-term concern that would likely weigh materially on results or improve results in an extended disinflationary period.

Unum (UNM)

Our $40 price objective for UNM is based on 80% of the U.S. large-cap life peer year-ahead (2024E) P/E multiple of 7x. Our target multiple is modestly below UNM's 8x-9x post financial crisis average and the P/E we target for most life insurance peers given Unum's heightened risk in long-term care, capital constraints and very low cash flow conversion related to its agreements with regulators, and lack of earnings growth trajectory.

Downside risks are charges or unfavorable developments for long-term care insurance, lower than expected sales and margins at the ongoing operations, and lower than anticipated interest rates. Further reserve charges for the company's long-term care risk, whether concluded upon internally or forced upon Unum by regulators, could further erode the capital flexibility and dividend paying capacity of the company. Upside risks are positive developments for long-term care insurance, better than expected sales and margins at the ongoing operations, and higher than anticipated interest rates.

Voya (VOYA)

Our price objective of $84 is based on a mixed-multiple sum-of-the-parts methodology consistent with the differentiated businesses in which Voya operates. We use a 2024E P/E multiple of 9x for the Retirement business, 8x for the Investment Management business, and 10x for Employee Benefits. These are equal to the average P/E multiples of appropriate peer groups equivalent to the values of Voya's businesses. Additionally, Voya's notable excess capital position, proceeds from a recent business sale and its sizable deferred tax asset combine for material upside potential compared with the current stock price.

Risks to our price objective are lower capital returns to shareholders than we expect and potential increased tax rates after the US presidential election and depending on legislative priorities.

W.R. Berkley (WRB)

Considering our 2024 EPS estimate, we arrive at a price objective of $77, valued at 150% of the large-cap P&C peers' P/E multiple of 10.1x. Berkley hasn't necessarily compounded equity in excess of other best-in-class peers in 15 years, though the premium valuation has held for several years, and we do not see it likely for it to re-rate downward. That said, book value growth has been material dependent on realized investment gains during an equity bull market, which could persist as long as the bull market lasts, but also presents a risk, should those conditions change.

Upside risk comes from recent price gains manifesting themselves as widening underwriting margins in excess of our expectations. Downside risk presented by the pressure from lower interest rates causing a decline in earnings power and potentially leading the company to miss our EPS expectations. The volatility associated with catastrophes also created the risk of missing and exceeding our EPS outlook. Additionally, the state of Berkley's loss reserves, be they deficient or redundant, creates a bi-direction risk for the stock.

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US - Insurance Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Allstate Corp.	ALL	ALL US	Joshua Shanker
	American International Group	AIG	AIG US	Joshua Shanker
	Arch Capital	ACGL	ACGL US	Joshua Shanker
	Assurant	AIZ	AIZ US	Grace Carter, CFA
	BRP Group, Inc.	BRP	BRP US	Joshua Shanker
	Corebridge Financial	CRBG	CRBG US	Joshua Shanker
	Everest Re	RE	RE US	Joshua Shanker
	MetLife	MET	MET US	Joshua Shanker
	Principal Financial Group	PFG	PFG US	Joshua Shanker
	Progressive	PGR	PGR US	Joshua Shanker
	RenaissanceRe	RNR	RNR US	Joshua Shanker
	The Hanover	THG	THG US	Grace Carter, CFA
	The Hartford	HIG	HIG US	Joshua Shanker
	Trupanion	TRUP	TRUP US	Joshua Shanker
	Voya	VOYA	VOYA US	Joshua Shanker
NEUTRAL				
	Aon	AON	AON US	Joshua Shanker
	Cincinnati Financial Corporation	CINF	CINF US	Grace Carter, CFA
	Lincoln National	LNC	LNC US	Joshua Shanker
	Prudential Financial	PRU	PRU US	Joshua Shanker
	Selective	SIGI	SIGI US	Grace Carter, CFA
	Unum	UNM	UNM US	Joshua Shanker
	W.R. Berkley	WRB	WRB US	Joshua Shanker
UNDERPERFORM				
	Arthur J. Gallagher & Co.	AJG	AJG US	Joshua Shanker
	Axis Capital	AXS	AXS US	Joshua Shanker
	Chubb Ltd	CB	CB US	Joshua Shanker
	CNA Financial	CNA	CNA US	Joshua Shanker
	Goosehead Insurance Inc.	GSHD	GSHD US	Joshua Shanker
	Lemonade, Inc.	LMND	LMND US	Joshua Shanker
	Marsh McLennan	MMC	MMC US	Joshua Shanker
	Travelers Cos	TRV	TRV US	Joshua Shanker
	Willis Towers Watson	WTW	WTW US	Joshua Shanker

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Equity Investment Rating Distribution: Financial Services Group (as of 31 Dec 2022)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	151	53.36%	Buy	100	66.23%
Hold	71	25.09%	Hold	43	60.56%
Sell	61	21.55%	Sell	42	68.85%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2022)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	1853	52.58%	Buy	1040	56.13%
Hold	840	23.84%	Hold	493	58.69%
Sell	831	23.58%	Sell	404	48.62%

[R1] Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster[R2]
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

[R2]Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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