# Q2 2021 Earnings Call

## Company Participants

- Abbe Goldstein, Senior Vice President, Investor Relations
- Alan D. Schnitzer, Chairman and Chief Executive Officer
- Dan Frey, Executive Vice President and Chief Financial Officer
- Gregory C. Toczydlowski, Executive Vice President and President, Business Insurance
- Michael F. Klein, Executive Vice President and President, Personal Insurance
- Thomas M. Kunkel, Executive Vice President and President, Bond & Specialty Insurance

## Other Participants

- Brian Meredith
- David Motemaden
- Elyse Greenspan
- Jamminder Bhullar
- Joshua Shanker
- Meyer Shields
- Michael W. Phillips
- Ryan Tunis
- Tracy Benguigui

## Presentation

### Operator

Good morning, ladies and gentlemen. Welcome to the Second Quarter Results Teleconference for Travelers. We ask that you hold all questions until the completion of formal remarks, at which time you will be given instructions for the question-and-answer session. As a reminder, this conference is being recorded on July 20, 2021.

At this time. I would like to turn the conference over to Ms.Abbe Goldstein. Senior Vice President of Investor Relations. Ms.Goldstein, you may begin.

### Abbe Goldstein {BIO 20602454 <GO>}

Thank you. Good morning and welcome to Travelers' discussion of our second quarter 2021 results. We released our press release, financial supplement, and webcast presentation earlier this morning. All of these materials can be found on our website at Travelers.com under the Investors section.

Speaking today will be Alan Schnitzer, Chairman and CEO; Dan Frey, Chief Financial Officer; and our three segment presidents: Greg Toczydlowski of Business Insurance; Tom Kunkel of Bond & Specialty Insurance; and Michael Klein of Personal Insurance. They will discuss the financial results of our business and the current market environment. They will refer to the webcast presentation as they go through prepared remarks, and then we will take questions.

Before I turn the call over to Alan, I would like to draw your attention to the explanatory note included at the end of the webcast presentation. Our presentation today includes forward-looking statements. The company cautions investors that any forward-looking statements involves risks and uncertainties and is not a guarantee of future performance. Actual results may differ materially from those expressed or implied in the forward-looking statements due to a variety of factors. These factors are prescribed under forward-looking statements in our earnings press release and in our most recent 10-Q and 10-K filed with the SEC. We do not undertake any obligation to update forward-looking statements.

Also in our remarks or responses to questions, we may mention some non-GAAP financial measures. Reconciliations are included in our recent earnings press release, financial supplement, and other materials available in the Investors section on our website.

And now, I'd like to turn the call over to Alan Schnitzer.

## Alan D. Schnitzer {BIO 3529437 <GO>}



Thank you, Abbe. Good morning, everyone, and thank you for joining us today. We are very pleased to report excellent underwriting investment results for the second quarter and first half of the year.

Core income for the quarter was $879 million or $3.45 per diluted share, generating a core return on equity of 13.7%. In terms of the underwriting results, higher underlying underwriting income, and net favorable prior-year reserve development as well as the lower level of catastrophe losses, all contributed to higher core income. Underlying underwriting income was 8% higher than in the prior quarter, driven by record net earned premiums of $7.6 billion and an excellent underlying combined ratio of 91.4%.

We are particularly pleased with the continued strong underlying fundamentals in each of our three business segments. In Business Insurance, net earned premiums were higher and the underlying combined ratio improved by 3.7 points, and the Specialty Insurance and Personal Insurance, both delivered meaningful increases in net earned premiums and continued strong margins.

Turning to investments, our high-quality investment portfolio generated net investment income of $682 million after-tax, reflecting very strong returns in our non-fixed income portfolio. These excellent results, together with our strong balance sheet, enabled us to grow adjusted book value per share by 13% over the past year, after making important investments for the future and returning significant excess capital to our shareholders.

During the quarter, we returned $625 million of excess capital to shareholders, including $401 million of share repurchases.

Turning to the top-line, the combination of the strong franchise value we offer to our customers and distribution partners, together with excellent execution by our field organization produced terrific results. During the quarter, we grew net written premiums to $8.1 billion, an increase of 11% or 8% after adjusting for the auto premium refunds in the prior year quarter. Each of our three segments contributed meaningfully to the top-line growth.

In Business Insurance, net written premiums grew by 5%, driven by retention, which ticked up almost a point, renewal premium change at a near record high of 9.5%, and 9% growth in new business. Combination of strong pricing and higher retention reflects continuing strength in the pricing environment. Inside renewal premium change, pure renewal rate change was a strong 7.1%. Greg will share more detail about the texture underneath renewal rate change in a few minutes. Renewal premium change also included the highest exposure growth we've seen in nine quarters, an encouraging sign of improvement in US economic activity.

In Bond & Specialty Insurance, net return premiums increased by 16%, driven by record renewal premium change of 12.7% in our management liability business, while retention remained strong. In our commercial businesses, returned pricing continues to comfortably outpace estimated loss trend, which will continue to benefit margins as it turns in. Continued strong pricing in retentions reflect the industry's clear-eyed view of the ongoing headwinds impacting returns for the industry, including weather volatility, low interest rates, and social inflation. We expect pricing to continue to outpace loss transfer some time.

In the Personal Insurance, production was again excellent this quarter. Net written premiums increased 8% after adjusting for the otter premium refunds in the prior year quarter. Policies in force in both auto and homeowners are at record levels, driven by continued strong retention and growth in new business.

While the impact of the pandemic on claim frequency seems to be attracting a lot of attention when it comes to personal auto, we've been equally focused on applying our company-wide performed and transform mandate to this business. We're very pleased with the results. We've accelerated our domestic auto policies in force growth from 1% to 4% over the last six quarters, bringing PIT [ph] count to a record high. This demonstrates the ongoing success of our three prong strategy in Personal Insurance to meet customers where they are, serve them how they want, and get them what they need. Going forward, we will continue to invest in advanced segmentation, multi-channel distribution, and providing great experiences to continue to deliver profitable growth. Mike will share more detail in a few minutes.

Our excellent top and bottom-line results this quarter for the first half of the year demonstrate that continued successful execution of our strategy to grow the top-line at attractive returns as well as the effectiveness of our well-defined and consistent investment philosophy. Our focused and well-executed innovation agenda has been an important contributor to the growth and profitability we have achieved and we will continue to relentlessly pursue our priorities of extending our list in this -- extending our lead in risk expertise, providing great experiences to our customers, distribution partners, and employees, and improving productivity and efficiency. With the momentum we have and the best talent in the industry, we are well-positioned to continue to create meaningful shareholder value overtime.

With that, I'm pleased to turn the call over to Dan.

## Dan Frey {BIO 20727678 <GO>}

Thank you, Alan. Core income for second quarter was $879 million, compared to a core loss of $50 million in the prior-year quarter. The significant improvement was the result of positive factors across the business, including a lower level of catastrophe losses, improved results, and our non-fixed income investment portfolio, more favorable prior-year reserve development, and increased underlying underwriting income.

Our second quarter results include $475 million of pre-tax cat losses, compared to $854 million in last year's second quarter. This quarter's cats were somewhat below of what we would've assumed for a typical second quarter, but year-to-date, cat losses are still above what we would have assumed given the high level of losses in the first quarter.

On a year-to-date basis, we have accumulated about $1.5 billion of qualifying losses toward the aggregate retention of $1.9 billion on our property aggregate catastrophe XOL Treaty. The Treaty provides $350 million of coverage on the first $500 million of losses above the aggregate retention amount.

Underlying underwriting income increased 8% to $617 million pre-tax, reflecting the higher level of earned premium in each of our segments and the strong underlying combined ratio of 91.4%, consistent with the prior year. As you'll hear from Greg, Tom, and Michael, improvements in the underlying combined ratio in both Business Insurance and Bond & Specialty were offset by an increase in the underlying combined ratio and Personal Insurance. Some of the increase in Personal Insurance was expected given that last year's quarter benefited from unusually low auto losses as a result of the pandemic.

The underlying loss ratio came in at 61.7%, up 1.3 points from last year's second quarter as the beneficial impact of earned pricing and excess of loss trend was more than offset by the comparison to a very low pandemic-related personal auto loss ratio in the year-ago quarter. Expense ratio of 29.7% is 1.3 points lower than the prior-year quarter as last year's result was elevated primarily due to the premium refunds we've provided to our personal auto customers.

Turning to prior-year reserve development, In Personal Insurance, both auto and property losses came in better-than-expected for recent accident years, resulting in $65 million pre-tax net favorable PYD. In Bond & Specialty Insurance, $44 million in pre-tax net favorable PYD was driven by favorable loss experienced in surety and fidelity related to recent accident years. In Business Insurance, net favorable prior-year reserve development of $73 million was driven by better-than-expected loss experienced in workers' comp across multiple accident years, partially offset by reserve strengthening in our run-off book.

Net investment income improved to $682 million after-tax this quarter. Our non-fixed income portfolio turned in particularly strong results this quarter, reflecting performance in the equity markets contributing $265 million after-tax. Consistent with our expectations, fixed income returns were down slightly from the prior-year quarter as the benefit from higher levels of invested assets was more than offset by a decline in yields. For the remainder of 2021, we expect fixed income NII, including earnings from short-term securities, of between $425 million and $435 million after-tax per quarter.

Turning to capital management, operating cash flows for the quarter of $1.8 billion were again very strong. All our capital ratios were at or better than target levels and we ended the quarter with holding company liquidity of approximately $2.4 billion. During the second quarter, we took advantage of favorable market conditions and raised the $750 million to help fund future growth with a 30-year debt issuance of 3.05%, representing our second lowest 30-year coupon ever and achieving one of the tightest spreads ever for a 30-year note issued by an insurance company.

The market value of the bonds in our portfolio generally rose as US treasury yields declined and credit spreads tightened during the second quarter, and accordingly, our after-tax net unrealized investment gains increased from $2.8 billion as of March 31st to $3.2 billion at June 30th. Adjusted book value per share, which excludes net unrealized investment gains and losses, was $103.88 at quarter-end, up 4% since year-end and up 13% year-over-year. We returned $625 million of capital to our shareholders during the second quarter with $224 million of dividends and $401 million in share repurchases.

Coming back to reinsurance for a moment, let me direct your attention to Slide 20 of the webcast presentation for a summary of our July 1st renewables. The structure of our main cat reinsurance program is generally consistent with the prior year. We renewed our Northeast Cat Treaty effective July 1st with substantially similar terms and pricing that was up only slightly on an exposure adjusted basis.

Our Cat Bond, BondPoint REIT 3, is now in the final year of its four-year term. In the annual reset for the 2021 hurricane season, the attachment point was adjusted from $1.87 billion to $1.98 billion, while the total cost of the program was flat year-over-year. More complete description of our cat reinsurance coverage, including our general cat aggregate XOL Treaty that covers an accumulation of certain property losses arising from multiple occurrences, is included in our 10-Q, which we filed earlier today and in our 2020 Form 10-K.

Before turning the call over to Greg, I'd like to make a few comments about inflation as the consumer price index has gotten a lot of attention lately. We are relatively less leveraged to overall CPI type inflation as compared to, say, medical inflation and social inflation. One place CPI type inflation can impact us is in our short tail lines. That withstanding our strong profitability in PI, as you'll hear from Michael, we are experiencing a degree of elevated severity. However, relatively short payout periods in short tail lines limit the impact of that exposure, and although it takes time to earn in over the policy period, we can price for those increases reasonably quickly.

Additionally, it's important to remember that we have some natural hedges in our business that mitigate the effects of inflation. First, higher inflation is often associated with stronger economic activity as well as higher wages and asset values, all of which contribute to higher insured exposures, and as we've discussed before, higher exposure contributes to improved margins. Second, although we're not seeing it at the moment, to the extent interest rates are in correlated to inflation, we would benefit from higher returns in our investment portfolio as inflation increases. Finally, let me reiterate that we are conscious of the inflation environment and the uncertainties surrounding it when we establish our loss peaks and our balance sheet reserves.

With that, I'm pleased to turn the call over to Greg for discussion of Business Insurance.

## Gregory C. Toczydlowski {BIO 16615940 <GO>}

Thanks, Dan. Business Insurance had a great quarter with strong financial results and terrific execution in the marketplace. Segment income was $643 million for the quarter, compared to a loss of $58 million in the prior quarter. Higher net investment income, lower catastrophe losses, higher underlying underwriting income, and favorable prior-year reserve development, all contributed to the year-over-year improvement.

We're particularly pleased with the underlying combined ratio of 93.3%, which improved by 3.7 points from the second quarter of 2020, primarily attributable to three things. First, about 2 points of the improvements resulted from earned pricing, exceeding loss cost trends, another 0.5 point or so resulted from lower non-cat weather, and third, the improvement also reflects the comparison to the modest net charge we took in the prior-year quarter related to the pandemic. In terms of non-cat whether or the year-over-year improvement was about 0.5 point favorable, as I just mentioned, this quarter's result was about 1.5 better than what we assumed for the quarter.

Turning to the top-line, net written premiums were up 5%, benefiting from strong renewal premium change, including both strong renewal rate and exposure levels that are trending back to pre-pandemic levels and higher year-over-year new business value. As for domestic production, renewal premium change was 9.5% of historically high result and up almost 4 points from the second quarter of last year.

Underlying the RPC, we achieved strong renewal rate change of 7.1% and healthy exposure growth that reflects an improving trend in our customers' outlook for their businesses. As Alan said, our ability to continue to achieve historically high pricing with improved retention speaks to the stability of pricing in the market. New business was up more than 9% with both select and middle-market contributing. I'll discuss those results in more detail in a moment when I get to the individual businesses. We're very pleased with these aggregate production results in our marketplace execution. We've generated written pricing that has been in excess of estimated loss trend for some time now resulting in significant improvement and the profitability of our BOP.

While this quarter's renewal rate change of 7.1% remains well in excess of loss trend, it was a little lower sequentially. Let me provide a little more context around that. A substantial majority of the decrease is attributable to a rational moderating of rate in our two specialty business units, Excess Casualty, which is inside Middle Market, and National Property. The bottom [ph] show incomes after three years of very strong compounding rate increases in these two businesses, so the tempering of rate is appropriate considering the improved return profile. Also, while renewal rate change was down sequentially for those businesses, rate increases were still in double-digits. More broadly, the rate increases we are seeing across Business Insurance continue to be stable and widespread across both our lines of business and our distribution of accounts.

As demonstrated on Slide 12, in our Middle Market and National Property businesses, we achieved the rate increases in 84% of the accounts that renewed in the second quarter, up from 81% in last year's second quarter. Even with persistent loss pressures and low fixed income yields, we will continue to see rate to further improve our margins. We will also continue to focus on all the non-rate levers to improve the risk profile and profitability across our portfolio. For example, in our National Property business, our underwriters continue to focus on improving terms and conditions transaction-by-transaction. Changes in terms like increase deductibles, management of stock limit, and reinsurance optimization are meaningful tools in enhancing our profitability and our underwriters continue to be active in utilizing all those levers.

As for the individual businesses, in select, renewal rate change was 4.3%, more than 2 points higher than the second quarter of 2021, while retention was 80%. These results reflect deliberate execution as we pursue improved returns in certain segments of the business and we're pleased with the progress we're making in this regard. Exposure growth was all over 4% for the quarter, which is an encouraging sign as the economy reopens. Lastly, new business was up 6% over the prior-year quarter, driven by the continued success of our new BOP 2.0 product, which is now live in 31 states. This state-of-the-art product includes industry-leading segmentation and a fast easy quoting experience. We are encouraged with our agents' adoption of the new products as both submissions and new policies are up.

In Middle Market, renewal premium change of over 9% and retention of 87% were both historically high. Renewal rate change at 7.4% remains strong in well and excess of loss trend. Finally, new business was up 16% over the prior year quarter, driven by success with larger accounts as well as some improvement in the quality of the flow in the market. As always, we remain disciplined around risk selection in underwriting.

To sum up, Business Insurance had a terrific quarter by all measures. We're pleased with our execution in further improving the underlying margins in the book and we continue to invest in the business for long-term profitable growth.

With that, I'll turn the call over to the Tom.

## Thomas M. Kunkel {BIO 16615934 <GO>}

Thanks, Greg. Bond & Specialty posted excellent returns and growth in the quarter. Segment income was $187 million, considerably more than double the prior-year quarter, driven by favorable prior-year reserve development, a significantly improved underlying underwriting margin, and higher business volumes. The underlying combined ratio of 83.4% improved by over 4.5 points from the prior-year quarter, as pricing that exceeded loss cost trends drove a lower underlying loss ratio.

Turning to the top-line, net written premiums grew an exceptional 16% in the quarter with solid contributions from all our businesses. In management liability, renewal premium change was a record 12.7%, driven by near-record rate. Retention remain strong at 86%, new business increased 6% from the second quarter of last year, our first quarterly increase since the beginning of the pandemic with strong new business pricing. Surety also grew for the first time since the beginning of the pandemic and international again posted meaningful growth, including strong retention and rate. So Bond & Specialty results were excellent and reflect our ability to successfully manage this business through a variety of business and economic cycles.

And now, I'll turn it over to Michael for Personal Insurance.

## Michael F. Klein {BIO 19674145 <GO>}

Thanks, Tom, and good morning, everyone. We're very pleased with our second quarter Personal Insurance results. Segment income of $121 million was up $111 million from the prior-year quarter, benefiting from lower catastrophes, higher net investment income, and higher net favorable prior-year reserve development. Partially offsetting these improvements was a lower underlying underwriting gain, which I will discuss in more detail in a moment.

Our second quarter combined ratio improved from the prior year quarter by about 1.5 points to 99.7%. Net written premiums grew 16%. Recall that in the prior-year quarter, we provided $216 million of premium refunds to automobile customers in response to the impact of the pandemic. Adjusting for these premium refunds, net written premiums grew a very strong 8%, with domestic homeowners up 12% and domestic automobile up 4%.

Automobile delivered another excellent quarter with a combined ratio of 91.6%. The underlying combined ratio was an impressive 92%, although up 6 points from our prior-year quarter, which reflected low loss activity during the initial months of the pandemic. The current quarter results, reflect the benefits of modestly lower claim frequency compared to pre-pandemic levels.

As we exited the quarter, claim frequency was closer to pre-pandemic levels and we would expect that trend to continue in the third quarter. Our strong current quarter profitability also reflects increased severity, particularly in collision and third-party physical damage claims, driven primarily by higher costs of used vehicles and parts. As auto loss experience approaches pre-pandemic levels, we plan to begin filing for rate increases in selected states later this year, as we continue to balance business volumes and profitability. While it will take some time for future rate actions to earn into our results, we are well-positioned to continue to be -- profitably grow in auto.

In homeowners and other, the second quarter combined ratio of 108.3% was 6 points lower than the prior-year quarter, driven by 13.5 point reduction in catastrophe losses. Partially offsetting the catastrophe favorability was an 8 point increase in the underlying combined ratio. Approximately one-third of this increase reflects non-catastrophe weather losses, which were in line with our expectations, but elevated over a less active prior-year quarter. The remainder of the increase reflects continued elevated frequency and severity of fire and non-weather weather losses. The increased severity we saw in the second quarter includes higher repair costs due to a combination of labor and material increases. We continue to see great increases in response to these trends and we'll continue to actively monitor inflation in loss cost trend changes and factor them into our pricing and underwriting decisions.

Turning to quarterly production, domestic automobile retention was up slightly to a strong 85%, new business increased by 19%, and policies in force grew 4%. Domestic homeowners and other delivered another excellent quarter with retention remaining strong at 85%, renewal premium change increasing to 8.2%, and new business growth of 28%, reflective of increased core activities and increase in average premium, along with the ongoing successful roll out of Quantum Home 2.0. Policies in force grew 7%.

As Alan mentioned, our policies in force growth, across both auto and homeowners, are at record levels. Actually, our policies in force across both auto and homeowners are at record levels, reflecting our ongoing efforts to perform and transform in personal insurance. When we launched Quantum Auto 2.0, we designed it with a modular product structure to give customers what they need and to deliver long-term performance. This has enabled us to seamlessly introduce new rating variables, such as, vehicle history, prior insurance history, and telematics, allowing us to continually improve our pricing segmentation.

Regarding telematics, we've seen take-out rates for IntelliDrive increased by 30% since the launch of our second generation offering, which features a fully redesigned mobile experience, monitors distracted driving, and improves our ability to match price to driving behavior.

Our momentum in auto aligns very well with our goal of providing total account solutions for customers. The Quantum Home 2.0 product is now available in over 40 states, generating consistent growth in policies in force. Both distributors and customers continue to see value in our combined auto and property offerings. Our multi-channel PI distribution strategy allows us to meet our customers where they are. As a result of the success of our new products, our existing relationships continue to perform well. Additionally, we've seen more demand for agent appointments, which is contributing meaningfully to our growth.

In order to serve customers how they want to be served, we are also investing in our digital capabilities. With advancements in our MyTravelers mobile app, we continue to digitize the customer journey of over 600,000 customers already downloading the app since it was launched earlier this year. Going forward, we will continue to invest in solutions that meet customers where they are, give them what they need, and serve them how they want, while working with our distribution partners to deliver profitable growth.

Now, I'll turn the call back over to Abbe.

## Abbe Goldstein {BIO 20602454 <GO>}

Thanks, Michael. Before we open it up for Q&A, I'd like to turn the call back over to Alan for a moment.

## Alan D. Schnitzer {BIO 3529437 <GO>}

Thanks, Abbe. As bitter-sweet as it is, we have one last piece of business this morning before we turn to Q&A. I want to acknowledge and thank our partner and friend, Tom Kunkel, will be retiring in September, after a spectacular 37-year career at Travelers. Tom's impact as the leader of our very successful Surety and Management Liability businesses has been profound. In addition to delivering exceptional financial results over many years, Tom and his leadership team fostered a culture of care, community, and excellence that extends throughout our Bond & Specialty organization and throughout Travelers. It's one of the many reasons why I'm so pleased that Jeff Klein [ph], currently a member of Tom's leadership team and Head of our Management Liability business, will succeed Tom. Jeff has been with Travelers from more than 20 years. He's a proven leader and the perfect candidate to take the range from Tom. You'll hear from Jeff on October on our third quarter earnings call. Tom, we're all going to miss you, personally and professionally.

And with that, we're happy to take your questions.



# Questions And Answers

## Operator

(Question And Answer)

Thank you. (Operator Instructions). We have our first question from the line of Michael Phillips from Morgan Stanley. Please go ahead.

## Q - Michael W. Phillips {BIO 21023048 <GO>}

Thank you and good morning everybody. I want to drill first, I guess Mike, one, from your comments on Personal Auto, and your comments I think towards the end when you said you'll begin to file some rate increases later in the year. Question kind of centered around the timing of that, frequency benefits for you seem to be lasting a little bit longer than some of your peers, maybe that's a mix of business issue that you might have a little more preferred, maybe you can confirm that. But what's driving -- if frequency started to come back to pre-pandemic levels and expect that to continue, I guess, why not take rate now? Why wait till later in the year and what's driving that need for rate? If it's not frequency and maybe it is, is it more the severity? So kind of a couple-pronged question there, but more on the timing of the other rate, why not now? And then really kind of what's driving? Is it more of a frequency or severity that's driving your need for rate? Thank you.

## A - Michael F. Klein {BIO 19674145 <GO>}

Sure, Michael. Thanks for the question. Really that the timing is really just a function of the process. We're actively putting together filing packages and engaged in conversations with State Insurance Departments as we speak. So it's not a question of waiting to get rate, it's just a function of the process of working with regulators to get rate increases filed and approved. And to your question about frequency and severity again, I think in my comments about the quarter in particular, we're seeing frequency coming out of the quarter, returning more towards pre-pandemic levels and we are seeing severity pressure has spiked out some of the physical damage pressures and I can give you a just a quick example there, right?

And you've all seen the news about used car prices being up 50% that particularly impacts us in the case of total losses where the average cash value and that loss is up pretty significantly. There's a little bit of an offsetting good guy there because we get more for the salvage recovery on that total vehicle but net-net that's putting upward pressure on severity and that's one example total cost to repair vehicles is up - bio injury [ph] severity is also got up, got upward pressure on it. So, we're planning really to both frequency and severity to answer your question on the drivers.

## Q - Michael W. Phillips {BIO 21023048 <GO>}

Okay. That's all for Mike and maybe it's the follow-up in a minute. If the timing you say is more of a process, it sounds like you'd rather do -- can do some sooner rather than later. Does the -- I mean, your margins today in a second quarter we're still better than 2Q 2019 -- I'm sorry, still better than 3 - but you expect things to change so do - with margin is still better do you expect much of a pushback from anybody at the state level to say you guys and maybe some of the industry still have really good profit here. So that might be a bit of a push back on - I don't know how much you expect to get from rate but that might be some pushback on the ability to get rate that you want given pretty decent return still?

## A - Michael F. Klein {BIO 19674145 <GO>}

Yeah. Michael, I think it's a great observation, and it is part of that process that I that I described is really a conversation with regulators about what the historical experience has been. But also pointing out that, part of that favorable experience is really due to the extraordinary event that was the fact -- that is the pandemic. And so we're in conversations with them about how to weight historical experience versus prospective views of trend and also state-by-state experience varies and our starting point varies by state. We've talked in in prior quarters about the fact that we did take rate reductions in over 20 states across the country. And so those are certainly some of the places we're looking at initially to see if we could take some of that rate back, which is a different conversation maybe than in a state where we didn't file a rate decrease historically.

So again, great observation and really all part of that process that we're that were engaging in as we speak.

## Q - Michael W. Phillips {BIO 21023048 <GO>}

Okay Michael, thank you very much for the details. I appreciate it.

## Operator

Thank you. The next question is from the line of Ryan Tunis from Autonomous Research. Your line is open.

## Q - Ryan Tunis {BIO 16502263 <GO>}

Hey, thanks. Good morning. Can you guys hear me?

(Multiple Speakers)

I'm sorry about that, just got back to the office today, so getting used to the old phone. So I just want to keep it on Personal Auto, when we think about where you're seeing some of the elevated lost trend, Michael, is it more geographic or is it preferred versus more standard? I mean like what are the kind of a variable is that you're looking at the most to kind of think about where you're seeing loss trying to come back the most?

## A - Michael F. Klein {BIO 19674145 <GO>}

Yeah, great, great question Ryan and good morning, welcome back to the office. We are seeing it -- there are variations across geographies. We look at things like return to normal indices, we look at driving data by state, and by geography. But broadly speaking most areas of the country are seeing driving activity return again, to close to pre-pandemic levels, closer in some places than others. We also continue to monitor as we've talked about in the past commuting miles versus non-commuting miles and there is still a different mix of miles today than there has been historically, but when you put all that together and you look at claim frequency, the frequency benefits we saw and that's what part of my comment about as we exited the quarter, the frequency benefits we've seen over the past few months and quarters have started to wane in and wane throughout the second quarter which is part of our comment about trends returning to pre-pandemic levels.

## Q - Ryan Tunis {BIO 16502263 <GO>}

Got it. And I guess my follow-up is one of the home side. So the home attritional loss ratio is above 60 [ph]. That's clearly somewhat elevated, but we've seen the price of something like lumber, timbers come down quite a bit since mid-2Q. How much of an alleviating factors should we think about that moving forward, in terms of the type of pressure that's putting on the loss ratio in home or was putting on the loss ratio on home?

## A - Michael F. Klein {BIO 19674145 <GO>}

Sure, it's a great question Ryan. I would say a couple things. First, in my remarks I did talk about frequency and severity in particularly frequency and severity of fire and non-weather water losses, driving some of that underlying deterioration. So clearly the lumber prices are severity item not a frequency item and we are seeing up - we did see uptick in the quarter in both. I would take a just a quick step back as we're talking about auto and property though and just make a couple of observations and then come back and finish the answer to your question. If you take a step back and you look at the segment combined ratio on both an overall and an underlying basis. It's very consistent with the long run average for this business. And when you look at the auto combined ratio, not surprisingly in the quarter, it still ran below the long-term average. And in Property, in the quarter, the combined ratio is call it, 4 to 6 points above those long-term averages on a total in an underlying basis. So, that just sort of gives you a little bit of an order of the magnitude of what we're talking about here.

I'd also remind you that Property -- in Property, the combined rates are the highest combined ratio we see in the year is the second quarter. So you got to sort of put the second quarter into context. But that said, the severity pressure we saw in the quarter was combination of labor and materials. So certainly the, 50% plus increases in lumber are in there, double-digit increase in roofing materials is in there, high single-digits to low double-digit increases and labor is in there. And when we look at our property loss cost mix, it's really labor followed by contents, followed by materials.

So even if -- the short answer your question I think is, even if lumber prices come back down that does still a relatively small component of the loss cost. But we do see period to period volatility and frequency and severity and the attritional loss in Property. So again, that's part of why I give you that long run view of where the quarter was relative to history and at the end of the day we take a step back and we look at the renewal premium change. We're driving in Property and our focus really is to continue to drive rate and property to address some of those pressures.

## Q - Ryan Tunis {BIO 16502263 <GO>}

That's really helpful. Thank you.

## Operator

Thank you. The next one is from the line of David Motemaden from Evercore ISI. Please go ahead.

## Q - David Motemaden {BIO 18818634 <GO>}

Hi, thanks. Good morning, just wanted to just follow up a bit more on the auto side, so maybe Michael. I'm just wondering, I guess, obviously you're taking rate. But how you're thinking about balancing, taking rate versus what could be maybe short-lived severity increases or is it view that these increases in severity that you're witnessing are not transitory and might be more sustainable?

## A - Michael F. Klein {BIO 19674145 <GO>}

Yeah, it's a great question and certainly, as we've talked about severity trend over time, we've pretty consistently talked about the fact that we take a long-run view of trend when we set our prices. Now, if the starting point is elevated because we've seen an uptick in severity and that in our lost costs, the question is your starting point elevated and are you trending off that elevated starting point or is your experience you're seeing or is the experience we're seeing in this quarter and normally. I think if I broke apart frequency and severity for you I'd say again, we continue to see the frequency trending towards pre-pandemic level that's continuing. How much of the auto materials cost, physical damage cost, inflation is transitory or not is a key question. And there's a lot of varying opinions around that and we'll factor our best estimate into that assessment as we factor in what we think we need for rate on a go-forward basis.

## A - Alan D. Schnitzer {BIO 3529437 <GO>}

Let me just add to that, whether inflation, what -- our view on whether inflation is transitory, we're certainly looking out over the duration of the liability. So when we're talking about CPI-type inflation again, lumber-used cars will (inaudible) up that's impacting relatively short tail line. So we don't really have to forecast long term in that case, and because it's short tail, the claim activity comes in pretty quickly, we see it reasonably quickly and we can react to it pretty quickly.

## A - Michael F. Klein {BIO 19674145 <GO>}

Yeah. Great, point Alan.

## Q - David Motemaden {BIO 18818634 <GO>}

Got it. That makes sense. That's helpful. And then, maybe a question for Alan, just on the investment in Fidelis, I was hoping maybe you could elaborate on the thought process behind that? And maybe sort of thinking around your own non-admitted offering and sort of aspirations there?

## A - Alan D. Schnitzer {BIO 3529437 <GO>}

Yes, thanks for that question. We've got a fair amount of interest in this, which I'm thrilled to have the interest in it. We're interested in it as well. Let me put it in a little bit of context, if you can infer from the fact that we didn't disclose terms, it's not a material investment for it. So I think that's just important background to start with. But having said that, when we think about investment activities, we're -- and as we've said, we're interested in things that provide some strategic capability. And, we've said for a long time that we're underweight E&S and this gives us a window into a successful innovative management team that has a lot of expertise in the niche non-admitted space. And in products and geographies that are that could teach us something as well. So, it really is about it about a learning exercise for us.

## Q - David Motemaden {BIO 18818634 <GO>}

Got it. Thank you.

## A - Alan D. Schnitzer {BIO 3529437 <GO>}

Thank you.

## Operator

Thank you. The next one is from the line of Jimmy Bhullar from JP Morgan.

## Q - Jamminder Bhullar

Hi, Good morning. So first just had a question on what you're seeing in the workers' comp market in terms of pricing, I think there's been an expectation that things would begin to turn. Are you seeing that? And then I have a follow-up.

## A - Gregory C. Toczydlowski {BIO 16615940 <GO>}

Morning, this is Greg. Yeah, workers' comp continues to bounce around. We've thought that we were going to hit the bottom of couple quarters back and then with the pandemic there has clearly been some favorable frequency activity around workers' comp and I think wages, payrolls et cetera. As we continue to work with the bureaus in terms of their lost cost recommendations, they are coming in less negative and I think the key will be around how they treat 2020. That's an anomalous year or if they're going to factor that into the overall rate making. So the overall book of business, we didn't quite hit a positive rate number, we are slightly negative in the quarter, but we do see improvement on it every quarter.

## Q - Jamminder Bhullar

And then on tote costs and sort of social inflation with sort of the reopening of courts, should we assume that we should start to see a little bit of a pickup and social inflation? And how does that affect your loss ratio? And have you been assuming have you been incorporating continued high social inflation in your lost picks through the past few quarters?

## A - Dan Frey {BIO 20727678 <GO>}

Hey, Jimmy, it's Dan, I'll take that one. We have taken the view that social inflation has gone nowhere. And that the elevated level of losses that we saw call it pre-pandemic are going to persist and that the elevated level of lost trend even off of that higher level of losses which is going to persist. So that's what we've assumed as we've continued to make our lost picks and assess our reserves. And I think it's going to be a while before we see courts work through the backlog of having been closed for much of the past year, priority in some jurisdictions is going to be given a criminal cases over civil cases whether the courts are reopening for in-person discussions or virtual, it's still a question in some jurisdictions. So, I think it's going to be a while before we know the answer, I think we said pretty consistently last year that there's uncertainty in that environment and because there's uncertainty we were taking a cautious view and our view of lost picks and reserves. But the short answer to the question is, we think social inflation is as strong as ever and that's reflected in our numbers.

## Q - Jamminder Bhullar

Okay, and then just lastly, I think Alan noted that the fact that you didn't disclose the price on Fidelis means that it wasn't a large investment, but should we assume that there should be any impact from the investment on your share buyback plans for this year?

## A - Alan D. Schnitzer {BIO 3529437 <GO>}

Yeah, Jimmy in part of our overall capital management strategy that's not going to be sort of almost by definition. It's not going to be not going to have a meaningful impact on our capital position at all.

## Q - Jamminder Bhullar

Okay. Thank you.

## Operator

Thank you. The next one is from the land of Josh Shanker from Bank of America. Please go ahead.

## Q - Joshua Shanker {BIO 21718992 <GO>}

Yeah, good morning everyone. I just want talk about - there has been a lot of question on Personal Auto, but I had one more, you - this has been the best month for growth in terms of new policies that you guys have seen since back in 2016, given that you firmly expected frequency to return. Is there a risk that you've put on customers' who came in because of a good price in the pandemic, but the price won't be adequate price post pandemic and they might lease?

## A - Michael F. Klein {BIO 19674145 <GO>}

Hey, Josh, this is Michael, I suppose there's always a risk and certainly there's pressure on retention when you start to increase prices on, that said, we feel comfortable with the pricing levels that we've been putting business on the books, I mentioned IntelliDrive as a key driver of some of our growth, distribution expansion, it's been a driver of some of our growth, there's a lot of things that you can point to including elevated code [ph] activity that are drivers of growth in Auto. We've seen some slight improvement in close rate in Auto, over the past few months as we've retained -- we've maintained RPC essentially flat but there are a lot of other drivers of growth than just price that we can point to the probably alleviate some of that.

## A - Dan Frey {BIO 20727678 <GO>}

Hey, Josh, it's Dan. Just one other comment on that. I think we've done a terrific job in the order book over recent years, in terms of understanding our appetite and having a consistent appetite. And I just point you to the last time we did take significant pricing in Auto back in 2017, 2018 timeframe. We did not shrink (inaudible) in that environment.

## Q - Joshua Shanker {BIO 21718992 <GO>}

Good point. And an unrelated topic which is sort of been addressed with the court reopening somewhat not. Can you talk about whether in 2Q you are seeing convergence between model lost cost trends and actual experience? I assume that you prepared for a lot more losses on incurred basis during the - for the pandemic that didn't occur because of the nature of courts. Is that narrowing right now, or we still experiencing loss (inaudible) far below the model overall?

## A - Michael F. Klein {BIO 19674145 <GO>}

Let me make sure I understand the question, Josh. You mean, you mean the trend in the loss ratio or you mean the level of incurred losses relative to ultimate losses?

## Q - Joshua Shanker {BIO 21718992 <GO>}

I mean, in every line of business you assume that the lost call trends will be 4%, 5%, 6% but during the pandemic it wasn't that because of courts and other reasons but you assume that that's just a delay. I'm trying to think, are you -- is your loss experience coming closer in line with your model projections? Or are we still have a huge back load of reserves for claims that haven't come through because pandemic conditions persist?

## A - Michael F. Klein {BIO 19674145 <GO>}

Yeah, I think closer to the latter. So we still have for example low pay to incurred ratios. We still have for example the majority of the ultimate losses we recognized be [ph] it for COVID sitting in IBNR.

And to the earlier question on court reopening again I think people are maybe jumping the gun on that. I think it's going to be quite wait a while before we work through the backlog here and see. So we are still expecting longer periods of development in terms of how long it's going to take to get the ultimate. And again as we said previously, even though the data itself looked good, we took a cautious view in terms of our loss picks and our reserves with assumptions more in line with our normal long-term lost trend [ph].

## Q - Joshua Shanker {BIO 21718992 <GO>}

All right then I'll dig in a little bit later, but I don't want to keep up the line, thank you very much.

## A - Michael F. Klein {BIO 19674145 <GO>}

Thanks Josh.

## Operator

Thank you. The next one is from Tracy from Barclays. Please go ahead.

## Q - Tracy Benguigui {BIO 21808177 <GO>}

Thank you. Dan you mentioned that Travelers is less leverage to overall CPI-type inflation. Are there better macroeconomic indicators we should be looking at if CPI is a lesser measure for long tail lines? I have muscle memory for my formal role that there are other indices you look at that is more nuanced for your businesses to measure claims inflation?

## A - Michael F. Klein {BIO 19674145 <GO>}

Yeah, Tracy, let me start and Dan can fill in whatever I miss. We're actually not trying to forecast CPI or inflation generally, we're trying to forecast lost costs. And we do that by analyzing our own data and incorporating forecast from third parties and we do that on a very granular basis. So take workers comp for example, we're not forecasting medical inflation, we're looking at components. So in prescription drug prices durable medical equipment et cetera. And we're doing that in the same mix that those (inaudible) cost contribute to our actual losses. So it's hard, I mean, obviously we can't give you a single number and it's hard to say, geez, go look at this index or that index because we're doing it on a funny very granular basis in part by tumbling our own data, squaring triangles and by reference to third-party sources.

## Q - Tracy Benguigui {BIO 21808177 <GO>}

Okay, so all those nuanced factors that you looking at does that worry you with respect to inflation if CPI is not the indicator we should be super focused on?

## A - Michael F. Klein {BIO 19674145 <GO>}

No, there's nothing about lost cost or inflation that's worrying us at all. In fact, we - the emphasis on in the conversation here is because to a degree we are seeing it but we saw pretty good profitability and personal lines and it's into the short term line and the consequence of that is we can see it very quickly and react to it very quickly and contrast that to say social inflation, which was an issue for us a few years ago, where takes a little bit longer for us although, I will say that I think as compared to many we saw that very, very quickly and there's not nearly as much leverage on the balance sheet. So, there's not as much risk in the reserves and we can price for it relatively quickly. So, there's, actually nothing at all about the inflation environment that's of concern to us at the moment in shorter lines or long-term lines.

## Q - Tracy Benguigui {BIO 21808177 <GO>}

Okay, great, just one follow-up on Fidelis, it's also a reinsurer. So, I'm just wondering if this partnership could look like a sidecar where (inaudible) own premiums to this platform where it could potentially compete with reinsurers on your panel?

## A - Dan Frey {BIO 20727678 <GO>}

Not, so, certainly, not at the moment, not as way we've contemplated this, it really is just the way we presented it is pretty simple, it's a really interesting business model, it's a fantastic management team, they've got a great track record, that their cultures are very compatible, what they do is very interesting to us and we wanted to learn more of that. For the time being, that's really all the risk to it and, maybe over time we'll collaborate with them and they'll be business opportunities, who knows? But for the time being it really is just as we've laid it out.

## Q - Tracy Benguigui {BIO 21808177 <GO>}

Thank you for taking my questions.

## A - Dan Frey {BIO 20727678 <GO>}

Thanks Tracy.

## Operator

Thank you. The next one is from Elyse Greenspan, from Wells Fargo.

## Q - Elyse Greenspan {BIO 17263315 <GO>}

Hi, thanks. Good morning. Alan, I guess my first question is on the Fidelis investment as well. Through the years you've said, you guys weren't interested in re-insurance fields. Obviously, there's unique features of this investment away from just re-insurance, but I just want to get a sense of just as we think about M&A, like has your stance on re-insurance changed and then you like issues $750 million of debt in the quarter, and it was earmarked for business growth. So I'm just trying to is - you tying that capital into potential M&A or is that more earmarked for organic business growth?

## A - Alan D. Schnitzer {BIO 3529437 <GO>}

Well, let me start with Fidelis then I'll ask Dan to comment on the capital raised. So there's just nothing at all about this that signals any shift in our thinking about reinsurance, we are primarily focused on being a primary writer with very limited interest in reinsurance and that remains the case. It just so happens that Fidelis writes some of their business in the form of reinsurance, but that's just one of their four pillars of business. There are some interesting aspects of the reinsurance business. They've got really thoughtful risk management tools, they are really thoughtful with risk and rewards.

And so there's the potential for us to learn something in terms of managing our own cap portfolio, and I will point out why it hasn't been and I don't expect it to be any significant focus for us. We do write a little bit of reinsurance where it's complementary to our core business. So for example we've got a (inaudible) re-business. So it's not completely important to us, it's a very small part of what we do. It's no change in strategic focus, but it's not alarming to us, and in this respect we think that there's something for us to learn.

## A - Dan Frey {BIO 20727678 <GO>}

And Elyse, regarding the capital, the capital question, no change at all in our philosophy or more urgency around M&A or lack of urgency around M&A. It's really coincidental the timing of when these things came together and again the Fidelis investment was small enough that it wouldn't have necessitated much in the way of capital management anyways. I think if you go back in the transcripts, 6 or even 8 quarters ago, we were talking about, eventually we would have the need to issue more debt just to keep up with growth in the top line and to maintain a debt to capital ratio that we're comfortable with.

## Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay. Thanks. And then my second question on, can you guys quantify the impact that exposure had on your premium growth in the quarter? And then within select accounts within business insurance, I noticed that the premiums declined in the quarter but I thought exposure would have benefited on that business line as well?

## A - Dan Frey {BIO 20727678 <GO>}

And so Elyse, it's Dan, I'm going to guess resented, resist the temptation to sort of try to do a reconciliation of upgrading [ph] premiums as the degree that there's positive exposure, the same way that the degree that there's positive rate that just means that the accounts that renewed would have renewed at that much more. Having said that, it's applicable to the accounts that renewed, that's the measure of that it would apply to. I don't know Greg, you want to -

## A - Gregory C. Toczydlowski {BIO 16615940 <GO>}

Yeah, I mean, just a little bit more color on Select. We've shared with you that we've been very focused on improving the profitability of that business. And so, we're certainly been very thoughtful around production and pursuing margin improvement for rates and terms of conditions and that sort. I will tell you also in the Select business, during the pandemic because of some of our ability to have a little more flexibility for a customer we suspended some billing and some cancellation activity and now that's back in play in the marketplace. You have a little bit of drag on the top line with that, just back to normal activity, but when comparing that to the base period that has a little bit of an impact also at least.

## Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay. Thanks for the color.

## Operator

Thank you. The next one is from Brian Meredith from UBS.

## Q - Brian Meredith {BIO 3108204 <GO>}

Yes. Thanks. Most of them have been asked. I just it's curious, wildfires are kind of kicking up here in the west coast, maybe you can talk a little bit about what you've kind of been doing over the last couple of years to get to manage your exposure to the wildfires?

## A - Michael F. Klein {BIO 19674145 <GO>}

Sure, Brian. This is Michael. And certainly, we're managing our exposure to wildfire across the business. But I'll start with the Personal Insurance. I think a lot of the actions are common across the place but Greg can chime in if I miss anything on the commercial line side. It really is a continuation of the conversation that we've been having with you in terms of the way we've been managing it, I think we've talked a lot about California in particular in the context of wildfires, but certainly the peril is the peril that exposes us across more states in the west than just California.

So one specific development I would point you to in 2021 is, we've extended our agreement with Wildfire Defense Systems to apply to Colorado, in addition to California, so we've got that sort of risk prevention partnership extending across an additional state in the west which we think on the margin is helpful. And then, maybe just an update on our progress in California, in addition to the launch of the new product, which we successfully got in market in 2020.

We're now converting California policies to that new product so think new pricing segmentation, think new rate level, think new eligibility as respect wildfire exposure and just last month we got an additional 6.9% rate increase approved on the property product in the state. So we continue to manage through rate eligibility terms and conditions. And we do continue to work our way through the non-renewal activity subject to the lifting of the moratorium as they expire on as another as another lever we're pulling. And again a lot of those are specific California comments, but you can think about those on in terms of again segmentation modeling, exposure management applying more broadly across the West.

## Q - Brian Meredith {BIO 3108204 <GO>}

Thanks. I guess the quick follow up here, just curious you continue that's really strong growth in your commercial property lines. Can talk a little bit about what the kind of market dynamics are in that line on that line that's the one area that I thought were seeing pricing really kind of moderate the quickest?

## A - Michael F. Klein {BIO 19674145 <GO>}

Yeah, we - as you saw we have plus 9% across the property line and really that the primary amount of growth underneath that is RPC driven. And that's why we gave you that supplement exhibit or Excess Casualty and National Property, were two of our many specialty lines that we have but to have certainly been the poster children for some rate momentum over the last couple years and as I said, still yet in double digit but moderating somewhat. But that's what's driving that growth.

## Q - Brian Meredith {BIO 3108204 <GO>}

Great. Thank you.

## A - Michael F. Klein {BIO 19674145 <GO>}

Thank you.

## Operator

Thank you. We have time for one more question and that would be from Meyer Shields from KBW. Your line is open.

## Q - Meyer Shields {BIO 4281064 <GO>}

Great, thank you so much for filling me in. One last, well, obviously last question on Personal Auto, can you talk about the trajectory of frequency month-by-month in the second quarter just so we can assess what's going on?

## A - Michael F. Klein {BIO 19674145 <GO>}

Meyer, I don't know if I am going to give you a numbers more specifically inside the quarter, I think, what we said well let's stand which is, that as (inaudible) the quarter frequency with closer to pre-pandemic levels, you sort of know where it had been running I think, coming into the quarter. And again, it approach pre-pandemic levels, as we left the quarter.

## Q - Meyer Shields {BIO 4281064 <GO>}

Okay. Fair enough. And then I guess, this is for Greg, when we look at the presentation on select accounts, the RPC for the first quarter of '21 showed up as 8.8% when you actually reported in 1Q it was 6.7% that seems from the outside like a big change, that's what you can talk about the process and how we should think about the inherent estimates in the RPC.

## A - Gregory C. Toczydlowski {BIO 16615940 <GO>}

Yeah, Meyer, both of those quarters don't close - the fourth quarter and the first quarter developed out, as you said, about two points. And I'll just remind you that, that's an estimate of what we believe the current force is going to look like in terms of the exposure growth. So we're always estimating that and when you have a V impact in the economy, your model sometimes don't keep up with that really quick and adroit change that's happening. So we basically shortened their model period. So if we were using a 6-month moving average thing, we move do a three month moving average to try to keep up with that change in the marketplace and that gives us a little bit change in the development. So we think will be in front of that going forward. But that was basically the methodology underneath that.

## Q - Meyer Shields {BIO 4281064 <GO>}

Okay, perfect. That's exactly we needed. Thank you.

## Operator

Thank you. Are there are no further questions at this time. Ms.Abbe Goldstein, please continue.

## A - Abbe Goldstein {BIO 20602454 <GO>}

Thank you very much. Appreciate everyone's time and for joining us this morning and as always, if you have any follow-up, please feel free to reach out to Investor Relations and good day, everyone.

## Operator

This concludes today's conference call. Thank you for participating. You may now disconnect.