Bank of America Merrill Lynch Securities Insurance Conference

Company Participants

- Beth Costello, Chief Financial Officer
- Christopher J. Swift, Chairman & Chief Executive Officer

Other Participants

- Jay Cohen

Presentation

Christopher J. Swift {BIO 3683719 <GO>}

So thank you for just for the opportunity. I thought I'd just touch upon a couple things. 2019 was a excellent year for the Hartford, both strategically and financially. Financially, and the results speak for themselves, but at high level we generated $2.1 billion of core earnings an ROE of 13.6% and we're able to grew book value per share about 11% for the second consecutive year.

Strategically, I think we've proven we have the ability to acquire, and integrate operations companies into our platform that helped us expand our underwriting capabilities, expand our product sets and grow our distribution channels and capabilities.

So really at the Hartford we have been focused and we'll continue to focus on execution in organic growth. We talked about for Navigators, the integration is proceeding well, we're about nine months into it, and I think we have our arms around it as far as what we have in the capabilities that we acquired.

We're pleased with it, but we're really focused on improving the underwriting performance of that business unit. We're looking at how we cross sell within our larger platform, we think we're bringing to Navigators enhance claims capabilities with our fast claims operations and then really leveraging all the Hartford capabilities.

And when I say that I specifically mean data and analytics in our deeper actually our real capabilities. So things are on track. In our earnings call in the fourth quarter, we did reaffirm our view that we can create $200 million of incremental core earnings and what we did was we shorten that by a year, when we closed the deal, we talked about generating that over a four to five year period of time. Now, we think, we could generate that over a three to four year period of time.

And as I said, we have our arms around Navigators it's operations, the changes that we've done over this past year, give us great confidence going forward that we'll be able to expand margins. We also talked about, expanding Navigators margins in that 5% to 6% range on an overall combined ratio. And that again is really driven primarily by underwriting action, pricing actions, policy limits, looking at terms and conditions differently, and quite honestly exiting businesses particularly in London, that just weren't profitable.

So if I then changed to the Commercial Lines, we provide our guidance for underlying combined ratio in that 92% to 94% range, that is an improvement over this year. Primarily, again driven by the five to six points of Navigators of improvement, and I mentioned, where that's coming from. And then also, we see improvement in our core Small Commercial, Middle and Large Commercials segments, in spite of some margin compression, slight white margin compression in workers comp, and that's just reality, that's just reality, and I'm being honest and transparent as we always are.

If I look at Group Benefits, Group Benefits add a outstanding year with $539 million of operating earnings core earnings, a margin of 8.9% and largely what we're foreshadowing is that they where at the late stages of finalizing the integration of the Aetna book and we're pivoting towards growth. Growth in new products, new services that complement our existing core capabilities, and ultimately focusing on a better customer experience, particularly the employer experience.

As relates to capital management, I think we continue to be thoughtful in managing excess capital that's generated beyond, what we need to fund growth in our operations. We announced our $1 billion buyback program a year-ago. We expect to buyback about 800 million of shares this year in 2020, and we raised the dividend 8%. So, as I sit here Jay, I think we ended 2019 with significant confidence in momentum as we head into 2020, about improving our operations particularly margins, and creating shareholder value for that. So that's what I would say.

Jay Cohen {BIO 1498813 <GO>}

Any opening comments from you just about how the balance sheet shaped up relative to what you expected at the end of the year.

Beth Costello {BIO 15349374 <GO>}

I think when you look at the things that we've done over the years to get the balance sheet, I think in a very good position and we've talked for a while about our goals relative to leverage ratios and so forth and we see ourselves really within of those goals as we look to pay down some maturing debt this March, so very pleased with the profile there as Chris commented on we're pleased to be able to increase the dividend again, this year, and so I think it positions us very well going into 2020.

Jay Cohen {BIO 1498813 <GO>}

Just a follow-up something Chris, you said about the Navigators, you talked about achieving your goals one year earlier. So that always begs the question, what changed relative to our your original expectations.

Christopher J. Swift {BIO 3683719 <GO>}

Sure. Well, we laid the path out to the $200 million as far as improved underwriting results, expense synergies, and enhance net investment income. All three of those are still the components, but we didn't anticipate this level of rate increase, we talked about it in the fourth quarter. I mean basically the Navigators Group is plus 15% and closer to 18%, and we see that continuing into the second half of '20.

So as those rates earn in your roll forward a couple years of continued rate increase, we think we do have our arms around a loss cost trends for Navigators. We're going to hit our goals a year sooner than we anticipated.

Jay Cohen {BIO 1498813 <GO>}

I assume you thought initially those prices might be up single-digit?

Christopher J. Swift {BIO 3683719 <GO>}

We in essence had a view -- I wouldn't say exactly single-digits, but in that higher range of single-digits just given the needed improvement where ROEs were, but we're basically doubled the rate increase in from our original expectations in spite of interest rates coming down in this really wasn't an expense play for us, this was an expanded capability and maximizing our distribution fleet.

Jay Cohen {BIO 1498813 <GO>}

Let's talk about I guess the Commercial Line market. You seem to express some conviction at this pricing momentum would continue into this year maybe even into next year, as you look at the world what gives you that level of confidence?

Christopher J. Swift {BIO 3683719 <GO>}

Well, the straight answer is I don't think as an industry broadly defined, we've really kept up with loss cost trends over the last five-years or six-years. And if you look at where we are today in certain lines of business with our combined ratios, it's going to take 18 to 24 months of continued rate increases -- rate on rate increases. I think to hit targeted returns and commercial auto liability and property. You coupled that with a low interest rate environment, lower for longer and with 10 year today 160, 155. I think as an industry we need to continue to be disciplined and focused on rate and underwriting to make up for that loss in NII that inevitably is going to happen.

Jay Cohen {BIO 1498813 <GO>}

The question that I get a lot is yes prices are going up but there's a reason claims are going up as well not across the Board, but in many lines. As you look at into 2020 and '21, is your assumption that the loss environment continues to get worse from here or get better, what's your underline assumption?

Christopher J. Swift {BIO 3683719 <GO>}

We believe, it's stable, but again, it's making up for sort of accumulation of years of not keeping up with trend. I think we've been pretty clear that we feel good about where we have trend peg today and that 5% range in aggregate for our portfolio, and we just need to continue execute above that to be able to expand margins, from here. So, but I would say again at least for our book of business, we don't see anything dramatically shifting, we've talked about sort of our litigation rates, our representation rates have been very stable.

We're not experiencing a major shift in any of our liabilities. We've seen over the years the last five-years is the need to make adjustments in loss picks for certain liability lines, primarily commercial auto in general liability, we've done that. So Jay for us and our book, we just need to keep up with that trend that we pegged for liability lines in that 5% range primary its maybe a little less, you get into umbrella and excess, it could be a little bit higher, you blend it all together.

And as an industry, which is need to catch up from where we were.

Jay Cohen {BIO 1498813 <GO>}

Is it fair to say that the backdrop is a fairly rational industry. In other words as you take this action, would you expect your new businesses suffer notably or your renewal retention to be impacted?

Christopher J. Swift {BIO 3683719 <GO>}

What I would say is the trade between rate and retention. You always need rate ahead of retention, because if you have an unprofitable account or unprofitable segment, just need to fix it and if it leaves you, it's unfortunate from a customer side, but that's you need the rate in your book.

So, I would say generally, our distribution partners understand the environment. We've been working hard with them, particularly the last six-months to nine-months to educate the reason for the rate, the trend environment and I think we have alignment with our distribution partners about what are the actions that we head into '20, and then also head into '21.

The best example, I can give you maybe just tangible is that, we worked really hard on our commercial auto book over the last six years. It's about a $600 million book of business to us. We put about 50 points of aggregate rate into the book over that period of time, and it still produced 102 combined ratio today. So, when I talk about the next 18 to 24 months to get that line to targeted rate increases. We're going to need 10 points to 12 points of rate this year, 10 points to 12 points are rate in '21 to even get close to earning an adequate return on risk adjusted capital.

Jay Cohen {BIO 1498813 <GO>}

You could argue guys have been maybe a little ahead of the curve there. So arguably others would have to at least see that kind of increase if not more.

Christopher J. Swift {BIO 3683719 <GO>}

I'm not going to disagree with you

Jay Cohen {BIO 1498813 <GO>}

Okay, fair enough. Let's turn to workers' comp. I guess it was last year or the year before. We had this bit of a speed bump, I think it was in the third quarter. We've talked, I think the market made too much out it, was it second quarter.

Christopher J. Swift {BIO 3683719 <GO>}

I think it was first half of the year.

Jay Cohen {BIO 1498813 <GO>}

Okay. What are you seeing as far as claims trends there now? And for us to actually see prices going up in workers' comp. I'm assuming there would have to be some sort of change in the claims trend.

Christopher J. Swift {BIO 3683719 <GO>}

Yeah, so you are right. We did basically the first half of the year signal that the frequency of claims not severity. The frequency of claims in certain segments of our book was increasing. And if you remember at that time, we talked about sort of the demand surge that we suspected occurred with tax reform and hiring and getting maybe more inexperienced workers into certain job classifications that pose just more injuries, early on and that is still is what largely happened in our book of business. So, if you look at segments, like retail, restaurants, I'll call it high demand maybe high turnover businesses, there was a little bit of surge hiring that just was inexperienced in certain classes including manufacturing.

I think that largely settled down in the second half of the year. And so as we sit here today the trend really over the last six quarters except for those blips in the first two quarters of '18 has been frequencies have gone back to normal, and have been slightly negative and severity particularity in medical is better than our long-term assumptions that we generated plan for in that 4% to 4.5% range.

So I think the line is performing well, we still make good margins and returns, but with the continued rate rollback pressure due to good experience, those margins as we alluded to and guided to are going to be under some slight pressure heading into '20.

Jay Cohen {BIO 1498813 <GO>}

What's interesting is those factors that you cited, when the frequency picked up, arguably are still around and in place yet, it seems like the frequency settled back down again. The impossible question is why do you think that happened? No, there's no answer, but if you can treaty it as a thought about it?

Christopher J. Swift {BIO 3683719 <GO>}

I called it demand surge, right. So, when you needed workers, there was a demand surge primarily rated, I believe to tax reform and some of the stimulus, and then what happens is people get trained as they get more experience as safety always continues to improve it reverted back to the long-term mean.

Jay Cohen {BIO 1498813 <GO>}

Let's talk about Small Commercial. You're obviously a leader in that area, but you're not standing still, you continue to make investments there. Can you talk about some of the more recent investments you've made, and how they could drive growth going forward in that platform?

Christopher J. Swift {BIO 3683719 <GO>}

Sure. Yeah, we're clearly really proud of what we've done with Small Commercial over an extended period of time. It's been about 30 years since we launched that segment of the business, and it's one that we've constantly invested in for innovation, for customer experience.

I think there's two examples that I can give you just quickly Jay without sounding like a commercial. Unless you want it to sound like a commercial.

Jay Cohen {BIO 1498813 <GO>}

Go right ahead. You got a platform might as well. We're not going to charge you for it.

Christopher J. Swift {BIO 3683719 <GO>}

Thank you. As we rolled out what we called Next-gen Spectrum, which is basically our BOP policy our Business Owners Policy, that combines property and liability insurance.

We've had a BOP out there for a long time that is used by many different classes of business in the industry, but this one was basically a modular design. So if you think of Amazon in your shopping cart, we're able to present to agents, that are quoting our BOPs a more modular approach of sort of what is a baseline -- policy-based line from a liability side, and then all the additional coverage and features that you can add whether it be cyber enhanced protection in liability.

Industry specific recommendations for like restaurants, or dentist office. So, we really customized it, so depending on what type of customer you were we're able to present to you optional coverages, price points for those optional coverages, that protect your business more holistically on a more transparent basis and clearly with more speed, so that sort of your running total of what your spend for your policy.

So, we think it was well revolutionize, the BOP business, and we weren't going to be able to do that, until we basically, invested in some core platform capabilities of how we administer policies, how do we quote, so those all investments in started four or five years ago on a baseline basis, that allowed us to innovate today with our next gen spectrum.

The other thing that I would just say, and I know everyone in this room now is it, but the power of data and analytics is real and our ability to cut down questions from let's say, 50 years ago down to something less than 10 to be able to pre fill data that makes underwriters and agents jobs easier, to be able to use imagery in underwriting, just the advancements in data and analytics that's embedded into the Small Commercial underwriting process is pretty impressive.

Jay Cohen {BIO 1498813 <GO>}

So, it's interesting you mentioned, Amazon, people are so used to buying goods that way, especially younger people, that are it's the phone or the computer, but that whole process of buying something with a card. And so, your I guess you're tapping into that, I think certainly as these younger people come up in the industry, that's a natural thing for them.

Christopher J. Swift {BIO 3683719 <GO>}

Sure. No, it really is and the way we really present it and if you want you can go online, and see it, it's sort of the base, sort of the good the better, the best. And then you could see the optional coverages that are attached to each of those different characterizations of good, better, and best.

Jay Cohen {BIO 1498813 <GO>}

There something that I guess you haven't been impacted too much by, but you'd hear well than the industry is this whole concept of social inflation except that some of your businesses. Give us your thoughts on what do you think is causing that, is it just more aggressive creative lawyers, is there a backdrop politically or socially that's changing it ?

Christopher J. Swift {BIO 3683719 <GO>}

True. Well, you like you said, and I said it a couple times in our earnings call. I mean it's a phenomenon that's affecting all aspects of the insurance business, East Coast, West Coast, Central and its effects vary obviously based on your business mix and what I was trying to describe is our primary liability to writer might have certain impacts, excess writers might have more as you get more severity into those types of conditions and events, but what we are also trying to say is that I think we've been ahead of the curve, when we've been adjusting and reacting to social inflation over the last five-years in various aspects of our book. The root cause, look, I'm not a sociologist.

Jay Cohen {BIO 1498813 <GO>}

That sounds good.

Christopher J. Swift {BIO 3683719 <GO>}

Yes. I am an accountant. I just think we're in a litigious environment. I think maybe plaintiffs' bar is doing a more effective job in arguing for larger settlements, maybe juries are more sympathetic to injuries and outcomes.

Whatever it is and others have talked about it, so I'm stealing some of their language, it's a tax on society that we all pay in one way shape or another. So how we fight it? We do it every day with our claims and law professionals and trying to say what's a reasonable settlement.

I always say we're in the business of playing claims, those that are legitimate covered by our contractual terms and languages, and that's fair. That's not excessive or punitive, and that's our philosophy that we approach for our shareholders and our policyholders.

Jay Cohen {BIO 1498813 <GO>}

I wanted to shift away from Commercial Line before I do that. Are there any questions out there on Hartford's Commercial Lines business before I make that shift. Do you have questions raise your hand, we'll get you a mic. I covered a lot of ground, you guys cover a lot of ground. And that was pretty good for an accountant by the way.

Christopher J. Swift {BIO 3683719 <GO>}

Resemble that.

Jay Cohen {BIO 1498813 <GO>}

That's let's shift to you. You had kind of alluded to before in your opening comments about getting the leverage ratio down to your goal walk us through, I guess the next two years capital generation. What debt you're retiring? And kind of when do you think you can get to those margin levels or the leverage levels that you expect?

Beth Costello {BIO 15349374 <GO>}

So we did I think lay out pretty clearly in our earnings release, our thoughts on capital generation for 2020. So what we're expecting as far as dividends from our operating companies and so, again our P&C Company targeting dividends about $850 million to $900 million, Group Benefits 3 to 350 and then mutual funds $100 million to $125 million.

We do still have some more tax attributes on our balance sheet that were monetizing, and so we expect a little over $500 million of cash receipt to the holding company as we both get refunds of our AMT credits, as well as just continue to use our net operating losses. So, very healthy cash flow to the holding companies as we look at 2020. As I mentioned, we do have some debt maturing in March and we do plan to pay that down not refinance, so that's $500 million of debt.

And so when we put that into the mix, it puts us in a really nice place relative to our leverage ratios. And then from a holding company cash requirement, it's really just interest in dividends. All of our operating expenses are allocated to our subsidiaries and interests in dividends are little bit over $700 million.

So, kind of give you a sense of the sort of what the cash flow generation is. As Chris said, we do have $800 million of share buybacks that we'd be doing in 2020 to complete our billion authorizations. And then as we look beyond that again, as our operating companies continue to improve as far as earnings, we take that into consideration as far as dividends in the future.

And so, I think and so I think there'd be some room for those to increase slightly and we just raised our dividend again. We've been on a path of doing that year-over-year, so we continue to evaluate if that made sense to do in the future, and then that kind of gives you a picture of just the excess cash flow that we have at the holding company to decide what the best use of that would be.

Jay Cohen {BIO 1498813 <GO>}

So, you've done two decent-sized deals, acquisitions over the past several years. And I'd say you executed on them well so far, but some hiccups with Navigators, but you're obviously achieving your goals quicker than you thought.

Christopher J. Swift {BIO 3683719 <GO>}

Incredible with the hiccups, but this is your stage,

Beth Costello {BIO 15349374 <GO>}

Well fair enough.

Christopher J. Swift {BIO 3683719 <GO>}

Because it was all part of the plan purchased and sort of opening balance sheet and reinsurance and all the adjustments. We're eyes wide open on getting our arms around day one.

Jay Cohen {BIO 1498813 <GO>}

So you've actually hit on both pretty well quite well, I would say. It always raises the question; You're not going to close your eyes to future acquisitions. When you think about the ability to acquire businesses. Someone comes to you tomorrow with the perfect deal what does that look like to you? Realistically.

Christopher J. Swift {BIO 3683719 <GO>}

Sure. Well, yeah again the contexts of our acquisitions were things that we needed to do from a platform side, to expand our capabilities to basically serve more customer needs. That was the primary genesis behind our acquisitions, whether it be the scale business that we achieved with Aetna or really some of the specialties and the liabilities. Specialty orientation we picked up with Navigators, I thought both were strategically important and financially will work out very well for shareholders.

So, the bars high going forward principally, because I think we have everything we need as a platform, as an organization. We just like to grow it organically make it bigger, have larger scale, have more shelf space in our agents office. So, so I'm trying to describe that there's not a burning desire of a need to do any additional acquisitions, but like you said, I mean we're aware, we'll listen but the bar to executed is very high because it is just really needs to be very,very accretive compared to where we are today.

But if something were to come along in the Small Commercial space or the Middle Market space that would be a nice complementary bolt on that would give us additional scale benefits. Particularly, in small I think we have the most efficient Small Commercial operation. So, we could leverage that great operating strengthened. With Middle Market, clearly, our goal is to be a bigger and more relevant player in that marketplace, and we're committed to doing it organically, but if there's something that accelerates that we'll consider it.

Jay Cohen {BIO 1498813 <GO>}

Got it. Any questions on capital or M&A? On this topic, no one wants to challenge what he said, fair enough.

Let's talk about a business that part doesn't get enough attention, because it's been a great business and that's the Benefits business. It feels like your 2020 guidance is really conservative, given how great these results have been? What are we missing here?

Christopher J. Swift {BIO 3683719 <GO>}

Well, yeah, I mean it's $5.5 billion business, we are the second largest writer behind MetLife, I think is right around the corner here.

So yeah, we're really proud of what we've built organically how we've improved that business. I'm always reminded, when I joined the Hartford in 2010, in 2011 that business earned about $65 million or $75 million of earnings. So it's at a pretty good turn around and the acquisition obviously helps.

So yeah, all I the guidance really implies, is at 8.9% margin, it's probably unsustainable. We experienced obviously very favorable severity, excuse me -- frequency and severity of getting people back to work and recovery our approach to pricing and reserving assume sort of a five year averaging, and that's what the guidance reflect.

So you're right, if the economy continues to perform, the people don't go out on disability meaning lower incidence continues, we have a chance to outperform, but the way we price products give them we make in three year rate guarantees or four in some cases, way we reserve is and we assume earnings would emerge is more on a five-year average basis of those incidents and recoveries. And that's what we guided to.

Jay Cohen {BIO 1498813 <GO>}

Got it.

Beth Costello {BIO 15349374 <GO>}

The only thing I'd add is what another component of the outperformance was the performance of the Investment portfolio. So our limited partnership portfolio performed very strongly across our businesses, but in Group Benefits as well and we have a -- we again take a long-term view when we plan, so that's also a component of that decrease.

Jay Cohen {BIO 1498813 <GO>}

We all hope that's going to continue. On this business you sort of suggested in your opening comments, Chris pivoting towards growth. We got a little bit of time left, talk about the sources of that growth? Where does that come from?

Christopher J. Swift {BIO 3683719 <GO>}

Sure, well, I think there are two main sources. Our core product capabilities Group Life, Group Disability both long-term and short-term are scale businesses, where we're not at scale is our voluntary businesses, and voluntary in our vernacular means, critical illness, hospital indemnity, AD&D, accidental death, business travel accident, you get into the A&H side of things so.

I think there's an opportunity with our customer base over 20 million customers, our distribution relationships to really enhance growth in our voluntary, A&H space and that's what we're going to do.

Beyond that, we're thinking about I'll call it wellness in general, and technology, and services, and how we might augment some of our core capabilities, but that those are things on the drawing board, but we are thinking just how is this whole health care wellness benefits space going to emerge. So, those are probably the three primary areas two short term voluntary and A&H, where we have products on the street today and one a little bit longer term where we're innovating on offerings and capable and services.

Jay Cohen {BIO 1498813 <GO>}

Got it. My last question in the time we have left. I was interested to hear in your call. When you were talking and your fourth quarter call. You mentioned a number of positive I'll call them ESG type attributes of the company. We generally don't hear that from insurance companies. My question is, why did you bring that up? Are you getting feedback from shareholders, investors, employees to suggest this as a bigger issue?

Christopher J. Swift {BIO 3683719 <GO>}

I think from an investor side and you could point to people in this room and their firms and some of the stances that people have taken on broad ESG issues.

Yes, it is becoming more and more important for investors to understand companies and their strategies and their logic behind ESG. I think we've been a leader in this area for a good decade. So this isn't anything new to some of the things that we've been working on as an organization.

We define it more from a sustainability perspective in I'll call it four quadrants: one governance and ethics, second quadrant would be diversity and pay equity, third quadrant would be communities and giving back and the fourth quadrant would be environmental EG your carbon footprint.

So we've been working on these things for well over a decade. We've gone public with goals. Last year about this time where I put out a sustainability goal report in those dimensions so yeah, I do think it's becoming more relevant, more top of mind because -- you need a multi-dimensional focus. I think for all stakeholders to create value over a long period of time, and obviously we're a shareholder driven organization.

We got to deliver to your shareholders first, but I believe there's ways of balancing that with the other dimensions of creating a good work environment, good community environment for the long term.

Jay Cohen {BIO 1498813 <GO>}

I thought it was great that you brought it up. I'm not getting attempt of questions on it, but I know in our department in the equities business in general, it has become a really big issue and it's great that you're kind of leading that and making sure your view of this is out there, it's great. We are really bumping up against the end of the session. why don't we call it quits here. Chris, Beth thank you very much for joining us again.

Christopher J. Swift {BIO 3683719 <GO>}

Thank you.

Jay Cohen {BIO 1498813 <GO>}

Fantastic, that's great.