S&P Capital IQ

CONTENTS

Universal Insurance Holdings, Inc. NYSE:UVE

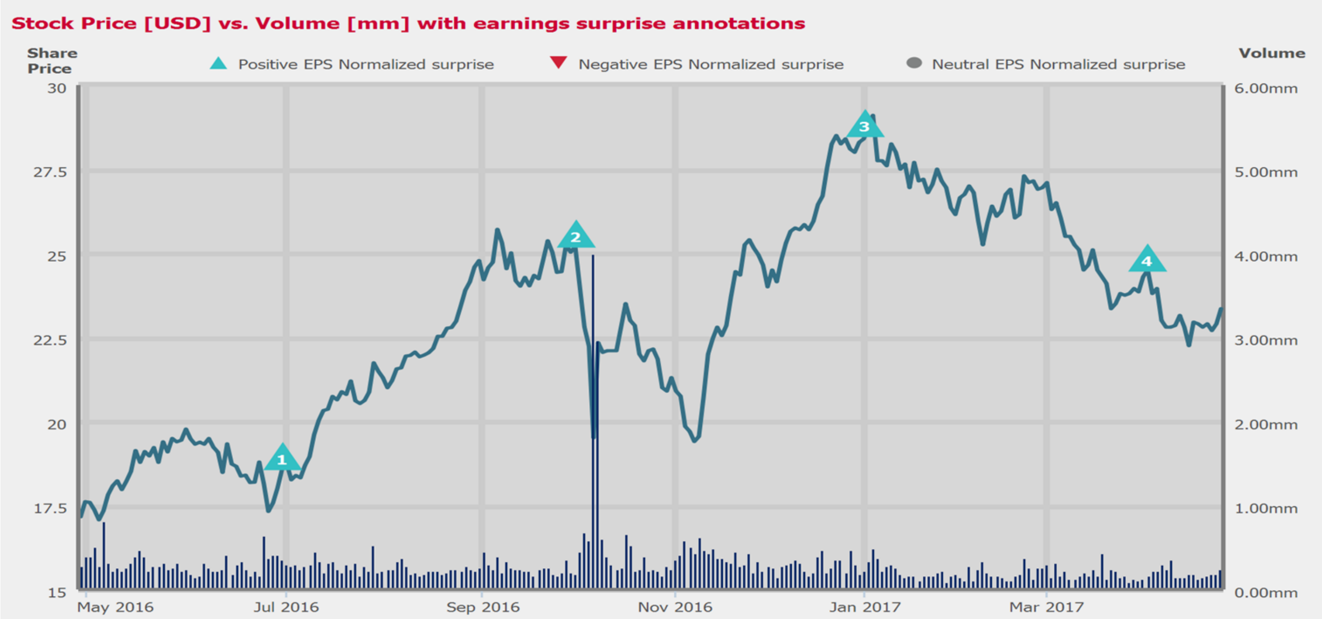
FQ2 2017 Earnings Call Transcripts

Tuesday, August 01, 2017 2:00 PM GMT

S&P Capital IQ Estimates

	-FQ2 2017-			-FQ3 2017-	-FY 2017-	-FY 2018-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.73	0.82	▲12.33	0.67	3.09	3.40
Revenue (mm)	-	-	-	-	-	802.39

Currency: USD
Consensus as of Aug-01-2017 2:30 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2016	0.81	0.94	▲16.05 %
FQ3 2016	0.60	0.75	▲25.00 %
FQ4 2016	0.20	0.38	▲90.00 %
FQ1 2017	0.70	0.86	▲22.86 %

Call Participants

EXECUTIVES

Dean Evans
Vice President of Investor Relations

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer

Jon W. Springer
President, Chief Risk Officer and Director

Sean P. Downes
Chairman and Chief Executive Officer

ANALYSTS

Arash Soleimani
Keefe, Bruyette, & Woods, Inc., Research Division

ATTENDEES

Unknown Attendee

Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Universal Insurance Holdings, Inc. Second Quarter 2017 Earnings Conference Call. [Operator Instructions] As a reminder, this conference is being recorded.

I would now like to introduce Vice President of Investor Relations, Mr. Dean Evans. Please go ahead, sir.

Dean Evans
Vice President of Investor Relations

Thank you. Good morning, everyone. Welcome to the Second Quarter 2017 Earnings Conference Call for Universal Insurance Holdings, Inc. My name is Dean Evans, and I'm the Vice President of Investor Relations here at Universal. With me in the room today are Chairman and Chief Executive Officer, Sean Downes; President and Chief Risk Officer, Jon Springer; and Chief Financial Officer, Frank Wilcox. Following Sean's opening remarks, Jon will provide an update on several important current topics and Frank will review financial results. The call will then be reopened for questions.

Yesterday afternoon, we issued our earnings release, which is available under the Press Releases section of our website at www.universalinsuranceholdings.com. A replay of this presentation will be available on the homepage of our website until August 16, 2017. Before we begin, please note that this presentation may contain forward-looking statements about our business and financial results. Forward-looking statements reflect our current view of future events and are typically associated with words such as believe, expect and anticipate or similar expressions. We caution those listening, including investors, not to rely solely on forward-looking statements as they imply risks and uncertainties, some of which cannot be predicted or quantified, and future results can differ materially from our expectations. We encourage you to carefully consider the risks described in our filings with the Securities and Exchange Commission, which are available on the SEC's website or the SEC Filings section of our website. We do not undertake any obligation to update or correct any forward-looking statements. With that, I'd like to turn the presentation over to our Chairman and Chief Executive Officer, Sean Downes.

Sean P. Downes
Chairman and Chief Executive Officer

Thank you, Dean. And thank you, everyone, for joining us today. As usual, I will begin by providing some highlights from the quarter and will then review our growth initiatives and strategy. Jon will cover several important current topics and Frank will conclude by discussing financial results. With that, let's turn to our results for the quarter. We are pleased to report another profitable quarter with strong top line growth. For the second quarter, we delivered a 9.2% increase in total revenues and an 8% increase in net earned premiums. We reported substantial underwriting profit despite an increased volume of severe weather events during the period, with a solid 81.3% net combined ratio for the quarter. Overall, we reported net income of $29.4 million and diluted EPS of $0.82 for the second quarter of 2017, which equates to a return on average common equity of 27.9%. During the second quarter, we have reached an important milestone for Universal. We now have more than $1 billion of in-force premium. We are very proud to have reached this milestone through considerable hard work from everyone at Universal, and believe we have positioned the company well for the future by pursuing various organic growth avenues. These include further growth in our home state of Florida, expanding our footprint into new states, strategic initiatives such as Universal Direct and new business lines such as a Commercial Residential product. These initiatives have resulted in a more stable, diversified and balanced business that is well positioned to drive growth and long-term shareholder value.

Our core Florida book continues to produce solid top line growth, with direct written premiums growing 5.6% in the second quarter versus the prior year's quarter. While we are certainly a large part of the Florida marketplace, as evidenced by our roughly 10% market share, we continue to believe that we have the opportunity to continue to profitably grow within Florida on an organic basis, given our tremendous agency network and Universal Direct. Additionally in June, we filed with the Florida OIR for an overall average rating increase across our entire Florida homeowners book of 3.4%. If approved, we expect to begin using these new rates in late September. Geographic expansion remains a key element of our growth strategy and we continue to see an increase in policy count, premiums in force, and total insured value for states outside of Florida in the second quarter, with each showing growth of more than 40% from the comparable quarter last year. During the quarter, we wrote our first homeowners policy and launched Universal Direct in New Jersey. Additionally, in June, we received approval from the New York Department of Financial Services for our homeowners rates and forms, and we anticipate writing policies in New York later this year. Universal is currently writing business in 15 states and is licensed in an additional 4 states. Universal Direct, our direct-to-consumer online platform for homeowners insurance, is now available in all of our active states and continues to demonstrate a strong growth trajectory. Since launch, we have nearly 5000 policies in force for approximately $5.5 million in premium. We continue to receive positive feedback from customers who appreciate the flexibility and convenience of purchasing homeowners insurance online. We are confident that our multipart organic growth strategy, coupled with our commitment to provide best-in-class product offerings and service to our policyholders, positions Universal for profitable growth in 2017 and beyond. With that, I will turn the call over to Jon Springer.

Jon W. Springer
President, Chief Risk Officer and Director

Thank you, Sean. I will touch on our underlying loss ratio adjustment and provide a brief update on Hurricane Matthew and also summarize our new reinsurance programs effective June 1.

As a reminder, I mentioned during the Q&A portion of last quarter's call that our original 2017 plan included 2.5 loss ratio points of expected weather losses on our Florida premium and 10 loss ratio points of expected weather losses on our Other States premium. These 2 numbers blended together produced an overall weather loss expectation of roughly 3.3 points per quarter on a direct basis. The significant rainstorm event in South Florida in early June has already produced over 800 claims. PCS 17 25, primarily in Georgia, in early April has produced over 330 claims and PCS 17 36 in Minnesota in mid-June has produced 140 claims. So we are again in a position where our quarterly weather losses exceed our plan. Primarily in light of this recent trend of weather losses exceeding our original plan, and to a lesser extent to account for our continued growth in our Other States book and the current marketplace dynamics in Florida, we have made the proactive decision to increase our underlying direct loss ratio by 1.25 points or approximately $3 million of additional losses per quarter. The current quarter includes this adjustment for our 2017 year-to-date results, reflecting an adjustment to the underlying loss ratio for both the first and second quarter of 2017 for an addition to second quarter 2017 losses of approximately $6 million or 3.6 points on a net loss and LAE ratio. In total, we are now budgeting nearly 4.5 points per quarter on a direct basis for weather losses within our underlying loss ratio expectations, or roughly $45 million for calendar year 2017, based upon our current direct earned premium projections.

As respects Hurricane Matthew, to date we have received a total of 8,816 claims and at present, only 208 claims remain open for a closure rate of nearly 98%. The total gross loss is now approaching $38 million, which resulted in a $1.1 million net prior year reserve adjustment during the second quarter. Importantly, our projection of Hurricane Matthew losses still remain within the initial range discussed on our third quarter 2016 earnings conference call and our reinsurance program is responding exactly as it was designed. Simply put, with the all-states loss now exceeding our retention, the all-states catastrophe tower is responding to limit the loss to $35 million, and in addition, the recovery from the Other States catastrophe program further reduces our pretax net retention for Matthew to $27.3 million. During the quarter, we completed our 2017/2018 reinsurance programs for both of our insurance companies and continue to build on the recent trend of adding additional conservatism to our reinsurance programs without increasing the percentage of premium spent on reinsurance. Even with UPCIC's growing business, we structured our catastrophe coverage in a similar manner and maintain the same $35 million catastrophe retention for our Florida loss and the same $5 million catastrophe retention for a loss involving states other than Florida. In addition, UPCIC also added a new contract to reduce its second, third and fourth event retention for our catastrophe loss involving states other than Florida to just $1 million and expanded the top of its reinsurance tower for a single event up to $2.65 billion. With the manner in which UPCIC purchases its catastrophe coverage, in order for the company to utilize all of the purchase limit, UPCIC would need to incur 2 events of $1.75 billion or 3 events of $1.16 billion or 4 events of $873 million. In any of these catastrophe scenarios, the company would be responsible for its retention up to a maximum of $35 million per event plus a onetime reinstatement cost not to exceed $23.3 million. To further inflate itself for future years, UPCIC has also now successfully secured over $300 million of catastrophe capacity with contractually agreed limits that extend for 2 or more years. American Platinum was also able to continue the conservatism trend by utilizing the same percentage of premium spent on reinsurance to add coverage for its new commercial lines business to all contracts and also maintain the same $2 million catastrophe retention. With that, I'll now turn the discussion over to Frank Wilcox for our financial highlights.

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer
Thank you, Jon. For the second quarter 2017, net income totaled $29.4 million, a decrease of 12.7% compared to 2016. Diluted EPS was $0.82, down from $0.94 for the second quarter of 2016, due to the decrease in net income. During the quarter, we continued to experience top line growth with increases in every major category of revenue compared to the prior year's quarter. Direct premiums earned of $244.6 million, offset by ceded premiums earned of $75.6 million, generated $169 million of net earned premiums for the second quarter of '17 compared to $156.5 million in the second quarter of '16. This was the result of organic growth from both Florida and Other State growth initiatives. Ceded premiums earned as a percentage of direct premiums earned was 31% during both the second quarter of '17 and '16. Commission revenue of $4.6 million for the quarter grew 10.3% compared to the same quarter in 2016, reflecting the differences in our reinsurance programs in effect during those periods, including an increase in our exposures covered by the reinsurance. Policy fees of $5.3 million for the quarter grew $10.5 million (sic) [10.5%] year-over-year from an increase in the number of policies written during the second quarter of '17 compared to the prior year quarter. Other revenues were $1.7 million, flat with the prior year's quarter. This line item is comprised primarily of financing fees and charges, and despite our high single top line growth in the quarter, has remained relatively flat, reflecting a shift in consumer behavior and our expansion outside of the Florida market, which tends to produce a higher level of financing fees and charges than our Other States portfolio. Net investment income for the quarter was $3.2 million, growth of 50.5% from the second quarter of 2016. This reflects actions taken to maximize yields while maintaining high credit quality as securities mature, as well as the growing size of our investment portfolio and a reduction in our investment expenses. We realized $1.7 million in gains, primarily from the sale of equity securities during the quarter, compared to $576,000 in realized gains in the second quarter of '16. We continue to maintain a high-quality investment portfolio composed primarily of fixed maturity securities, of which 98.5% are investment-grade securities, and we take a conservative approach to managing our investments. The weighted average duration of the fixed maturity investments in our available-for-sale portfolio at June 30, 2017, was 3.2 years. While the book yield of this portfolio was 1.79% for the second quarter of '17 versus 1.47% in the second quarter of '16. We generated a net combined ratio of 81.3% for the second quarter of 2017 compared to 73.4% for the second quarter of 2016. The net loss and LAE ratio was 47.4% compared to 38.4% in the prior year's quarter. As Jon discussed, the current quarter's loss ratio includes an increased expectation for weather losses for our 2017 year-to-date results, including both the first and second quarter of 2017, which resulted in an addition to second quarter 2017 losses of approximately $6 million or 3.6% on the net loss and LAE ratio. Additionally, the second quarter of 2017 included prior year reserve development of $1.1 million, 0.7 points on the loss and LAE ratio, driven by additional losses for Hurricane Matthew, while the second quarter of '16 included a negligible amount of prior year reserve development. Lastly, our underlying net loss ratio increased compared to last year's quarter as a result of continued growth in our Other States book and current marketplace dynamics. Our net expense ratio for the second quarter of 2017 was 33.9% compared to 35% for the same period in 2016. Our net acquisition cost ratio remained relatively the same at 19.5% for the quarter compared to 19.6% in 2016. Our other operating expense ratio was 14.4% in the first quarter of 2017 versus 15.4% in the prior year's quarter, reflecting a reduction in insurance, legal and consulting expenses as well as economies of scale. The effective income tax rate was 38.7% for both the second quarter of '17 and '16, which is in line with expectations. Our balance sheet continues to strengthen with stockholders equity and book value per common share of $421.1 million and $12.09 per share as of June 30, 2017, annual growth of 19.8% and 20.7%, respectively. Total unrestricted cash and invested assets were $880.4 million compared to $841.7 million as of June 30, 2016, and combined surplus for our insurance subsidiaries was $369 million as of June 30, 2017, respectively. As stated many

times, we are committed to actively managing our capital position and continued to take actions on that front in the second quarter of 2017. We repurchased 254,214 shares for $6.4 million for an average cost of $25.06 per share. We believe these repurchases represented a tremendous value in light of our current return on equity. $9 million remains on our current repurchase authorization. We declared a dividend of $0.14 per share in the second quarter, equating to an annualized dividend of 2.4% at current share price levels. Return on equity was 27.9% in the second quarter of 2017 compared to 39.6% in the second quarter of 2016. We remain dedicated to providing value to our shareholders and believe this 27.9% return on equity coupled with our 2.4% dividend yield is an excellent result. At this point, I'd like to turn the call back to the operator.

Question and Answer

Operator

[Operator Instructions] And our first question comes from the line of Arash Soleimani with KBW.

Arash Soleimani
Keefe, Bruyette, & Woods, Inc., Research Division

On the rate filing that you mentioned, I know we've seen some other carriers who ended up getting considerably more than what they asked for. Do you have that expectation as well?

Sean P. Downes
Chairman and Chief Executive Officer

We've had some dialogue with them, Arash. For me to say or give you my opinion on if they're going to ask us to take more or less, obviously, wouldn't be prudent this time. We filed for a 3.4% rate increase across the board. We believe that if this is approved, it'll be implemented at the end of September. But I wouldn't be able to give you any more color on what we think they are going to ask us to do.

Arash Soleimani
Keefe, Bruyette, & Woods, Inc., Research Division

And also, can you talk a bit about your growth within Florida, specifically, Tri County. I know a lot of your peers have been shrinking there. Just wanted to get your thoughts on why you feel comfortable growing there while others seem to be, I guess, hesitant to do so?

Jon W. Springer
President, Chief Risk Officer and Director

Sure, Arash, this is Jon. Yes, obviously, we are not going to comment on what our competitors are doing or where they find themselves, or such circumstances that they find themselves in to decide to shut down or nonrenew business. But we're committed to the state of Florida and specifically, to South Florida. As you know, the vast majority of our employees live here. We employ nearly 500 people here. We recognize that it is a challenging environment as we stand here currently, but we are still an open and active market. Our growth rate in South Florida, when represented as a percentage, really is running about the same as it was a year ago. Whether you are looking at quarter-over-quarter or half year over half year, even full year over full year, we're growing at about the same rate.

Arash Soleimani
Keefe, Bruyette, & Woods, Inc., Research Division

And another question I had was, I know Citizens has some new policy language out about using their network of approved contractors. Is that something UVE would look into me-too-ing?

Sean P. Downes
Chairman and Chief Executive Officer

Arash, this is Sean. Obviously, we me-too-ed their language as it's related to dry-outs, water extraction, et cetera. That went into effect at the end of '16, and we believe that, that has been a positive for us. As far as what they're doing now, we've looked into that actually many years ago and we don't feel that that's anything right now that's a positive for us or that would affect us in the manner which would help us lower our severity. What we're trying to do, and I think we have mentioned to you before, is continuing to try to increase all the different facets of our claims division and having a large litigation department with over 50 people in it, having our Fast Track, having our SIU divisions. All those things, I think, contribute to us being able to control our severity. And getting involved in the actual fixing, if you will, or the drying out, if you will, of an individual loss, I think, would take away our time and efforts and which we think are better served in focusing on how to build the best litigation and claims department that we can.

Arash Soleimani
Keefe, Bruyette, & Woods, Inc., Research Division

And the other question I have is just, can you provide a bit of an update on the AOB environment, and how that's looking quarter-over-quarter?

Sean P. Downes
Chairman and Chief Executive Officer

Yes. Well, I will tell you, since we did me-too the Citizens language, we are seeing a slight reduction as it relates to the EMS portion of an individual AOB claim. Our severity and frequency is relatively flat over the last few quarters. We have seen a large increase as it relates to lawsuits as a part of AOB, but that's just a position that these plaintiff's attorneys are using for a multitude of different reasons. One, we are seeing 3 and 4 different lawsuits on the same claim. And I think also prior to the legislative session that occurred, when there was some uncertainty regarding what changes would occur as it related to AOB, you saw an influx of lawsuits being filed. But again, with our large litigation firm inside handling all of our first-party claims, and for the layman, that means all claims where our insurers are suing us or they're people that they've given the representative portion of their claim to, it -- we are looking at like a 40% reduction in our loss adjustment expense as it directly relates to these claims in this litigious environment as opposed to if we were handling these claims out to an outside law firm.

Arash Soleimani
Keefe, Bruyette, & Woods, Inc., Research Division

And when you mention that you are seeing, I guess, a bit of an uptick in the number of lawsuits, does that change your expected loss ratio at all or that remains kind of stable with what you thought maybe 3 or 6 months ago?

Sean P. Downes
Chairman and Chief Executive Officer

Well, I'll tell you, like I said, there is some positive signs as it relates to the emergency water extraction. Again, these lawsuits here, a lot of these lawsuits are occurring when we agree to pay $3000 as it's mandated by the Citizens language that we me-too-ed to. Then you're seeing sometimes these are just immediately filing suit. They do not want to go through the process of mediation, et cetera, and a large reason for that is because a lot of these major players in this field have so many claims from many different carriers that they just don't have the people to handle the claims, so they find it a lot easier just to file a lawsuit. And our internal team is handling that and we feel pretty positive about it. So again, I think it's a little bit of posturing on their part, but I think there was influx of lawsuits as it related to the unknown decision-making process of the legislator, legislation that was coming out as it relates to AOB. And I believe going forward, I think you'll see that starts to trickle down somewhat as it relates to the lawsuits.

Arash Soleimani
Keefe, Bruyette, & Woods, Inc., Research Division

And my last question is, obviously, your earnings and capital looked good. In that light, can you talk about your willingness to buy back stock during wind season? And also how do you think about buybacks given the weakness in the stock year-to-date and some of the improvements in the Florida environment?

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer

Arash, this is Frank. As I mentioned in my prepared comments, we purchased over 254,000 for $6.4 million in the second quarter, which was an increase compared to the first quarter. And we recognize the prices is somewhat suppressed right now, presenting opportunities. We'll be discussing those opportunities with the board in light of the best use of our capital going forward.

Operator

And our next question comes from the line of private investor [Rob Morrison].

Unknown Attendee

I just have one quick question this morning. It looks like your reported a gross Hurricane Matthew loss of $38 million and you have a retention of $35 million. But I think you said that the net Matthew loss was $27.3 million. Can you just give me a quick explanation on how you get that?

Jon W. Springer
President, Chief Risk Officer and Director

Yes. Thanks, [Rob]. This is Jon Springer. Probably the easiest way to think about it, [Rob], is we do have a core $35 million retention for any loss involving all -- any and all of the states that we write in. We also buy what we oftentimes refer to as a supplemental program that only covers the states outside of Florida. And if that program pays, it functions to reduce our retention from $35 million down. So in the example of Hurricane Matthew, at present, we are expecting a recovery from that supplemental Other States program of $7.7 million, which serves to reduce our overall retention from $35 million down to $27.3 million.

Operator

Our next question comes from the line of [Bimal Gupta] with UVE.

Unknown Attendee

My question is regarding total number of policies that you have issued in the second quarter. Could you talk about diversification between [indiscernible] and the total quality in force as of June 30?

Sean P. Downes
Chairman and Chief Executive Officer

[Bimal], your -- the call is kind of garbled a little bit. We really didn't understand. It sounds like -- you are going in and out a little bit.

Unknown Attendee

I want to know how much is the total number of policies in force as of June 30, 2017. And what are the new policies you have written in during the second quarter? Talk about Florida and Other States, diversity.

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer

So [Bimal], this is Frank. As of the end of quarter, June 30, we had a total of over 721,000 in policies, which represented a 10% increase compared to the same time last year. Out of that, 721,596 were in Florida for about a 5.5% increase year-over-year, and 126,000 were outside of Florida for a 40% increase year-over-year.

Operator

And I'm showing no further questions. So with that, I would like to turn the call back over to Chairman and Chief Executive Officer, Sean Downes, for closing remarks.

Sean P. Downes
Chairman and Chief Executive Officer

Thank you. As always in closing, I would personally like to thank all of our shareholders, employees, Board of Directors, policyholders and my management team for their hard work and loyalty to Universal. This concludes the call. Thank you very much.

Operator
Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program, and you may all disconnect. Everyone, have a wonderful day.