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Earnings Call

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Call Participants

EXECUTIVES

Dino Ennio Robusto
Chairman & CEO

Ralitza Todorova
Vice President of Investor Relations & Rating Agencies

Scott Robert Lindquist
Executive VP & CFO

ANALYSTS

Joshua David Shanker
BofA Securities, Research Division

Unknown Analyst

Presentation

Operator

Ladies and gentlemen, good day and welcome to the CNA First Quarter 2024 Earnings Conference Call. [Operator Instructions] As a reminder, today's conference is being recorded.

At this time, I'd like to turn the call over to Ralitza Todorova, VP of Investor Relations & Rating Agencies, for opening remarks and introduction of today's speakers. Please go ahead.

Ralitza Todorova
Vice President of Investor Relations & Rating Agencies

Thank you, Jamie. Good morning, and welcome to CNA's discussion of our first quarter 2024 financial results. Our first quarter earnings press release, presentation and financial supplement were released this morning and are available on the Investor Relations section of our website, www.cna.com.

Speaking today will be Dino Robusto, Chairman and Chief Executive Officer; and Scott Lindquist, Chief Financial Officer. Following their prepared remarks, we will open the line for questions.

Today's call may include forward-looking statements and references to non-GAAP financial measures. Any forward-looking statements involve risks and uncertainties that may cause actual results to differ materially from the statements made during the call. Information concerning those risks is contained in the earnings press release and in CNA's most recent SEC filings. In addition, the forward-looking statements speak only as of today, Monday, May 6, 2024. CNA expressly disclaims any obligation to update or revise any forward-looking statements made during this call.

Regarding the non-GAAP measures, reconciliations to the most comparable GAAP measures and other information have been provided in our earnings press release, financial supplement and other filings with the SEC.

This call is being recorded and webcast. A replay of the call may be accessed on our website. If you are reading a transcript of this call, please note that the transcript may not be reviewed for accuracy, thus it may contain transcription errors that could materially alter the intent or meaning of the statements.

With that, I will turn the call over to our Chairman and CEO, Dino Robusto.

Dino Ennio Robusto
Chairman & CEO

Thank you, Ralitza, and good morning all. In the first quarter, we produced very strong results with excellent profitability, higher investment income, robust top line growth and accelerating rate achievement in our commercial casualty lines as well as strong retention in all segments.

Core income increased by $30 million in the first quarter to $355 million, our highest first quarter core income on record. The last 2 quarters have produced the largest volume of core income on record for our organization, a testament to our underwriting performance, strong investment returns and overall profitable growth. Net investment income of $609 million pretax increased $84 million year-over-year, with our alternatives portfolio and our fixed income portfolio contributing almost equally to the increased income.

The all-in combined ratio was 94.6%, with pretax catastrophe losses of $88 million or 3.8 points of the combined ratio compared to the relatively benign first quarter last year with $52 million or 2.4 points. This year was more in line with our first quarter average of 3.7 points over the last 5 years. Prior period development for P&C overall was favorable by 0.2 points on the combined ratio.

Our pretax P&C underlying underwriting gain was over $200 million for the fourth successive quarter with a P&C underlying combined ratio of 91%. This is the 13th consecutive quarter with an underlying combined ratio below 92%. The underlying loss ratio was 60.5%, and the expense ratio was 30.1% in the quarter.

The underlying loss ratio was up a little more than 0.5 point compared to the most recent 4-quarter average. This slight increase was driven mainly by a mix shift within the Commercial segment, which had greater growth in national accounts in recent quarters where the casualty lines carry a higher underlying loss ratio. The remainder is from several puts and takes, including the negative rate pressure for several quarters in management liability lines, which impacts Specialty and, to a lesser degree, International as well.

In the quarter, we continued to achieve strong production performance with 8% growth in gross written premium ex captives and 6% growth in net written premium. Renewal premium change overall was 6%, up 1 point from the fourth quarter. Rate change was up 0.5 point, but still rounds to 4%, and exposure was also up 0.5 point.

In the U.S., where there has been persistent pressure from social inflation, rate was plus 6% ex work comp; and renewal premium change was plus 8%, which continues to be above our long-run loss cost trends of 6.5% in the U.S. Outside the U.S., long-run loss cost trends in the aggregate are about 1 point lower than in the U.S. as we don't experience the same level of social inflation pressure. So our overall P&C long-run loss cost trend remains between 6% and 6.5%.

New business was up 5% in the quarter to $529 million with continued strong growth in our Commercial business units, as we achieved throughout 2023. Overall, P&C retention remained high at 85% this quarter, consistent with last quarter.

Turning to our 3 business units. The all-in combined ratio for Commercial was 97.6%. Cat losses of $82 million this quarter added 6.8 points to the combined ratio. The underlying combined ratio of 90.8% was a record low and 1 point lower than last year. The underlying underwriting gain of $111 million in Commercial was a record high.

The underlying loss ratio was 62%, and the expense ratio was 28.2%, the lowest on record. As I mentioned last quarter, the loss ratios for the post-pandemic accident years in the classes of business most impacted by social inflation, med mal, auto, GL and excess casualty, continue to hold up well as we took a conservative approach in those initial loss ratio selections.

For the remaining classes in aggregate, we have experienced favorable development from the more recent accident years based on our initial loss ratio picks. Of course, these recent years are still immature, and we will continue to monitor for any emergence over time that deviates from our initial expectations.

Gross written premium ex captives grew 17% in the quarter, and net written premium growth was 13%. New business grew 18%, and retention improved by 2 points to 85% in the quarter. Renewal premium change in Commercial was 8%, with rate up 6% and exposure increases up 2%. Rate and renewal premium change excluding work comp were 9% and 10%, respectively, continuing to exceed long-run loss cost trends.

An area we have repeatedly highlighted for you is our success at pushing for higher pricing in our U.S. commercial casualty lines. And in the first quarter, commercial auto rate increases were up 14%, excess casualty was up 11% and primary general liability was up mid-single digit with renewal premium change of high single digit due to rising revenues and payrolls. These rate increases are double what they were 6 quarters ago.

Our national accounts rate increases are down a few points compared to the fourth quarter, which is mainly a function of quarter-to-quarter variability given the impact individual large accounts can have on the overall rate change. Although still early in the second quarter, we are not seeing that lower trend continue. In work comp, overall renewal premium change is about flat in the quarter with exposure increase offsetting low to mid-single-digit rate decreases.

Within Specialty, the all-in combined ratio was 90.7% in the first quarter, including 0.6 points of favorable prior period development, making this 15 straight quarters below 91%. The underlying combined ratio was 91.3% with an underlying loss ratio of 59.2%, and the expense ratio was 31.8%.

Gross written premium ex captives growth for Specialty was down 1% this quarter, and net written premium growth was up plus 1. We capitalized on some growth opportunities in portions of our health care portfolio, but this was partially offset by our decision to remain prudent in our management liability lines until we see further improvement in the pricing environment.

Within Specialty, rates in aggregate were up plus 2% this quarter, reflecting a 2-point improvement from the fourth quarter. The rate declines in our financial institutions and management liability classes moderated this quarter, and public D&O was only slightly negative, improving in each of the last 3 quarters. Our health care rates continue to improve and are in the high single digits.

And the cumulative rate and improved terms and conditions we achieved over the hard market years is allowing us to profitably grow this business again. Our profitable Affinity Programs continue to produce stable rate change in the low- to mid-single-digit range, down slightly this quarter, which is impacted by program mix seasonality. Retention in Specialty remained very strong at 88% for the quarter, and retentions have been at or above 87% for almost 2 straight years.

For International, the all-in combined ratio was 93.3% in the quarter, including $6 million or 2 points of cat losses. The underlying combined ratio was 91.3% with an underlying loss ratio of 58.1%, and the expense ratio was 33.2%. The underlying combined ratio in International has been below 92% for 11 consecutive quarters.

International gross written premiums were down 6%, and net written premiums were down 4% in the quarter. Similar to the U.S. Specialty actions, we remained prudent in our management liability lines, which limited our new business opportunities. We also had a 2-point impact on retention from our underwriting actions to non-renew our political violence exposure, which we initiated in the fourth quarter.

Rates in International at 1% are down 1 point from the fourth quarter. Given the cumulative rate increases and extensive re-underwriting actions we took for the last several years, we expect our International operations to be an increasingly consistent contributor to our overall profitable growth.

And with that, I will turn it over to Scott.

Scott Robert Lindquist
Executive VP & CFO

Thank you, Dino, and good morning, everyone. Core income of $355 million is up 9% compared to the first quarter of last year, leading to a core return on equity of 11.5% and reflects another quarter of strong underwriting and investment results.

Our P&C expense ratio for the first quarter was 30.1% compared to 30.0% (sic) [30.7%] last year, reflecting higher net earned premium. We tend to have a certain amount of variability quarter-to-quarter in this ratio. For the balance of 2024, we expect higher spend on technology and talent as compared to the quarter just ended. Accordingly, we believe an expense ratio closer to last year's first quarter ratio of 30.7% is a reasonable run rate for the full year.

The P&C net prior period development impact on the combined ratio was 0.2 points favorable in the current quarter. Favorable development in the Specialty segment was driven by surety and was partially offset by unfavorable development in warranty.

In auto warranty, higher labor rates and car part costs are driving an increase in severity, while higher car prices and interest rates are resulting in lengthier durations of car ownership, which leads to higher frequency of warranty claims. This same dynamic is impacting claims cost in our noninsurance auto warranty business, which were up 3%, while related revenues are flat as compared to 2023 first quarter. You can see these line items in the Specialty results of operations in our financial supplement.

For Life & Group, we had core income of $5 million for the first quarter compared to a $3 million core loss for the prior year quarter, reflecting higher earnings from limited partnership investments. Active in-force management risk-mitigation activities continue, including rate filings, benefit-reduction offers and policy buyouts.

The current quarter results include a $4 million pretax loss related to $29 million of cash policy buyouts. We expect to continue offering buyouts in 2024 with the impact to earnings from such activities varying quarter-to-quarter, depending on timing and mix of buyout elections.

Our Corporate segment produced a core loss of $22 million in the first quarter compared to an $18 million loss in the first quarter of 2023. Included in the first quarter results is a $5 million after-tax charge related to ongoing office consolidation activities I previewed in our last quarter's earnings call. Looking forward and as previously mentioned, we expect additional office consolidation charges of $7 million pretax in each of the second and third quarters.

Finally, a reminder that we will be undertaking our annual ground-up review of legacy mass tort exposures during the second quarter, the results of which will be recorded in the Corporate segment.

Turning to investments. Total pretax net investment income was $609 million in the first quarter compared to $525 million in the prior year quarter. The increase was driven almost equally by our fixed income and other investments as well as our limited partnership and common stock portfolios. Limited partnerships and common stocks returned a $68 million gain or a 2.9% return in the current quarter compared to a $28 million gain or a 1.3% return in the prior year quarter.

Fixed income and other investments generated $541 million of income, up 9% compared to the prior year quarter. Our fixed income portfolio continues to produce consistent income, which has been increasing as a result of favorable reinvestment rates and strong cash flows from operations. The effective income yield of our consolidated portfolio was 4.7% in the first quarter compared to 4.6% in the prior year quarter.

As of the end of the first quarter, reinvestment rates continue to be well above our P&C effective income yield of 4.3% and modestly above our Life & Group portfolio effective income yield of 5.6%. A reminder that the Life & Group portfolio is a longer-duration portfolio with embedded yields more comparable to today's interest rate environment.

Looking ahead, we currently expect income from fixed income and other investments to be about $540 million in the second quarter, which will be a 7% increase from the second quarter of 2023. And for the full year 2024, we currently expect about $2.175 billion or a 5% increase as compared to the full year 2023, which would result in the total portfolio effective yield to approach 4.8% by the end of 2024.

At quarter-end, our balance sheet continues to be very solid with stockholders' equity excluding AOCI of $12.2 billion or $45.10 per share, an increase of 2% from year-end 2023 adjusting for dividends. Stockholders' equity including AOCI was $9.7 billion or $35.62 per share. As a result of rising interest rates during the quarter, the net unrealized loss in our fixed income portfolio is now at $2.3 billion as of quarter-end.

Finally, we ended the quarter with statutory capital and surplus in the Combined Continental Casualty Companies of $10.9 billion, which is flat with year-end 2023. Operating cash flow was strong once again at $504 million for the quarter despite $29 million in long-term care cash policy buyouts during the quarter, reflecting both strong underwriting results and higher earnings from our fixed income portfolio.

Turning to taxes. The effective tax rate on core income for the first quarter was 20.9%, which is in line with our full year 2024 expectations. Finally, we are pleased to announce our regular quarterly dividend of $0.44 per share to be paid on June 6, 2024, to shareholders of record on May 20, 2024.

With that, I will turn it back to Dino.

Dino Ennio Robusto
Chairman & CEO

Thanks, Scott. CNA is off to an excellent start in 2024 with strong levels of core income driven by substantial net investment income and strong underwriting performance. We achieved high single-digit growth in gross written premium ex captives, and our retention remains very strong at 85%. The market remains rational in most classes of business with rates reflective of the individual dynamics impacting the various lines of business.

In the commercial casualty classes in the U.S., rates continue to improve. And then property rates, although off from their high watermark in 2023, continue to offer great new business opportunities. And so we remain optimistic about our ability to successfully navigate the favorable market dynamics and continue to grow the company profitably as well as build our investment returns.
With that, we will be happy to take your questions.

Question and Answer

Operator

[Operator Instructions] And our first question today comes from Josh Shanker from Bank of America.

Joshua David Shanker
BofA Securities, Research Division

If I can go back in a time machine 20 years ago, 2004, there might have been some conservatism on the margins, but you probably should have just written every single piece of business that was out there. It was that good of a market. And things are more mixed today. Are they more mixed or less mixed than they were, let's say, in 2021? How good of a market is it out there? I know -- and that maybe things have gotten so granular and sophistication has gotten to a point that there will never be a universally hard market. But -- and indulge me for a second, some competitors didn't grow it all this quarter and some did, and it leaves a -- how good is that market that's out there right now?

Dino Ennio Robusto
Chairman & CEO

Josh, it's Dino. We agree with you that the market is favorable, and we continue to take advantage of it. But you also highlighted that it's a nuanced, almost a mini-cycle approach. And that is indeed the issue and very, very different than prior cycles, without a doubt. And so we navigate each one accordingly.

On casualty, we continue to get very strong rate increases, and I expect they will continue. And that will continue to give us good opportunities as we saw in national accounts, also casualty as well as middle market. On property, when you think about all of the cumulative rate, you think about the valuation changes, the terms and conditions, see favorable opportunities there.

Management liability, notwithstanding that we still have a cumulative 50% to maybe 60% of rate increase since the start of the hard market, the reality is some of the competition, in particular from new entrants, as it has been expressed by others also, is too aggressive. And so we are fine to wait on the sidelines and pursue those areas so we can still have a good growth rate as we do, whether that be it in surety, be it in health care on the Specialty side or, as I just talked about, in the Commercial.

So I think it gets down to your point of a very nuanced mini-cycle market, and you have to act accordingly. But overall, I'd consider it a favorable market, and it's going to continue in '24.

Joshua David Shanker
BofA Securities, Research Division

And is it -- do you have the ability to capture as much business as you want where you want it? Or if your appetite increased, would that affect price?

Dino Ennio Robusto
Chairman & CEO

So what I would say is, Josh, over the years, in particular the last 6, 7 years, we've talked extensively about our migration from a generalist commercial underwriter to a specialist underwriter. And we focus on those specialties and we penetrate them quite successfully.

But as I've indicated before, our market share in a lot of those areas remains relatively small. So there is plenty of opportunity, and we're going to continue to go after it. It is one of the reasons, as Scott indicated, you're going to see additional investments, technology, talent. And then we're going to divert that to continue to penetrate our specialties. So we see plenty of opportunity.

Joshua David Shanker
BofA Securities, Research Division

And in terms of, Scott, you mentioned a warning -- or not a warning, as [that evolved more] completely, but just a guidance that we should expect that as usual, in 2Q, we're going to see the legacy mass torts review. Is that asbestos and environmental? Or are there other mass torts that get reviewed in 2Q?

Scott Robert Lindquist
Executive VP & CFO

So yes, thanks, Josh. It's Scott here. So if you take a look at historically, it's been kind of general mass tort. A couple of years ago, archdiocese cases, abuse cases over the past few years. I hate to predict what's going to happen this quarter. The team is still doing the work on that. But I would just kind of take a look at the history over the past few years and what we've done in the second quarter. And we've done some refreshes in the fourth quarter, too, the past couple of years. But that's probably all I'd say at this point.

Joshua David Shanker
BofA Securities, Research Division

And one mass tort that gets a lot of press, but there's not a lot of detail on or a lot of news per se, certainly, is PFAS. Is there anything that you can tell us about your thoughts on how you think about it?

Scott Robert Lindquist
Executive VP & CFO

Yes -- oh, go ahead.

Dino Ennio Robusto
Chairman & CEO

No, no, go ahead.

Scott Robert Lindquist
Executive VP & CFO

No, I was going to say, I mean I have no specific comments on that other than what we see out there is in our reserves right now. And I have nothing else really to say on that.

Dino Ennio Robusto
Chairman & CEO

Totally agree with Scott. It's early and limited information. What we have, as Scott points out, is in the reserves.

Operator

[Operator Instructions] Our next question comes from Meyer Shields from KBW.

Unknown Analyst

This is [Jane] on for Meyer. I just had a question on reserves. Do you see any changes in patterns within reserves for recent years for casualty lines? Can you please share some like view on that, please?

Dino Ennio Robusto
Chairman & CEO

It's Dino. We've been highly transparent over the last several years, and we have outlined in considerable detail all the actions we have done to strengthen our reserves, in particular, in the block of 2015 to 2019. And the biggest trend that we commented on and is still significant, albeit maybe more expected than a few years back, was social inflation, which really put severity pressure on our loss cost trends and in quite a few casualty classes actually doubling them over the last 5 years. So that's the main essence of what we've seen.

Unknown Analyst

Got it. My second question is on the International operations, you mentioned expecting contributing to overall profitability. Just curious your strategy there, can you please add more color on that?

Dino Ennio Robusto
Chairman & CEO

So on the International, we also, over the years, have described all of the underwriting actions that we have taken, in particular, relative to our syndicate to reduce the catastrophe exposure. It has been profitable for quite a few quarters now. As we've indicated, we had some pressure on growth in the first quarter for the reasons that I also indicated in my prepared remarks, being that of being prudent on management liability and a decision to remove from political violence.

But going forward, we expect it to continue to contribute profitable growth to the organization. We feel very, very good about our International operations, in particular, when you consider that on some segments, the starting point is very good even before the hard market segments like middle market in the U.K. and Canada, we're already very profitable. We got additional cumulative rate. We added improved terms and conditions. So as you can tell, we are quite bullish on our International operation going forward.

Operator

And ladies and gentlemen, that will now conclude today's question-and-answer session. I'd like to turn the floor back over to Dino Robusto for closing remarks.

Dino Ennio Robusto
Chairman & CEO

Thanks very much. I do have some this time around.

In closing, I'd like to give an update as to future earnings calls for CNA. In light of reduced analyst participation in recent years, in future quarters, we will simply post the transcript in place of hosting a live call. The transcript we post will continue to include the level of detail you are accustomed to hearing in our earnings call remarks. The transcript will also incorporate select Q&As that are intended to address timely and topical focus areas for CNA and our industry as well as answers to questions -- and we will answer questions that are submitted to us in advance.

We are, of course, committed to remaining as transparent as we have always been. And as always, if you ever need any further clarification, we encourage you to reach out to our Investor Relations team.

Finally, we look forward to attending industry investor conferences in the future as we have done in the past, and we look forward to continuing the dialogue with the investor and analyst community. And thank you all for joining us today.

Operator
Ladies and gentlemen, with that, we'll conclude today's conference call and presentation. We thank you for joining. You may now disconnect your lines.