S&P Capital IQ

CONTENTS

Universal Insurance Holdings, Inc. NYSE:UVE

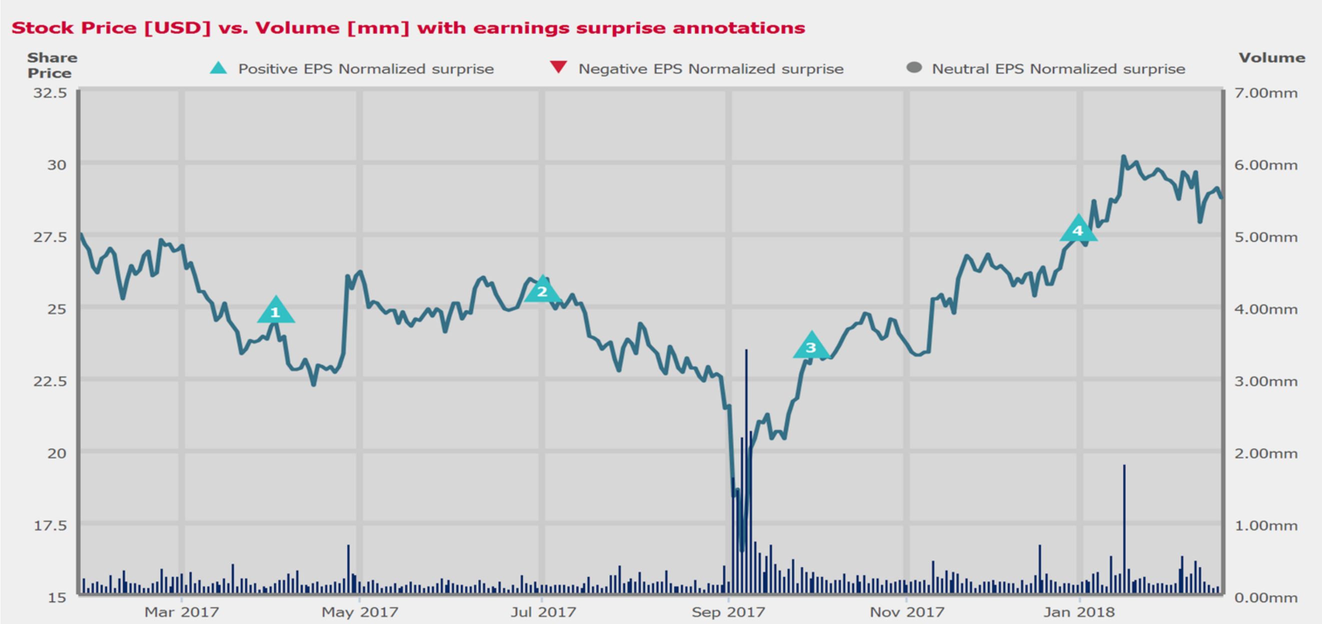
FQ1 2018 Earnings Call Transcripts

Wednesday, April 25, 2018 2:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2018-			-FQ2 2018-	-FY 2018-	-FY 2019-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.87	1.12	▲28.74	1.03	3.69	4.15
Revenue (mm)	-	-	-	-	-	875.14

Currency: USD
Consensus as of Apr-25-2018 7:45 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2017	0.70	0.86	▲22.86 %
FQ2 2017	0.73	0.82	▲12.33 %
FQ3 2017	0.23	0.28	▲21.74 %
FQ4 2017	0.80	1.16	▲45.00 %

Call Participants

EXECUTIVES

Dean Evans
Vice President of Investor Relations

Frank Crawford Wilcox
CFO & Principal Accounting Officer

Jon William Springer
President, Chief Risk Officer & Director

Sean Patrick Downes
Chairman of the Board & Chief Executive Officer

ANALYSTS

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

Samir Khare
Capital Returns Management, LLC

Presentation

Operator

Good day, ladies and gentlemen, and welcome to the UVE First Quarter 2018 Earnings Conference Call. [Operator Instructions] As a reminder, today's conference is being recorded. I would like to introduce your host for today's conference, Mr. Dean Evans, VP of Investor Relations. Sir, please go ahead.

Dean Evans
Vice President of Investor Relations

Thank you, Michelle, and good morning, everyone. Welcome to the First Quarter 2018 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 release's section of our website at www.universalinsuranceholdings.com. A replay of this presentation will be available on the homepage of our website until May 9, 2018.

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, 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 Patrick Downes
Chairman of the Board & Chief Executive Officer

Thank you, Dean, and thank you, everyone, for joining us today. As usual, I'll begin by providing some highlights from the quarter and we'll then review our growth initiatives and strategy. Jon will cover several important current topics and Frank will conclude by discussing financial results.

We are pleased with our results for the first quarter. Overall, reported net income of $40.1 million and diluted EPS of $1.12 for the first quarter of 2018, which equates to an annualized ROE of 34.6% for the quarter. We reported excellent top line growth in the first quarter, with 10% growth in direct premiums written, including 7.2% growth within Florida and 32.7% growth in other states.

Our underwriting profitability was strong with a 76.5% combined ratio for the quarter. The current year's quarter includes no weather losses beyond plan and a negligible reserve change, and we highlight this because we have taken a conservative approach to our underlying loss pick in light of the increased level of catastrophic activity in recent years, coupled with the impact from current market conditions in Florida, most notably related to the assignment of [indiscernible] claims.

Our service company subsidiaries continue to produce benefits in the aftermath of Hurricane Irma, as both Universal Adjusting Corporation and Blue Atlantic Reinsurance Corporation contributed positively to the first quarter results.

Lastly, as Frank will discuss in more detail later in the call, our effective tax rate for the quarter benefited from the federal tax reform that was passed in late 2017, which had a meaningful positive impact on our net income for the quarter. I'd like to briefly discuss our growth outlook heading forward. We believe we have positioned Universal well for the future by pursuing various organic growth avenues, which have resulted in a more stable, diversified and balanced business. Our core Florida book continues to produce strong organic growth and we continue to believe that we can profitably grow on an organic basis in Florida, using both our robust agency network and our direct-to-consumer platform, Universal Direct. Our 3.4% average statewide rate increase was approved by the Florida OIR in early December and the new rates were effective for new business on December 7 and for renewals on January 26, and our retention ratio of these impacted policies has continued to run over 90% during the first quarter.

Geographic expansion remains a key element of our growth strategy. In direct premiums written within our Other States book grew a strong 32.7% in the first quarter. We now actively write business in 17 states after writing our first policy in New Hampshire in early April. And we have licenses in additional 3 states: Illinois, Iowa and West Virginia.

Universal Direct, our unique direct-to-consumer online homeowners insurance platform, is available in all of our active states and continues to demonstrate solid growth trajectory. Currently, we have approximately 8,700 policies in force for more than $10 million of in-force premium. We are off to a strong start in 2018 and continue to believe that Universal is extremely well positioned going forward.

We remain confident that our multipart organic growth strategy will enable us to deliver profitable premium growth in both Florida and the 16 other states where we write business. We have a solid balance sheet with a conservative investment portfolio, minimal debt and an appropriately set loss reserve position. And we are protected by a comprehensive reinsurance program. And our unique vertically integrated structure positions us well to capitalize in the event of a disruptive industry catastrophe, as was highlighted by our performance during Hurricane Irma.

Given these strengths, we are excited about what the future holds for Universal, and we expect to continue to deliver substantial value to our shareholders.

With that, I will turn the call over to Jon Springer.

Jon William Springer
President, Chief Risk Officer & Director

Thank you, Sean. I would like to first start with an update on Hurricane Irma and then discuss the current reinsurance environment as we are soon approaching our June 1 renewals.

By way of background, on October 10, roughly one month after landfall, we released a public estimate of $350 million to $450 million in gross losses from Hurricane Irma. We are now 7.5 months removed from when the storm first made landfall in Florida, and our information on the event continues to evolve on a daily basis. More importantly, as we advised previously, given our reinsurance tower extends to $2.8 billion per UPCIC, Hurricane Irma is a retention event. As we advised last quarter, the manner in which our reinsurance program responded reduced UPCIC's retention for this event to $27.2 million. None of that has changed. However, at this time, following a comprehensive review of the event over the past few weeks, we are advising that we are prospectively increasing our estimate of gross losses relating to Hurricane Irma by $50 million. Again to confirm, this change in gross loss estimate will have absolutely no impact on the financials of UPCIC. Our comprehensive reinsurance program performed as it was designed and will continue to limit total net loss and LAE from Hurricane Irma to the $27.2 million for UPCIC and the $2 million for APPCIC, which is below the combined retention of $37 million for both of our insurance subsidiaries due to additional recoveries received from our UPCIC Other States reinsurance program. This change in gross loss estimate comes primarily due to the continuation of reported claims. We had 10,173 new claims reported during the first quarter of 2018 and an additional 2,300 in the first 3 weeks of April, bringing our total claim count to date to 76,283. We have closed 68,487, roughly 90% of these claims, with an average loss and LAE severity across all claims of approximately 5,200 and an average loss and LAE severity of just over 7,500 on claims closed with payment.

We can also report that the percentage of claims reopening with a resulting change in incurred loss is running just 14.5%. I believe this compares to the 35-plus-percent number announced previously by

Citizens. All of this is a testament to the hard work of our employees, many of whom have been working long hours since the storm made landfall in early September.

As a result of Hurricane Irma, both the fourth quarter of 2017 and the first quarter of 2018 included the benefit of additional revenues within our service provider subsidiaries, which led to a higher level of profitability than would otherwise be the case in a normal quarter. Blue Atlantic Reinsurance Corporation received $600,000 of reinstatement commissions during the first quarter of 2018, and Universal Adjusting Corporation produced $10.4 million of pretax profit during the first quarter of 2018, the vast majority of which was related to additional revenues created due to the continued increased workload as a result of Hurricane Irma.

Switching now to reinsurance. Over the course of the past 2 months, we've met face-to-face with the vast majority of our reinsurance partners to discuss our experiences in Hurricane Irma and the upcoming June 1 renewals. I think the most important takeaway is the reinsurers desire to truly differentiate the insurance companies that operate in Florida. As Hurricane Irma continues to evolve, it has become more evident to reinsurers that companies that had made a quality investment in their claims option and those who had not. It is very difficult to catch up post event, so any lack of preparation will continue to manifest itself in higher severity numbers and a greater percentage of reopened claims.

As we have stated many times since Irma made landfall, we are very pleased with our reinsurance program design and the response of our professional reinsurance partners. Without a doubt, Hurricane Irma was a devastating event for many. But from a professional reinsurer perspective, it was exactly the type of event that is modeled for, priced accordingly and expected to occur.

From a reinsurance renewal perspective, when you take into account our previously discussed multiyear capacity and the coverage we purchased from the state-run FHCF, we have just 32% of our total reinsurance premium budget up for renewal this June 1. After receiving and evaluating quotes from our lead reinsurers, we entered the market with firm order terms last week on the core All States catastrophe tower for UPCIC. At this point in the process, I'm not going to comment on specific pricing levels, but I will say that when you factor in all of the variables, including the rate change that Sean mentioned, the 2018 renewal is shaping up to be a year where we'll be keeping our catastrophe retention at the same level, buying catastrophe coverage to a higher level and spending the same or less as a percent of earned premium to do so. With that, I'll turn the discussion over to Frank Wilcox for our financial highlights.

Frank Crawford Wilcox
CFO & Principal Accounting Officer

Thank you, Jon. For the first quarter of 2018, net income totaled $40.1 million, an increase of 28.4% compared to the first quarter of '17. Diluted EPS was $1.12, up from $0.86 for the first quarter of 2017.

We reported strong total revenue growth of 9.5% in the quarter, driven by growth in premium volume, the statewide rate increase of 3.4% in Florida, net investment income, commission revenue, policy fees and other revenue. Direct premiums earned grew 11% to $262.3 million, offset by ceded premiums earned of $79.7 million, leading to growth in net earned premiums of 13% to $182.6 million. Ceded premiums earned, as a percent of direct premiums earned, was 30.4% during the first quarter of 2018 compared to 31.7% in the first quarter of '17.

Commission revenue, policy fees and other revenue each posted solid growth versus the prior year's quarter. Included within commission revenue was $600,000 of fee income related to the reinstatement commissions received by Blue Atlantic during the first quarter of 2018.

We generated a net combined ratio of 76.5% in the first quarter of '18 compared to 78.9% in the first quarter of '17. The net loss in LAE ratio improved to 41.6% from 43.7% in the prior year's quarter. First quarter of 2018 included no impact from weather events above plan compared to $3 million or 1.9 percentage points of weather losses above plan in the first quarter of 2017. Prior accident year reserve movements were negligible in both the current and prior year's quarters.

The first quarter '18 loss adjustment expenses included the benefit of $10.4 million or 5.7 percentage points from additional revenues earned by Universal Adjusting Corporation related to Hurricane Irma.

Our underlying loss in LAE ratio increased compared to the prior year, reflecting continued geographic expansion as non-catastrophe loss ratios in Other States booked are generally higher than in Florida; an increased level of projected weather losses; and the marketplace dynamics within our home state of Florida, including the impact of AOB-related claims.

Our net expense ratio was 34.9% in the first quarter of '18 compared to 35.2% in the first quarter of '17.

Our net policy acquisition cost ratio increased to 20.8% compared to 20.1% in the prior year's quarter, with the increase largely driven by geographic expansion as our Other States book typically has a higher commission expense than within Florida.

Our other operating expense ratio was 14.1% in the first quarter of '18 versus 15.1% in the prior year's quarter, which generally reflects the benefits of economies of scale.

Net investment income was $4.8 million, growth of 77% from the first quarter of '17. The increase is the result of higher returns from our available-for-sale of debt securities, driven by growth in total invested assets, favorable market trends and actions taken to increase yield while maintaining high credit quality, as well as higher return from cash and cash equivalents due to actions taken to optimize treasury management, coupled with an increase in interest rates.

We reported $2.6 million of realized investment losses during the quarter compared to $63,000 of realized investment losses in the first quarter of '17. We reported $5.1 million of unrealized investment losses during the first quarter of '18, driven by a decline in our equity securities portfolio. Notably, this line item was added in the first quarter of '18 as a result of the adoption of accounting guidance for equity securities. The comparable number from our equity portfolio for the first quarter of '17 was $1.7 million of pretax gains, which was not included in net income in the prior period, but was included in other comprehensive income on an after-tax basis.

Total unrestricted cash and invested assets were $974.4 million as of March 31, 2018, growth of 17.9% from March 31 of '17. We take a conservative approach to managing our investments and maintain a high-quality investment portfolio comprised primarily of fixed maturity securities, which are 99% investment grade. The weighted average duration of the fixed maturity investments in our available-for-sale portfolio as of March 31, 2018 was 2.5 years.

The effective tax rate for the first quarter of '18 was 22.5% compared to 34.1% in the prior year's quarter. The decrease in our effective tax rate is primarily the result of the enactment of the Tax Cut and Jobs Act of 2017 which resulted in a reduction in the federal corporate tax rate from 35% to 21%, effective January 1, 2018. The current year's quarter included a credit to income tax expense of $1.8 million for excess tax benefits resulting from stock-based awards that vested and/or were exercised during the first quarter, benefiting the quarter's -- the current quarter's effective tax rate by 3.5 percentage points. The prior year's quarter included $2.1 million of credits to income tax expense related to discrete items, benefiting that quarter's effective tax rate by 4.4 percentage points.

We remain committed to actively managing our capital position. During the first quarter of 2018, we repurchased 92,749 shares for $2.7 million, an average cost of $29.61 per share. Our current share repurchase authorization program has $17 million remaining and runs through December 31, 2018.

We paid a regular quarterly dividend in the first quarter of '18 of $0.14 per share, which equates to an annualized dividend yield of 1.7% based on current share price levels.

Stockholders equity was $465.1 million at March 31, 2018, growth of 5.7% from year end 2017, while book value per common share was $13.28 as of March 31, 2018, growth of 4.8% from December 31, 2017, or 16.8% from the end of the first quarter in 2017.

Combined surplus for our insurance subsidiaries was $338 million at March 31, 2018 compared to $324 million at December 31, 2017.
Annualized return on average common equity was 34.6% for the first quarter of 2018, compared to 31.4% in the prior year's quarter. We remain dedicated to providing value to our shareholders and believe this level of return on equity is an excellent result. At this point, I'd like to turn the call back to the operator.

Question and Answer

Operator

[Operator Instructions] Our first question comes from Arash Soleimani with KBW.

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

Just -- first question was in terms of the growth, it's been pretty strong in the premium growth. Is this kind of like 10% level sustainable? Or should we think of it as more kind of mid, upper, mid-single digits?

Sean Patrick Downes
Chairman of the Board & Chief Executive Officer

Good morning, Arash, this is Sean. Because of our geographic expansion and our loyal agency force that continues to expand and Universal Direct, I think you should look at as a bracket basically of between 7% and 10% going forward that is definitely attainable.

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

Okay. And with -- is commercial residential something you're kind of keeping an eye on, but not really focusing on growing in the near term because of the rate environment there?

Sean Patrick Downes
Chairman of the Board & Chief Executive Officer

Exactly. I mean, we're definitely putting some business on. But the current rate environment we just don't believe is adequate at this time, and we're not in the business of chasing premium. But we are set and ready to go in case there is a disruption in the marketplace. But at this time I just don't think the environment is adequate enough for us to be putting on business.

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

Okay. I don't know if Jon had mentioned this, but what are you seeing -- I know there are only certain layers that you have that are coming up for renewal. The others are on a multi-year basis. But what's the -- I guess pricing environment for layers that were actually hit by losses?

Jon William Springer
President, Chief Risk Officer & Director

Yes. As I mentioned, Arash, in my opening remarks, given that we are literally right in the middle of the process, I don't think it's appropriate for us to comment on specific layers, pricing, that sort of thing. I made a general comment relative to where our overall reinsurance spend will end up relative to last year. But we're not going to talk about specific layers.

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

Okay, that's fair. And then in terms of subrogation, would you say you reached a point with subrogation where you're, sort of, I guess, like a fair run rate going forward? Or do you think there's still kind of improvement to be had in that -- in your subrogation operation?

Frank Crawford Wilcox
CFO & Principal Accounting Officer

Subrogation unit continues to improve because of the hard work of our employees and the material investments we have made over the last 3 or 4 years in that space. I think it's a little too early to determine basically what the critical mass level is and where we'd be bottoming out at as far as picking a percentage. We are continuing to improve going forward and I believe that will continue specifically over the next year, a year to 2.

Operator

And our next question comes from the line of Samir Khare with Capital Returns.

Samir Khare
Capital Returns Management, LLC

Just a few quick questions about Universal Direct. What was the premium volume that you guys actually wrote this quarter? And what was the amount of premium you guys wrote in Q4 as well?

Frank Crawford Wilcox
CFO & Principal Accounting Officer

I believe it's approximately $2 million in Q1 and a little bit under that in Q4 off the top of my head, Samir.

Samir Khare
Capital Returns Management, LLC

And then recognizing that there was a benefit in this quarter on the tax rate. What's the good tax rate to use going forward?

Frank Crawford Wilcox
CFO & Principal Accounting Officer

Samir, this is Frank. Good morning. Excluding discrete items, I'd put a range on the effective -- the underlying effective tax rate between 25% to 27%.

Samir Khare
Capital Returns Management, LLC

All right. And then any anticipation of more, I guess income from adjusting Irma claims, coming in Q2?

Sean Patrick Downes
Chairman of the Board & Chief Executive Officer

There will be some, but not as great as Q1. Obviously, we're seeing a reduction in the claims that we're receiving currently right now, so I wouldn't expect anything, such as what we put up in Q1.

Samir Khare
Capital Returns Management, LLC

And the claims you said were coming in, in Q1 and Q2, is there any reason you think that these claims came in much later? I'm just trying to better understand if there's a different complexion to them, say higher severity, they're more complex, or if there is higher turn involvement versus noticeable bluff?

Sean Patrick Downes
Chairman of the Board & Chief Executive Officer

Well, first and foremost, obviously there's a lot of transient folks in Florida that have 2 different dwellings that live up north, et cetera. So sometimes you get situation where folks come down, realize they've had a loss and turn it in and that causes a delay. Also some of the AOB situation has to deal with it where an individual insured would have had their claim handled and it would have been below deductible and because of some certain situations that, be it public adjusters, or attorneys, et cetera, have been marketing, people then sign up with these folks and the claim would reopen. Our reopen rate is running significantly lower than everybody else, approximately right around 14%. So I couldn't really give you a definitive answer, but I think it's a blending of those 2 situations.

Samir Khare

Capital Returns Management, LLC

Okay. And that 14% number that you just quoted, is that -- does that include re-open claims for what we'll call supplemental payments? Or just is that kind of more the traditional reopen claims because of adjusters and whatnot?

Sean Patrick Downes
Chairman of the Board & Chief Executive Officer

I didn't hear what you said. I heard you say reopen but then you went a little bit radio silent on me there.

Samir Khare
Capital Returns Management, LLC

Sorry I'm wondering what that 14% metric is that -- does that include claims that are reopen for supplemental payments?

Sean Patrick Downes
Chairman of the Board & Chief Executive Officer

Yes.

Samir Khare
Capital Returns Management, LLC

Okay.

Sean Patrick Downes
Chairman of the Board & Chief Executive Officer

In other words it could be recoverable depreciation, anything at all that's a supplement, all that goes into that same bracket.

Samir Khare
Capital Returns Management, LLC

Okay. And then any update on the -- I think the number that you gave the last quarter was 12% of claims you expect to result in AOB from -- in the losses. Any update to that number?

Sean Patrick Downes
Chairman of the Board & Chief Executive Officer

No. It's running about the same rate.

Samir Khare
Capital Returns Management, LLC

Okay. And then I think Jon said that the gross Irma losses, you expect to increase that by $50 million. Should I think of that -- the whole range increasing by $50 million? Or is it on top of the range of -- going from $450 million to $500 million?

Jon William Springer
President, Chief Risk Officer & Director

You should think of it as on top of the $450 million. So $500 million is the new number going forward.

Samir Khare
Capital Returns Management, LLC

Got it. And can you give me the split of the Irma gross losses, HO-3 versus HO 6, what's the paid severity for each?

Sean Patrick Downes
Chairman of the Board & Chief Executive Officer

Well, right now I can tell you that 25% of the losses are a little bit under HO 6. And the HO 6 severity is running right around 4,200. And the H all other, let's just call it is running around 7,200.

Operator

And I'm showing no further questions at this time and I would like to turn the conference back over to Sean Downes for any further remarks.

Sean Patrick Downes
Chairman of the Board & 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.

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 great day.