S&P Global
Market Intelligence

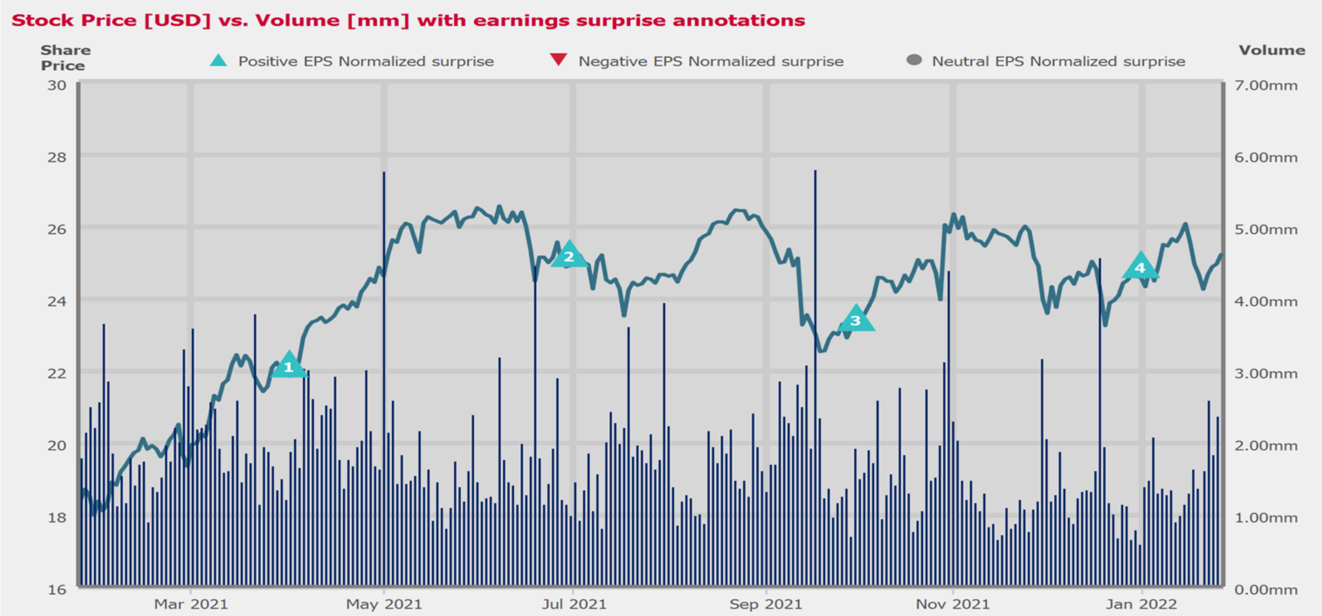
Old Republic International Corporation
NYSE:ORI
FQ4 2021 Earnings Call Transcripts

Thursday, January 27, 2022 8:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2021-			-FQ1 2022-	-FY 2021-			-FY 2022-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS
EPS Normalized	0.74	0.88	▲18.92	0.66	2.94	3.08	▲4.76	2.65
Revenue (mm)	2186.00	2720.50	▲24.45	2060.00	8806.00	9341.60	▲6.08	8578.00

Currency: USD
Consensus as of Jan-28-2022 1:32 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2021	0.45	0.69	▲53.33 %
FQ2 2021	0.52	0.73	▲40.38 %
FQ3 2021	0.63	0.79	▲25.40 %
FQ4 2021	0.74	0.88	▲18.92 %

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Call Participants

EXECUTIVES

Carolyn Jean Monroe
President

Craig Richard Smiddy
President, CEO & Director

Francis Joseph Sodaro
Senior VP, CFO & Chief Accounting Officer

ANALYSTS

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Matthew John Carletti
JMP Securities LLC, Research Division

ATTENDEES

Joe Calabrese

Presentation

Operator

Good afternoon. My name is David, and I will be your conference operator today. At this time, I'd like to welcome everyone to the Old Republic International Fourth Quarter 2021 Earnings Conference Call. Today's conference is being recorded. [Operator Instructions] Joe Calabrese with the Financial Relations Board, you may begin your conference.

Joe Calabrese

Thank you. Good afternoon, everyone, and thank you for joining us for the Old Republic conference call to discuss fourth quarter 2021 results. This morning, we distributed a copy of the press release and posted a separate statistical supplement, which we assume you have seen and/or otherwise have access to during the call. Both of the documents are available at Old Republic's website, which is www.oldrepublic.com.

Please be advised this call may involve forward-looking statements as discussed in the press release and fiscal supplements dated January 27, 2022. Risks associated with these statements can be found in the company's latest SEC filings.

This afternoon's conference call will be led by Craig Smiddy, President and CEO of Old Republic International Corporation, and several other senior executive members as planned for this meeting.

At this time, I would like to turn the call over to Craig Smiddy. Please go ahead, sir.

Craig Richard Smiddy
President, CEO & Director

Thank you, Joe. Good afternoon and best wishes to everyone in this new year. Welcome again to Old Republic's fourth quarter earnings call. With me today are Frank Sodaro, CFO; and Carolyn Monroe, President of our Title Insurance business.

Well, we're very pleased to report that ORI produced another terrific quarter, as well as a third consecutive record-setting year. Both our major segments, General Insurance and Title Insurance posted outstanding results. Net premiums and fees earned increased to $2 billion for the quarter and $8 billion for the year. That's up 19% over the prior year. At the same time, pretax operating income increased to $335 million for the quarter and $1.2 billion for the year, eclipsing the $1 billion mark for the first time and up over 40% over the prior year.

The consolidated combined ratio improved to 88% for the quarter and 89.9% for the year, a 3.4 point improvement over the prior year.

General Insurance net premiums earned increased by 5% over the prior year, and title net premiums and fees earned increased by 34% over the prior year.

So we think it's clear that our diverse portfolio of specialty products in both General Insurance and Title Insurance continue to deliver strong growth and exceptional profitability as demonstrated by these results.

So I'll now turn the discussion over to Frank, and then Frank will turn things back to me to cover General Insurance, followed by Carolyn, who will discuss our Title Insurance business, and then we'll open up the conversation to Q&A. So Frank?

Francis Joseph Sodaro
Senior VP, CFO & Chief Accounting Officer

Thank you, Craig, and good afternoon, everyone. This morning, we reported fourth quarter net income, excluding investment gains and losses, of $268 million, a 20% year-over-year increase. For the full year, this figure was $935 million, up 40%.

On a per share basis, comparable year-over-year numbers were $0.88 versus $0.75 for the quarter, and $3.08 versus $2.24 for the full year. Improved results in the year were driven by substantial growth in underwriting profitability in the General Insurance and Title Insurance segments. And you're going to hear more about that a little later.

Shareholders' equity ended at nearly $6.9 billion, resulting in book value per share of $22.76. When adding back dividends, book value increased just over 21% from the prior year-end, driven by our strong operating earnings and higher investment valuations.

Net investment income was relatively flat for the quarter and year as an increase in the level of investments and lower yields on new investment purchases affected both periods. The investment portfolio was comprised of approximately 68% in highly rated bonds and short-term investments, with the remaining 32% allocated to large cap dividend paying stocks. The average maturity on the bond portfolio is 4.4 years with both book and market yields of just over 2.4%. The fair value of the equity portfolio increased by $460 million during the quarter and $750 million for the year.

I'll now turn to claim reserve development. All 3 operating segments recognized favorable claim reserve development for all periods presented. In total, the consolidated claim ratio benefited by 4.6 and 2.7 percentage points for the quarter and year, respectively, compared to 2.3 and 1.2 percentage points for the same periods a year ago.

Shifting to our runoff mortgage operations. Premiums and risk in force continued to decline in line with our expectations. Claims costs this year reflect a significant reduction in newly reported defaults and higher cure rates on loans already in default in addition to lower claims severity resulting from increasing home values. The group paid another $25 million dividend to the parent, bringing the total to $100 million for the year. Subject to regulatory approval, we expect 2022 dividend at or above this level.

Total GAAP shareholders' equity for the mortgage companies ended the year at $360 million.

So to wrap up my remarks, this quarter capped a year of outstanding financial performance. We paid an annual dividend for the 80th straight year and have increased our dividend in each of the last 40 years. We paid a special dividend of $1.50. And over the last 5 years, we've returned $2.5 billion to shareholders.

Our balance sheet is in excellent shape. We are well capitalized and our businesses are positioned for continued profitable growth.

I'll now turn the call back over to Craig for a discussion of General Insurance.

Craig Richard Smiddy
President, CEO & Director

Okay. Frank, thank you. For General Insurance, net premiums earned increased by 8% for this quarter and 5% for the year. We continue to achieve strong rate increases on most lines of coverage other than workers' compensation, while renewal retention ratios and new business production remain very strong.

Pretax operating income rose by 33% for the quarter and 34% for the year, primarily coming from improved claim ratios. The overall combined ratio improved over 4 points for the quarter to 88%, and over 4 points for the year to 91%. Claim ratios reported were inclusive of favorable prior period development of 6.6 points for the quarter and 3.8 points for the year.

Turning to commercial auto, specifically. Net premiums earned grew by 5% for the quarter and 8% for the year. The commercial auto claim ratio improved to 61% for the quarter and 71% for the year. Claim frequency that we saw was not quite back to pre-pandemic levels, while claim severity continue to increase, although we observed that it was at a slower pace.

Rate increases in auto liability are continuing in the low double-digit range. So we think we're staying ahead of overall frequency and severity trends, taking into consideration the rates that we continue to achieve.

Now turning to workers' compensation. Net premiums earned were lower by 3% for the quarter and 10% for the year. The workers' comp claim ratio was 61% for the quarter and 59% for the year. Here, claim frequency is still slightly below pre-pandemic levels, while claim severity is slightly up. Rate decreases in workers' comp were, for us, in the very low single-digit range, but we think our rate levels remain adequate, and we will continue to maintain the underwriting discipline that we have so far.

Our aggregated commercial auto, workers' comp and general liability claim ratio came in at 61% for the quarter and 66% for the year. That's an improvement of 5 points over the prior year.

In financial indemnity, property and other coverages as we list them in the financial supplement, we continue to obtain strong rate increases and produce favorable claim ratios contributing to our improved overall claim ratio in General Insurance. These lines of coverage grew by 15% in 2021. And noteworthy, these lines are up over 40% since 2018, which reflects our efforts to diversify our lines of coverage and enhance our underwriting margins.

So the underwriting excellence initiative that we talked about in prior quarters, which we began several years ago, is clearly paying off as we hone our focus on better segmentation, improved risk selection, pricing precision, and we think these efforts will continue to support adequate rate levels, high retention ratios, new business production, and ultimately, continued strong underwriting profitability.

So that concludes my remarks for the General Insurance group, and I'll now turn the discussion over to Carolyn, who I know is anxious and eager to report on Title Insurance's outstanding quarter and year. Carolyn?

Carolyn Jean Monroe
President

Thank you, Craig. As reported this morning, the Title Group posted an all-time high for quarterly underwriting revenue, while quarterly operating profits only trailed the record set of results reported in the second quarter of 2021. Total premium and fee revenue for the quarter of approximately $1.2 billion was up 15% from the prior year fourth quarter. Premium and fee revenue for the year surpassed the $4 billion mark for the first time ever, a 34% increase over full year 2020.

Our pretax operating income of $137 million for the quarter compared to $132 million last year. Year-to-date, our pretax operating income of $515 million exceeds pretax operating income for the same period in 2020 by $171 million or approximately 50%. Full year 2021 results set an all-time record for the Title group.

Commercial premiums were up 63% over fourth quarter 2020 and up 36% for full year 2021 over 2020. The quarterly and annual figures both represent all-time highs. Commercial premiums represented 18% of our total premiums in the fourth quarter and 15.6% for the full year 2021.

While we have seen a decline in order counts over the second half of the year as a result of the slowdown in the refinance sector, purchase transactions, which generate a higher fee per file, remained healthy to close out the year.

In our technology portfolio, Pavaso, the market leader in digital closings, will continue delivering improvements to help in the broader industry adoption. Recognizing the value of Pavaso's capabilities, we are integrating and leveraging those across our family of Title technology companies. This includes our secure portal ready2close within our settlement software RamQuest and ePN, our e-recording company. This will provide an end-to-end digital closing experience for the consumer.

Last quarter, I introduced our new integration platform, [Supermarket]. With the goal to integrate with anything, it will service our agents with an interconnected platform of external partners and technologies that interact and exchange information throughout the entire business workflow. [Supermarket] is live with initial partners performing real-time requests with a road map of growth in place. [Supermarket] will, with a one-stop integration, provide access to a variety of technology services and products to our agent partners.

While simultaneously delivering services to our agents, we are expanding on our internal use of technology. Building on the successful use of RPA, we are actively piloting machine learning with optical character recognition to automate and improve business processes.

We began 2022 investing in our digital future, while continuing to make enhancements to our current environment. These investments will assist our agents and employees in the constantly evolving digital landscape.

And I will now turn it back over to Craig.

Craig Richard Smiddy
President, CEO & Director

Okay, Carolyn, and congratulations on a terrific quarter and a terrific year.

Well, again, we're very pleased with this third year of record-setting operating results. We think these results reflect success of our specialty strategy in General Insurance and Title Insurance, enabling us to produce significant value for our shareholders.

So this concludes our prepared remarks, and we'll now open up the discussion to Q&A where I will answer your questions or I'll ask Frank or Carolyn to respond.

Question and Answer

Operator

[Operator Instructions] We'll take our first question from Greg Peters with Raymond James.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

I guess for the General Insurance component, I'm going to focus on prior year development and the expense ratio. First, on prior year development, definitely a change if you look at the statistical supplement relative to the last several years. And I was wondering if you could give us more color on what's going, which accident years you're getting the favorable development from and which lines and with the outlook there?

Craig Richard Smiddy
President, CEO & Director

Greg, it's Craig here. I think I'll ask Frank to address that, and then I'll chime in if there's anything to add.

Francis Joseph Sodaro
Senior VP, CFO & Chief Accounting Officer

Okay. So the quarter in Europe have a very similar story. The favorable development is coming predominantly from 2010 through 2017. All those years are contributing to the favorable development. And the vast majority is coming through on workers' comp and commercial auto. So it's a similar story to last quarter and just a continuation of it.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Got it. And so just as a follow-up on that answer, I mean, one of the industry themes that everyone's been hearing about is social inflation as it relates to jury verdicts in severity, especially in commercial auto. Should I infer from this that maybe that you've finally achieved getting near rate adequacy in that line of business as it relates to your book?

Craig Richard Smiddy
President, CEO & Director

I think that's a fair assumption, Greg. Clearly, when we set our loss ratio picks for the year, we'll still be cautious and conservative. But all indications are that based on the favorable development that we are seeing in commercial auto liability, in particular, that it seems the compounding double-digit rate increases that we've had for 7 or 8 years. We've talked about, I know, every one of these quarterly calls, and you're finally seeing all of the fruits of our labor come through in the compounding of those rate increases.

And as you know, we're conservative about releasing reserves from prior years on longer tail lines. We, unlike a lot of our peers, we wait, generally speaking, 5 years on workers' compensation, 3, 4 years on auto liability. So that conservative position is starting to play out, and we're seeing, again, very strong reserve levels in those prior years.

And when we look back at them, I want to be clear, too, that given that some of those years still have to settle out, we take into consideration what's happening with social inflation and inflation in general. And when we look back at those years, we appreciate that, that can have -- still have some impacts on any claims that remain unsettled. So likewise, we take a conservative view on those years and make sure that the reserves we have up are adequate in our mind.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Got it. On the expense ratio, just looking at the full year, definitely running, what, 90 basis points higher than the previous year. And certainly, what, 160 basis points higher than your 10-year average. Obviously, business mix can have an effect here, like if you were skewing more towards surety or something like that. But how should we think about the expense ratio going forward?

Craig Richard Smiddy

President, CEO & Director

Definitely, Greg, there are good reasons why that there is a change there, particularly in the fourth quarter. So let me have Frank try to fill in, and then I can pick back up if there's anything for me to add.

Francis Joseph Sodaro
Senior VP, CFO & Chief Accounting Officer

Greg, so you hit on some of it. And I'll focus on the quarter because that there's an impact, obviously, on the year also from that. It's just more dramatic in the quarter. So there is a mix change happening, and we've talked a little bit about that with workers' comp make -- comprising a smaller part of the total, and that tends to have a lower commission rate. So therefore, lower expense level. And the lines that we're adding these other coverages have slightly higher expense ratios, but then they are actually expected to have better underwriting margins. So there's a little bit of a trade-off there that we're seeing in the expense ratio.

But another part of this, pretty much an equal part of this, is that we just had in the quarter an accumulation of some benefit plan true-ups and some miscellaneous charges that all happen to go the same way in the quarter. We don't expect those to recur. So those are -- you see that more in the quarter, but it's also impacting the year.

Craig Richard Smiddy
President, CEO & Director

And Greg, I'll just wrap up by saying we have consistently stated as we do in this quarter's release that our target is for in the General Insurance group for a 25% or below expense ratio. We recognize that we're above that. particularly with these items that Frank mentioned.

And as we go along, we're not moving that target. If the mix continues to trend more towards these other lines that I talked about and that Frank talked about, primarily the financial indemnity lines, the property lines, and the other coverage lines. If we keep -- as we said, we're deliberately growing those lines to diversify. And then you have a bit of a double impact because at the same time, as Frank stated, workers' compensation portion of the portfolio is decreasing, and that had a lower commission ratio. So you have a bit of a double whammy there.

And if those trends continue in the mix, we may take a look at that target. But as of right now, it still remains our long-term target to hit that 25% or below. And as Frank said, fourth quarter is an anomaly and not a predictor of where we're going to be in '22.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Got it. Pivot, Carolyn, on the Title piece. I don't want to diminish the outstanding results for '21, but we're always forward-looking. And if I look at the direct orders open, the direct orders closed on a year-over-year basis, the numbers are trending down. Therefore, it seems like '22 relative to '21 could be -- there could be some erosion in your results, not that an 89 combined ratio for the quarter or for the year is anything to sneeze at. But I'm just curious about your perspective on as you -- the '22 outlook relative to '21.

Carolyn Jean Monroe
President

Well, the drop in orders is mainly because of the mix, the drop in the refi business. And purchase orders are higher fee profile for us. And we recognize that we're still in a very hot real estate market. And while refi orders are down, the resale market is still really strong. We feel good about the market right now. Commercial is still strong after a difficult 2020. But we also understand hot markets don't last forever and any one thing can change them.

We're dependent on inventory, interest rates, a strong economy. And I feel like we're positioned, though, that really no matter what happens, we'll be able to perform.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Okay. Just an observation, is going through your financial supplement, your -- for the runoff business, I know it's steeped in legacy. But you provide a lot of detail for business now that it is only generating $32 million of annualized earned premium. And I think some of us would probably rather see more detail around, say, for example, your General Insurance business rather than a couple of extra pages about a runoff business that's become so small. Just pointing out something that I'm sure you guys are well aware of.

Craig Richard Smiddy
President, CEO & Director

Thank you, Greg. And we appreciate your comment. And as you might have noticed in our releases, in our annual review and other public information, we've tried to give less real estate to the runoff business, and we have discussed those financial supplements. And we'll continue to take a look at it. So we note it, and we'll keep our eye on it and we'll continue to deemphasize that runoff business as we go along and give it less and less real estate and airtime.

Operator

[Operator Instructions] Next, we'll go to Matt Carletti with JMP Securities.

Matthew John Carletti
JMP Securities LLC, Research Division

Greg covered a lot of ground there, so I think I only have really kind of 1, 2 title questions left. So specifically, I was hoping -- I know you've given this to us, but I was hoping you could remind us of, say, for 2021, what the mix of the title book looks like, resi refi, resi purchase and then commercial.

Carolyn Jean Monroe
President

So for 2021, for the full year, our purchase represented 72% of our revenue, refi was 28%. In the fourth quarter, it was closer to 75%-25%. And then commercial is -- for the full year, it was about 15.6%.

Matthew John Carletti
JMP Securities LLC, Research Division

Got it. Great. And then just an observation question, as you look at the past several weeks here, obviously, mortgage rates have started to rise. How should we think about that? I mean, obviously, you talked a little bit about it has a negative impact on refi volumes. Have you seen like any open orders or anything, a positive impact on purchases? There's been a lot of talk about kind of shaking some people off of the bench that have been thinking about doing something and then realizing that now might be the time. Have you observed any of that? Or is that more in theory at this point and we'll see what happens?

Carolyn Jean Monroe
President

Yes. We have observed it. Once we got through the people finally got off vacation and started getting back into it, we've really noticed it probably the last couple of weeks, the purchase business picking up for us.

Matthew John Carletti
JMP Securities LLC, Research Division

Great. Very helpful. Congrats on a nice quarter and year.

Operator

And that does conclude today's question-and-answer session. I'll turn it back over to management for any additional or closing remarks.

Craig Richard Smiddy
President, CEO & Director

Okay. Well, as it seems to be the case when we have a good quarter and a great year like this, there's not a lot of difficult or challenging questions for us. And right now, we, as I stated earlier, feel very good about where Old Republic International sits with our 2 key businesses, General Insurance and Title Insurance, and we look forward to another productive, good year in 2022. I wish all of you the best, and thank you for your support and for listening to our conference call today. So thank you very in much.

Operator

And this concludes today's conference call. You may now disconnect.