S&P Global
Market Intelligence

Kemper Corporation NYSE:KMPR

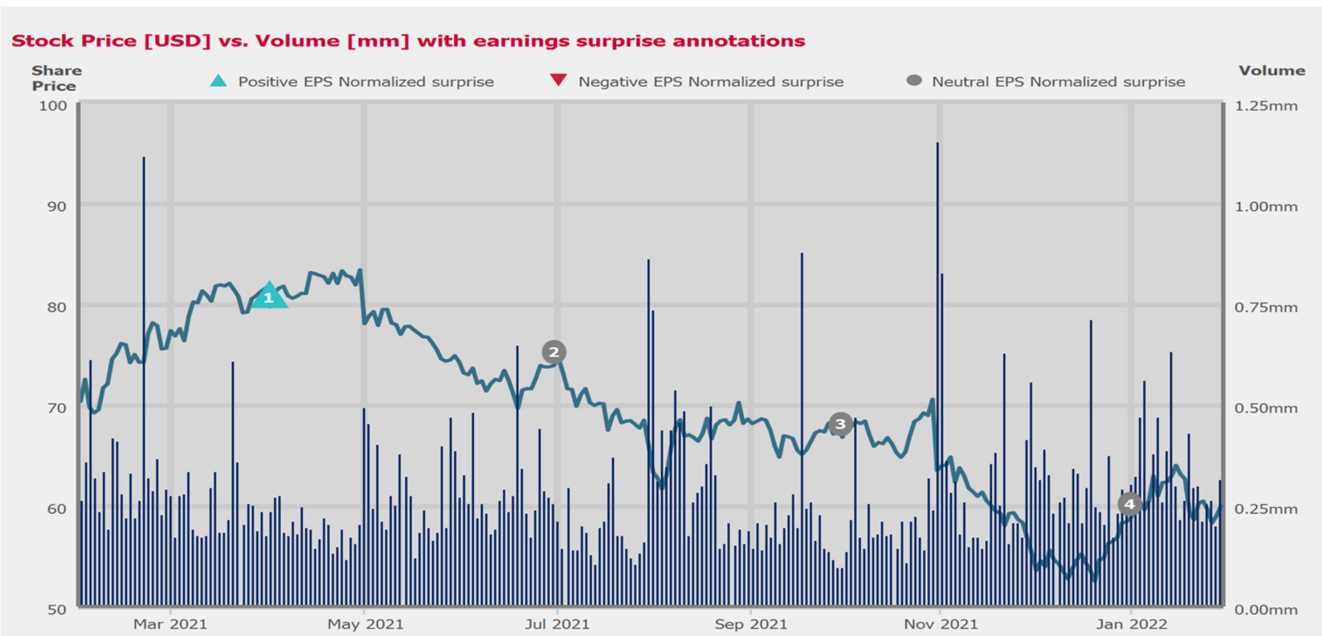
FQ4 2021 Earnings Call Transcripts

Monday, January 31, 2022 10:00 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	(0.28)	(2.05)	NM	(0.67)	(1.67)	(3.40)	NM	0.07
Revenue (mm)	1471.61	1240.60	(15.70 %)	1467.17	5706.93	5131.40	(10.08 %)	5950.70

Currency: USD
Consensus as of Feb-01-2022 11:24 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2021	1.29	1.31	1.55 %
FQ2 2021	1.37	(1.54)	NM
FQ3 2021	(0.21)	(1.19)	NM
FQ4 2021	(0.28)	(2.05)	NM

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Call Participants

EXECUTIVES

Duane Allen Sanders
Executive VP and President of Property & Casualty Division

James J. McKinney
Executive VP & CFO

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Karen Guerra;Vice President of Investor Relations

ANALYSTS

Brian Robert Meredith
UBS Investment Bank, Research Division

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

Gary Kent Ransom
Dowling & Partners Securities, LLC

Paul Newsome
Piper Sandler & Co., Research Division

Presentation

Operator

Good afternoon, ladies and gentlemen, and welcome to the Kemper's Fourth Quarter 2021 Earnings Conference Call. My name is Tania, and I will be your operator for today's call. [Operator Instructions] As a reminder, this conference call is being recorded for replay purposes. I would now like to introduce your host for today's call, Karen Guerra, Kemper's Vice President of Investor Relations. Ms. Guerra, you may begin.

Karen Guerra;Vice President of Investor Relations

Thank you, operator. Good afternoon, everyone, and welcome to Kemper's discussion of our fourth quarter and full year 2021 results. This afternoon, you'll hear from Joe Lacher, Kemper's President, Chief Executive Officer and Chairman; Jim McKinney, Kemper's Executive Vice President and Chief Financial Officer; Duane Sanders, Kemper's Executive Vice President and the Property & Casualty Division President.

We'll make a few opening remarks to provide context around our fourth quarter results and then open the call for a Q&A session.

During the interactive portion of our call, our presenters will be joined by John Boschelli, Kemper's Executive Vice President and Chief Investment Officer; Erich Sternberg, Kemper's Executive Vice President and Life & Health Division President.

After the markets closed today, we issued our earnings release and published our earnings presentation and financial supplement. We intend to file our Form 10-K with the SEC on or about February 10. Our discussion today may contain forward-looking statements within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements include, but are not limited to, the company's outlook and its future results of operations and financial conditions. Our actual future results and financial conditions may differ materially from these statements. These statements may also be impacted by the COVID-19 pandemic. For information on additional risks that may impact these forward-looking statements, please refer to our 2020 Form 10-K as well as our fourth quarter earnings release.

This afternoon's discussion also includes non-GAAP financial measures we believe are meaningful to investors. In our financial supplement, earnings presentation and earnings release, we have defined and reconciled all the non-GAAP financial measures to GAAP where required in accordance with SEC rules. You can find these documents on the Investors section of our website, kemper.com.

All comparative references will be to the corresponding 2020 period unless otherwise stated. I will now turn the call over to Joe.

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Thank you, Karen. Good afternoon, everyone, and thank you for joining us. Earlier today, we reported our fourth quarter and full year results. Goes without saying, we were disappointed with our profitability.

The pandemic-driven environmental challenges we've discussed in the last couple of quarters not only remain but has intensified. These challenges have impacted each of our businesses. In P&C, last quarter, we discussed the relationship between earned rate and loss severity.

We talked about the fact that loss inflation is immediately incurred and negatively impacts results. Rate increases are subject to regulatory approvals, roll on to policies at renewal and are earned over the life of the policy.

The benefit of those increases is therefore, delayed. The suspension of rate increases during the pandemic and the inflation surge that came with reopening the economy has created an historic mismatch between policy cost and pricing. In the fourth quarter, we continued to see increases in inflation-driven loss severity.

Labor rates, auto body repairs and rental car rates all continued to rise due to inflationary trends related to supply chain issues and labor shortage. As an example, in 2021, used car prices were up 51% from 2019 and 37% over 2020.

In the last quarter alone, they were up 9%. These increases in costs have a direct and immediate impact on our margins and did not moderate. To respond to this environment, during the quarter, we made significant progress on both rate and non-rate profit improvement.

Overall, we exceeded our targets for the number of rate filings submitted, the percentage of our book impacted and the level of rate increases approved. These actions will favorably impact future results.

We see this aggregate inflation rate imbalance continuing in the short term. Due to the actions we have taken and will continue to take, we believe the situation will stabilize and ultimately restore margins to appropriate levels.

Progress will initially be gradual, then more rapid as earned rate benefits are fully realized. The Life & Health segment continues to be negatively impacted by the pandemic. In the quarter, the business continued to incur excess mortality.

Throughout the initial wave, then the Delta variant and now Omicron, our excess mortality rates have remained largely in line with national trends. In summary, we closed the year making significant progress that will become increasingly visible in our results. We are actively taking rate and non-rate actions to restore our margins and are working to accelerate this process every way possible. Duane will discuss more shortly.

Unfortunately, the most significant improvement levers will take time. It's a little like planting tomatoes after the winter. You can't start until after it warms up, and it's going to take 80 days before you can eat the fruit. There's no way to get the fruit faster. We couldn't take rate until frequency rebounded from the lockdowns. And once filed, rate takes time to bear fruit. There isn't a way to meaningfully accelerate it. Though it will take time, we are confident our actions will be successful and position us for growth. I'll now turn the call over to Jim to discuss our operating results in more detail.

James J. McKinney
Executive VP & CFO

Thank you, Joe. Let's turn to Page 4. For the quarter, we generated a net loss of $106 million or $1.66 per share as reported, and $101 million or $1.59 per share as adjusted for acquisitions.

We also produced an adjusted consolidated net operating loss of $131 million or $2.05 per share, as reported, or $126 million or $1.98 per share as adjusted.

Earned premium increased 12% on a reported basis and 5% after adjusting for the AAC acquisition. The net loss for the quarter was primarily driven by environmental headwinds that impacted loss costs throughout our P&C businesses. Our focus has been and will remain on restoring Kemper to target profitability.

During the third and fourth quarter combined, the P&C teams filed for approximately 11 points of rate on 56% of our personal auto books. Further, the team executed a number of underwriting and non-rate actions to improve margins. Duane will provide greater detail on this topic later.

Turning to Page 5. Return on tangible equity, excluding unrealized gains, was negative 4.9%. This is below our targeted long-run return. Excluding unrealized gains, tangible book value per share declined $7.21 compared to last December.

Of this change, $3.11 is related to the acquisition of American Access and the corresponding goodwill the transaction created. The corrective actions we have taken and are taking in response to higher loss cost trends will over time enable us to achieve our historical value creation levels.

On Page 6, we highlight our view of operating income that continued to be negatively impacted by environmental challenges. As mentioned earlier, this quarter, we witnessed higher severity leading to our Specialty P&C segment reporting an as-adjusted underlying combined ratio of 119%.

In addition, in our Life & Health segment, we continued to experience elevated life benefit costs due to excess COVID-related mortality and increased persistency.

On Page 7, we review some of the key capital metrics we use to track our performance, including growth in tangible book value per share and tangible return on equity. For the last few quarters, we have been below target.

We believe these challenges to be short term in nature and do not expect them to impact our long-run targets. Recent performance is a direct result of the environmental challenges impacting the industry. While this is disappointing, we've instituted and will continue to institute corrective measures to restore the business to target profitability.

On Page 8, we highlight the strength of our balance sheet. Our substantial capital and liquidity positions enable us to navigate and optimize within the current environment. We continue to produce strong cash flow, generating over $350 million for the year. This has enabled us to continue to make investments in our business and optimize our geographic footprint for the long-term profitable growth. Our insurance entities are well capitalized. Liquidity remains strong and our debt-to-capital ratio of 21.9% remains within our target range.

Moving to Page 9. We provide an overview of the highlights to our multiyear excess of loss reinsurance and our annual aggregate catastrophe programs. Each year, we review our programs to align with our risk appetite and to minimize our cost of capital. For 2022, we purchased an additional $75 million in limits in our excess of loss program due to our Specialty Auto growth.

Our program will cover losses at 95% of $300 million in excess of $50 million. In addition, we renewed our catastrophe aggregate program with a $5 million increase in the retention level. This program is intended to reduce earnings volatility from high frequency, low severity events. Increased limits and the corresponding costs were offset by savings on the cat ag program, Thus, there was minimal impact to our year-over-year costs.

Turning to Page 10. Net investment income for the quarter was $108 million. Our portfolio construction is designed to match liabilities and provide stable income through various cycles. This quarter, we generated a pretax equivalent yield of 4.6%.

In closing, the company's quarterly financial performance continues to be pressured by various environmental factors. We are confident that the corrective actions we have taken and are taking will, over time, return us to our financial targets. With that, I'll now turn the call over to Duane, who will provide details on our P&C segment.

Duane Allen Sanders
Executive VP and President of Property & Casualty Division

Thank you, Jim, and good afternoon, everyone. Let's turn to Page 11. Last quarter, we introduced this slide to help illustrate the working dynamics we are navigating. At the onset of the pandemic, miles driven and accident frequency were historically low.

During this time, Kemper had effectively no rate increases, and additionally, along with most major carriers, delivered premium rebates to customers. As we emerged from lockdowns, we saw loss trends shoot up against prepandemic unchanged rates. These dynamics will continue to put pressure on margins in 2022 as the written rate translates to earned rate later in the year.

This illustration is intended to bring clarity and context to the profit restoration journey. As the diagram highlights, the inflationary and rate curves create several potential paths and time lines to get there.

Moving to Page 12. We'll begin with the Specialty P&C. Against the challenging backdrop of inflationary trends related to labor shortages and supply chain issues, along with frequency reaching pre-pandemic levels, the segment experienced an underlying combined loss ratio year-over-year increase of 28 points, a sequential quarter increase of 11 points.

Despite this quarter's loss and temporary rate imbalance, our view of long-term profitability of the business remains highly favorable. The chart on the upper right shows the progress made in obtaining rates throughout the year, including an approximate time line on how actions will earn through our businesses.

For example, during the fourth quarter, we filed for approximately 8% rate on roughly 57% of our book, with much of the 2021 rate already effective. We're in the process of filing for an additional 7% on 60% of our specialty book in the first quarter.

Understandably, it takes time for filed in effective rate to be written and earned into our results. We expect the majority of the filed rates in 2021 to be earned in 2022, with the most significant earned impact in the second half of the year.

Now let's turn to Page 13. The Preferred P&C segment continues to face similar challenges. Looking at the chart on the upper right, we filed for approximately 12% rate on roughly 23% of our preferred auto book during the fourth quarter. We're in the process of filing for an additional 10% on 17% of our book in the first quarter.

In summary, the organization is focused on the most important levers to restoring profitability. I'll now turn the call back to Joe.

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Thank you, Duane. As we turn to our Life & Health segment on Page 14, we highlight that life earned premium increased 5% due to persistency improvement. The base value of in-force policies continues to increase, driven by higher persistency in new business sales. We also observed and are encouraged by strong consumer demand for our products.

Lastly, our mortality results remain in line with countrywide trends. As the mortality impacts of COVID subside, life mortality and benefit costs should revert to more normalized levels.

In closing, although we're disappointed in this quarter's financial results, I couldn't be prouder of our team and how our organization has responded to the circumstances and challenges over the last couple of years. We remain focused on managing through these circumstances, returning to target probability and expanding on our long-term competitive advantages.
I'll now turn the call over to the operator for questions.

Question and Answer

Operator

[Operator Instructions] The first question is from the line of Greg Peters with Raymond James.

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

I'd like to just focus on the information you provided in Slides 11, 12 and 13. And on 12 and 13, particularly of interest was, where you give us a chart in the upper right-hand corner defining how much rate has been filed for, and how much should be impacting the first quarter results in '22. And then if you look at the -- in both for specialty and preferred, you see that the amount of rate impact is going to be less than what the deterioration has been. So I guess I'm looking for a reconciliation of that, as we think about first quarter, second quarter, third quarter.

And then the other piece of this is there's more than just rate that you can do to improve your results, and you know this, you can cancel agents, you cannot -- you can be more strict on new business. So I'm curious what's going on in that -- on that side of the underwriting house, if possible?

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Sure, Greg. This is Joe. I'll take a shot at it and then -- first, let me walk you through the top right corner of 12 and 13 a little bit to make sure

[Audio Gap]

And it is intended to let you see sort of how things waterfall their way through. Let's use 12 as the example. In the third quarter of '21, we filed for rate on 34% of our premium and its weighted average was 3%. That also happened to be effective in that quarter. You're getting a written impact in the quarter of 1.8% of rate and 0.1% earned. Those are not just from the third quarter. Those are from all prior quarters that occurred during the pandemic.

What you see when you drop to the fourth quarter is we filed for rates that had 57% of our premium impacted and then for 8% rate, only 37% of that was effective. That means there was another 20% that's filed, but it's still pending department approval.

The overall impact of 3.5 written points -- that maps to some combination of what occurred in the second and third quarter as well. Where we're trying to help you see how each of these works their way through, it's not intended to be a perfect

[Audio Gap]

and you can't quite see it without providing a massive set of tables to work those things across.

Ultimately, we expect you're going to want to understand the earned impact and how that works through loss ratios. And that will come over time as you work it from

[Audio Gap]

Now we are clearly doing a variety of non-rate actions, a variety of non-rate actions. We are canceling agents. We have adjusted new business, underwriting tiering. We are working with commissions. We are doing a whole

[Audio Gap]

from a non-rate perspective. We're changing billing plans

[Audio Gap]

of adjusting what risks we write. All of those things are occurring fairly significantly across our book of business. And those do have a tendency, depending on the activity, to have a quicker earned impact. And so they are coming -- they're a little bit less crystal clear to quantify in this kind of chart. Is that -- Greg, is that helping? Or...

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

Yes, that was a great explanation of the charts. And I guess, Joe, everyone is listening in on this call, just wondering when that inflection point -- you look at the chart on Page 11, and rate meeting an exceeding loss trend is the holy grail that everyone wants you to get to. And are we going to see more deterioration before it starts to stabilize and improve? Or is this as bad as it's going to get? And the timing, when will we get to that holy grail?

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Yes. And those are exactly the right questions. And I'm literally going to go back to a couple of comments I made, and

[Audio Gap]

The complexity of Slide 11 is what is loss trend going to be going forward and for how long? And how fast do regulators allow rate to be effective?

We can control the non-rate activities and move those relatively briskly. I don't think, if we back up a quarter or 2 quarters, we were an early view that inflation was going to start rising. And I think most folks thought we were pessimistic and weren't predicting what was coming.

I think most of the industry

[Audio Gap]

projection of what's coming. I'm not 100% sure where that's going to be over the next couple of quarters. I do know that we are seeing the regulatory environment recognizing the uniqueness of this space. Not everyone, but I -- we've had great success in, say, in Florida and Texas, filing multiple rate filings for significant amounts of rate that are moving us along that path.

That, in fact, is the $24,000 question that we're dealing with. Our sense is the fourth quarter tends to be a seasonally worse quarter and the first quarter tends to be a seasonally better quarter. That might be several points, 2, 3, 4 points even, that are a plus. And you wouldn't have seen a lot of the non-rate impact in the third quarter. You'll see a little in the fourth, and you'll see more coming in the first and second.

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

Got it. I guess the other -- the big state is California. And I know if you go over a certain threshold in terms of rate filing, you'll all of a sudden get the consumer advocate involved, et cetera. Can you give us an update on how your negotiations are progressing with the state of California?

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Sure. At this point, we have 4 programs in California. All 4 programs have had a rate filing introduced to the

[Audio Gap]

close to the 6.9%, just under 7%, threshold that you just described. Several of them have been accepted and moved into analysts.

Several of them are relatively recent in terms of when we get the

[Audio Gap]

I'm not during the fourth. I believe our rate filing was one of the first -- I think it was the first to move from sort of that

[Audio Gap]

to be viewed by and worked on by an analyst. So we felt good about that.

And we're working through the process with the insurance department. I have a reasonable degree of confidence that the insurance commissioner and the department are thoughtful about all of the issues that are going on. They recognize, like other insurance departments around the country, that loss inflation is running high.

It's a historic issue that we're dealing with from an industry perspective. And it really is important to them to keep vibrant [viable] open markets in terms of what they're doing. And I think they're going to recognize that moving on

[Audio Gap]

is critical to the health of the industry and health of the market overall, and I'm optimistic that they'll be responsive.

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

Got it. I guess the last question. I know there's others that want to ask questions, so I'll -- this will be my last one. Prior year development, can you comment on both the prior year development in the Specialty Auto and the other parts of your business, please?

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Yes, sure. So in specialty, a relatively marginal favorable development that's come through on some of the coverages like BI, but not -- I wouldn't highlight a larger broad trend other than I would indicate [that] we continue to try to make sure we're making thoughtful reserve selections. And you just saw a little bit of favorability relative to that.

In terms of the [BI] book, what I would suggest and what we've seen a little bit coming in from that front is some increased costs associated with litigation inside New York, with some of our policyholders, and some of the other traditional trends you're seeing nothing here really from a new -- an overly new trend perspective, but an item that has kind of been working through relative to just the way that

[Audio Gap]

acting in some of the behavior changes that -- as a result of the pandemic.

And so with that, we saw a couple of those data points and then reacted to them this quarter just to make sure that we're in the right spot.

Operator

The next question is from the line of Paul Newsome with Piper Sandler.

Paul Newsome
Piper Sandler & Co., Research Division

Always tough to have tough results, but I know you guys are working as hard as you can to right the ship. First question, just a simple one. Roughly the [30%] that's not getting rate -- actually, they haven't got the impact rate in specialty, is that -- should we think of that as basically the California book? Or is that just a too simple way to look at it?

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Yes, it's a good question, Paul. Maybe the chart is causing us a challenge. That's not a cumulative set. It's not that there was 34% in the third quarter, then another 23% [got it]

[Audio Gap]

That is 34% of the premium [got it] and an additional 57% and an additional 60% will get it in the first. So in some cases, what you've got is some are getting their second or third helping.

So included in the 57% and the 60% is all of our California books. Some of them were in the 57%, some of them were in the 60%. Every book we have in California in Specialty Auto has received an increase. In some cases, as an example, I believe Florida was in the 34%, and Florida was also in the 57%.

So they're incremental, it's not cumulative. And again, we're -- you can pull the rate filings in individual states and you can see them. We were trying to get

[Audio Gap]

in a way that let us see the total overall in this process.

Paul Newsome
Piper Sandler & Co., Research Division

Okay. Great. I mean the information is definitely helpful.

Duane Allen Sanders
Executive VP and President of Property & Casualty Division

One of the biggest points where there is kind of the delay between the effective and then eventually the earned, to your point, yes, a bigger chunk of that is California at this stage. And again, we'll -- you can track timing of approval, the same as us, with online filings.

It will be delayed and then there will be an implementation date that's probably 45 days out from whenever that approval comes in. So that is what it is, and we'll continue to update the tables. And hopefully, what you've seen is a good consistency here with these and we're trying to provide as much insight here as possible to try to enable that.

Paul Newsome
Piper Sandler & Co., Research Division

No. No, the data is definitely very helpful. You've already touched on this, but normally, the fourth quarter for you guys is a little bit of a worse quarter from a seasonal projection in a couple of points.

Anything beyond that, given the unusual nature of today's environment, that would sort of change that seasonality if we can sort of pull out all the pandemic stuff?

Duane Allen Sanders
Executive VP and President of Property & Casualty Division

Yes, Paul, not that we know. I think the big item, and I think Joe highlighted this in some of his comments on that. When you see inflationary trends and we're giving it purely in the example side here, for example, used car prices, and you see 9% quarter -- sequential quarter-over-quarter growth, those are big numbers.

It's to the extent that they're going to move like that and continue to move like that for the year of [37]. So what that tells you is it's not really slowed down yet. To the extent the economy slows down a little bit or people's behavior is -- like they're not going to go up for forever.

It is a -- an element that does depreciate. There's probably an elongation to some degree of the utility in that depreciation curve, to some extent that will take kind of given just what the supply-demand imbalance is.

But until we see some moderation or [stavability] in those things, I think it's going to be a little bit more volatile than what we would normally like. But I think that, that pressure potentially exists up and down, right, when it comes to these things because once you do have the right supply, you do have some of these things normally. Again, this is a depreciating asset that has a -- it has a limited value and a limit of life to it. So it will go to zero at some point in time. But we're just not seeing that at this stage.

Paul Newsome
Piper Sandler & Co., Research Division

Great. Last question. I'd like to ask a little bit more on capital. It looks like overall capital is fine. But I noticed the RBC ratio in the P&C business were down a bit in 2021. But at the same time, you are growing PIF at least in the specialty business. Does that suggest that you might be pushing capital down into the P&C business over the next year?

Duane Allen Sanders
Executive VP and President of Property & Casualty Division

It's very possible that we would. I mean, what we've highlighted is that the HoldCo is here to service

[Audio Gap]

for our insurance entities and our businesses. To the extent that we're not where we would want to be from -- in terms of our risk appetite or other elements in terms of prudence, we would make injections appropriately.

We have plenty of capital and liquidity available at the HoldCo to do that without creating any type pressure or other. But we're going to navigate through this environment very thoughtfully, and we're going to make sure that our entities remain strong -- capitalized strong and really when policyholders and others would look at us, they can -- they're going to know that Kemper is more than able to stand behind our promises.

And we're also going to know that we're able to -- we're not going to make any rash or -- decisions or other that are forced on us. We've got a strong, stable business that we'll optimize through this environment.

Operator

The next question is from the line of Gary Ransom with Dowling & Partners.

Gary Kent Ransom
Dowling & Partners Securities, LLC

Yes. You may have already sort of answered this on the fourth quarter loss ratio and seasonality. But was there any true-ups for the current accident year that might have run through the number in the fourth quarter?

Duane Allen Sanders
Executive VP and President of Property & Casualty Division

Yes. So there's roughly about 2 points in the [pay] book that I think you're most focused on that's running through. It's relative -- largely is focused on the third quarter. What you're seeing is some increased inflation severity trends, not necessarily in our [pace] but in terms of how we expect those to play out as we continue to move forward in the future and what we think that inflationary environment is going to be on our collision coverages. So that's there. Again, inflation, especially in used cars continues to run hotter, even hotter than our probably higher projections than most, but that's driving a component of that. We also saw a little bit on the BI front, just, again, not necessarily in the page up into that point in time, but we're looking at kind of increased inflationary trends, looking at differences as it relates to behavior changes, whether it be attorney rep rates or other elements.

And so we've reacted a little bit to that from an LAE perspective to make sure that we've got that accounted for on a go-forward basis. And we'll see how that kind of comes together. But there's about 2 points in summary that is inside there.

Gary Kent Ransom
Dowling & Partners Securities, LLC

Was there anything from the Florida PIP issue? Or did those estimates hold from last quarter?

Duane Allen Sanders
Executive VP and President of Property & Casualty Division

No, those estimates have held. No further update.

Gary Kent Ransom
Dowling & Partners Securities, LLC

Have held, okay. Great. Then I also have to ask about frequency. I think last quarter, you more or less talked about frequency coming back to 2019 levels more or less within a point. Is that still generally the case?

Duane Allen Sanders
Executive VP and President of Property & Casualty Division

That is still the case. No change from that front at this [point].

Gary Kent Ransom
Dowling & Partners Securities, LLC

Okay.

Duane Allen Sanders
Executive VP and President of Property & Casualty Division

I mean [indiscernible] versus a frequency. I think what you're really trying to add is this a frequency item or a severity item. Right now based on our reviews and when we pull back the covers in every which way direction, what we come out with and it'll be interesting once we get other schedule Ps in that because I think they'll provide some additional comparison points, but we're seeing this as a severity [item]. There's nothing from an underwriting perspective or other that we're seeing these large changes. We just continue

[Audio Gap]

the costs associated with items increasing and we're trying to react to that the best that we can. But the industry structurally isn't really set up for 50% kind of 2-year type changes and other. Now we'll work through it. It's not the -- it just takes time to get to these. It's not whether -- it's not an if, it's just a when, and we're working that as fast as we can at this stage.

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

And it's principally in metal coverages. So it's severity issue frequency, and it's predominantly inside of the metal coverages.

Operator

The next question is from the line of Brian Meredith with UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

A couple of questions here for you. First, just a clarification, I just want to understand that I'm getting this chart on Page 12. If I look at the overall impact on a written basis, so I think what you're saying is that these are individual by quarter what the written impact. So the cumulative impact by the end of the first quarter should be something north of 11%? Am I getting that right?

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

No. What you should do is say that 5.8%, that's the cumulative impact on written of all of those and what it is for to be written, that policy had to either have been new or renewed. So as an example, if the third quarter '21 number, if it had been approved in August, it might not be an effective. It will not hit some of those policies on renewal.

It will hit some in September, some in October, some it won't hit till March or April. That 37% that became effective in the fourth quarter, some of that was, say, in December. So the first policy that actually gets the impact of that would be in January.

And if a 12-month policy if you could get one quarter of it in the year, but with 6-month policies, you get half in the first quarter. So that is intended on the right side of the dotted line show you the cumulative impact. Normally, this would be a really hard chart to read. There wasn't a lot of rate that was running

[Audio Gap]

so it is intended to give a cumulative. And again, I don't think that's going to be different from most folks have out there. I think we're just trying to put it in a way that you can sort of illustratively see it working its way in. It will accelerate rapidly as you get into the second and third quarter because of everything you see. If you just do the math on what you see running through the fourth and the first, that surge comes through.

Brian Robert Meredith
UBS Investment Bank, Research Division

Okay. Great. That's helpful. And then just quickly, just a clarification. Your policies are 6-month policies, right? So could I have just -- some people were just a little surprised that the earned impact was as low as it was?

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

No. We've got a mixture of policies effectively, we have more 6-month policies, I think, than most preferred standard carriers, but more than 50% of the book is going to be 12-month policies that are coming through there.

Brian Robert Meredith
UBS Investment Bank, Research Division

So even in your specialty segment?

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Yes, even in our specialty segment because again, we're careful to say inside of specialty, it's specialty, not just nonstandard. The nonstandard part of it is predominantly 6-month policies, but there are pieces of this where we very specifically might look at it and say, it's another specialty, the Hispanic customer segment. There are pieces of this that are nonstandard and there's pieces of it that are closer to standard.

Brian Robert Meredith
UBS Investment Bank, Research Division

Got you. Okay. Helpful.

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

And that difference in underwriting profile that that's deliberate on our part.

Brian Robert Meredith
UBS Investment Bank, Research Division

Okay. That makes sense. And then I'm just curious, going back to the non-rate actions, maybe you can give us some perspective. How much of an impact would you expect that to have as far as getting back to your profitability? Is it 1/4 of it, 1/2 of it? Because if I just take a look at where you are right now with your loss ratios, I mean, it looks like you need, assuming loss trend is 0, 20% to 25% cumulative rate to get back to your kind of normalized margins.

Now that's not assuming nonrate action. So how much will that contribute?

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Yes. We're -- I'm trying to figure out how to get you exactly the answer you want, Brian, and I understand it, and I'm going to give you an answer and then we'll talk about it a little bit and you'll understand the

[Audio Gap]

It ultimately, probably comes in to somewhere around 1/3 to 1/2. And now I'm going to get to be a little bit of an insurance wonk and mechanic. We should just commission like a point or two. If we did it, that would affect and have sort of an immediate earning impact that gets you to something. We have, in a lot of our programs, underwriting tiers that -- there's an ability inside of the same rate level to move you to a higher [Audio Gap]

How those are slotted. That doesn't change the renewal book, but that does change the new business coming in. So that sort of has an immediate impact on what's running through new.

We could eliminate an agency. Well, that might stop new business on that for that agency, but it doesn't immediately cause their new business -- I mean, so the renewal book to go away. So there are pieces of this that go in immediately across the whole book,

[Audio Gap] new only or might have

[Audio Gap]

So we're working all of those at this point. I mean, there's some stuff we can do just on general expenses underneath. We're working all of those. The first 1/3 of the non-rate actions get felt fastest and the back half or 2/3 go a little slower. And I'm trying to get you the precision you want because I know what you want to do is what -- exactly what I would want to do is put it into

[Audio Gap]

That helps you project the loss ratio and combined ratio improvement. And I'm not sure how to capture it in precisely the way that I think you're looking for it.

Brian Robert Meredith
UBS Investment Bank, Research Division

Okay. That's helpful. That helps a lot. And then maybe we can focus a little bit just on top line and kind of what are your expectations over the next 12 to 18 months as you fix this problem? What's going to happen with respect to PIF counts in your specialty business?

And maybe a little bit on how you manage or handle your distribution in periods like we are right now.

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Yes. We're pushing pretty hard on underwriting restrictions and

[Audio Gap]

Some of this is going to be a function of what's competitively done in the market. And we -- I would expect the business will be flat and maybe down some over the near term. We would be happy or very comfortable if it was down a little more than that in the near term. They're -- the more underwriting disruption one company provides the more

[Audio Gap]

The more everybody is doing that, there's less of a place for it to land. So you can more quickly impact new business, but sometimes you actually see a little uptick in retention because it's harder for those customers to move and they deal with the underwriting or pricing things that are happening to them.

So it's not completely clear the pace with which the market is also moving. I would expect that we'll be closer to flat or down some inside of specialty and would be comfortable it was down a bit more near term.

Brian Robert Meredith
UBS Investment Bank, Research Division

Okay. And then I guess my last question...

Duane Allen Sanders
Executive VP and President of Property & Casualty Division

I would -- just to be careful to split this between PIF and kind of written and earned. And so for the PIF, I would suggest that the written or earned will likely exceed and continue to grow as a result of both the pricing and the underwriting actions that we're taking. So probably some slight deterioration maybe on the PIF side, but I would hold, again, a lot of market components associated with that and how things will move. So we'll see, but definitely, I think you're going to see continued strong probably earned and written growth as both the rate and underwriting actions continue to earn in.

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Yes, that's a perfect clarification on my comments were PIF related. That will definitely, with the rate activity, what I would expect the written and earned to go up.

Brian Robert Meredith
UBS Investment Bank, Research Division

Got you. And then last question for you. Let's think out 12 to 18 months from now and what potential opportunities are. I mean, I would think that if you all are seeing these types of issues and some of your larger competitors are, the small to midsize players that you compete a lot with, and that's where you're really targeting, must be having a really difficult time right now.

Do you see opportunities kind of both inorganically and organically kind of really grab share, call it, once profitability gets to where you need it to be?

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Yes, it's -- so 2 pieces of it. One, we are 100% focused right now on focusing on restoring our underlying profitability, but I would be shocked if we don't find a large chunk of the competition we have in the space that is slower and is behind on the bigger issues. I don't think they're as financially strong. I don't think they spotted the issues as quick, and I don't think our ability to

[Audio Gap]

So I do expect that there's going to be a little messy for a couple of quarters, cleaning it up, and I think it's going to be worse for them and it's going to take them longer.

And I think ultimately, that will present an opportunity. I will enjoy that opportunity a lot more than we're enjoying right now [what we're working with].

Operator

The next question is from Greg Peters with Raymond James.

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

Thanks for allowing me to ask a follow-up. With the focus for most of the presentation on the non-life business, I think it's probably appropriate to spend a minute and talk about the Life business, too. Because that really has been a headwind because of COVID-related issues. How are you thinking about that business for this year, for fiscal year '22 and for fiscal year '23?

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Yes. No, great question. I think it's a great business first overall. And to really get a full view of the economics, I think it's important to actually take a look through statutory returns, which, again, will have some of the additional return elements or investment elements in terms of hedging.

You'll see it made roughly $40 million if you're tracking through the year when you put this in. Not great, not bad, but about a 10% return, right, on the surplus that's inside that. Again, down from historical

[Audio Gap]

target. I highlight that because I still think you're going to see much more of a return to kind of the pandemic.

That's what all of our models, things of that nature would indicate. But I would tell you that the pandemic continues to take turns that are unanticipated at certain points or maybe anticipated, but it's lasted a lot longer.

Originally, you thought that vaccines -- and they are having a marked impact. But if you're even looking now, while you have an Omicron component of this, and you look at -- and you sit there and say, well, yes, it might be less -- have less of a severity impact in certain components, just because of the speed with which it has spread, you're now actually seeing mortality rates, right, that are in excess of what they were during the second peak associated.

So hopefully, we'll get through this period, both as a country, and more broadly speaking, and things will return to more of those pre-pandemic norms. But

[Audio Gap]

and when I say short term, I think within the next year to 2 years, in each stage, I think we've gotten better at responding. When I say we, I think, from a country, medicine, many things have gotten better on that front. But at that same point in time, there could be continued volatility from expectations or those base case expectations. But hopefully, once we're through there, what you'll see is more of a return to that long-term earnings pattern that we've had there.

I can tell you from an underlying -- from persistency and some of the economic elements that are underneath that. And if I were to think about it from a value in force or other perspective, it's increasing in value in terms of where we're going, which suggests those trends.

But it also was saying, hey, the pandemic is not going to continue to go on forever. And when I think about a business that nations are 30-plus kind of year cash flow decisions that you're making. Okay. So we got a year or 2 years, again, still pay -- but not what we've historically had.

Hopefully, that's just a minor blip in terms of what ends up being a very strong -- over

[Audio Gap]

the period. And as, again, things kind of hopefully revert back to more normal, and we work our way through this.

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

Got it. And just I can't help myself. On Slide 9 of your presentation, you provide us the detail around your reinsurance program. For the 2021 program year for the cat aggregate program, did you use all of your $50 million, in excess of $60 million? Or...

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

For the 2021, like, I think you're asking specifically did we have enough cat events above the $500,000 from the inside the property business to hit our retention level, not hit our retention level in 2021.

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

And you did not exceed that? You did not exceed that...

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

We didn't get any recoveries -- so we -- not only do we not use the $50 million, we didn't start using the $50 million.

Operator

I will now turn the conference over to the presenters for any closing remarks.

Joseph Patrick Lacher
President, CEO & Non-Executive Chairman

Well, thank you, everybody, for joining the call. We appreciate your

[Audio Gap]

a lot of work cut out for us here, which I think we've described

[Audio Gap]

excited to get after it. And for Brian, where you suggested, we'll be, hopefully, a few quarters out. Thanks, everybody.

Operator
That concludes Kemper's Fourth Quarter 2021 Earnings Conference Call. Thank you for your participation. You may now disconnect your lines.