S&P Capital IQ

CONTENTS

Universal Insurance Holdings, Inc. NYSE:UVE

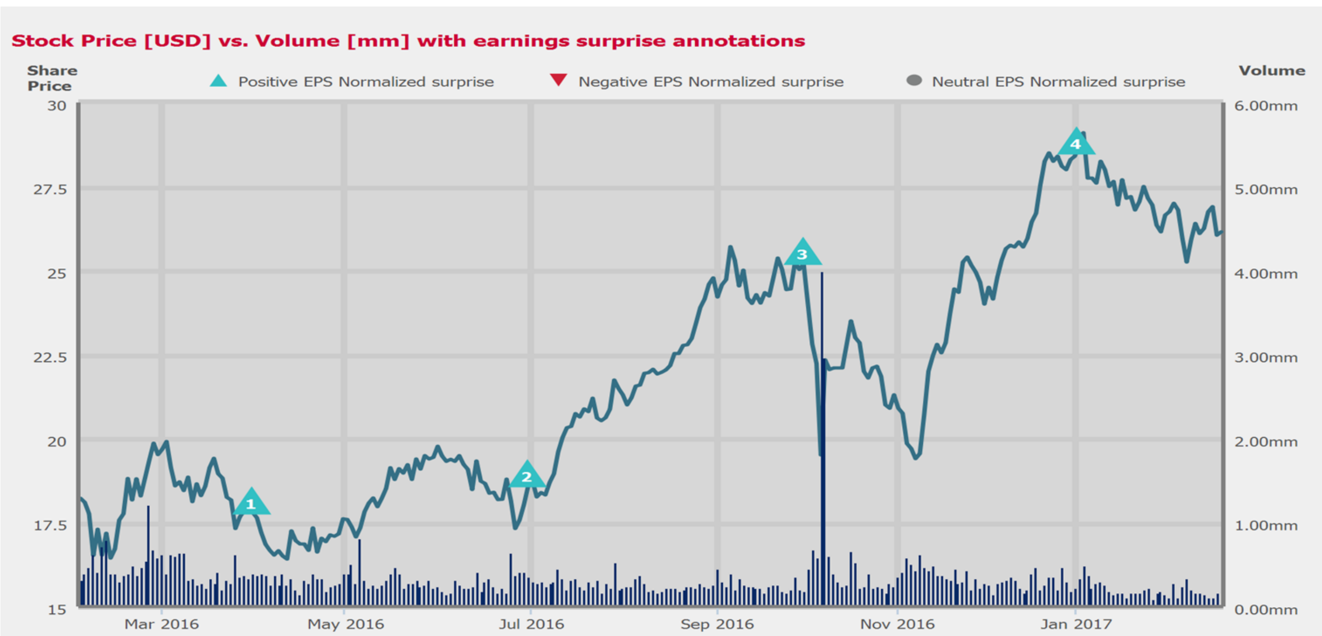
FQ1 2017 Earnings Call Transcripts

Wednesday, April 26, 2017 2:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2017-			-FQ2 2017-	-FY 2017-	-FY 2018-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.70	0.86	▲22.86	0.88	3.01	3.25

Currency: USD
Consensus as of Apr-26-2017 2:20 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2016	0.63	0.71	▲1 12.70 %
FQ2 2016	0.81	0.94	▲2 16.05 %
FQ3 2016	0.60	0.75	▲3 25.00 %
FQ4 2016	0.20	0.38	▲4 90.00 %

Call Participants

EXECUTIVES

Dean Evans
Vice President of Investor Relations

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer

Jon W. Springer
President, Chief Risk Officer and Director

Sean P. Downes
Chairman and Chief Executive Officer

ANALYSTS

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

Samir Khare
Capital Returns Management, LLC

ATTENDEES

Unknown Attendee

Presentation

Operator

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

I would now like to turn the conference over to Dean Evans, Vice President Investor Relations. Please begin.

Dean Evans
Vice President of Investor Relations

Thank you, Latoia. And good morning, everyone. Welcome to the first quarter 2017 earnings conference call for Universal Insurance Holdings, Inc. My name is Dean Evans, and I'm the Vice President of Investor Relations here at Universal.

With me in the room today are Chairman and Chief Executive Officer, Sean Downes; President and Chief Risk Officer, Jon Springer; and Chief Financial Officer, Frank Wilcox. Following Sean's opening remarks, Jon will provide an update on reinsurance, and Frank will review financial results. The call will then be reopened for questions.

Yesterday afternoon, we issued our earnings release, which is available under the Press Releases section of our website at www.universalinsuranceholdings.com. A replay of this presentation will be available on the homepage of our website until May 11, 2017.

Before we begin, please note that this presentation may contain forward-looking statements about our business and financial results. Forward-looking statements reflect our current view of future events and are typically associated with words such as believe, expect and anticipate or similar expressions. We caution those listening, including investors, not to rely solely on forward-looking statements as they imply risks and uncertainties, some of which cannot be predicted or quantified, and future results can differ materially from our expectations. We encourage you to carefully consider the risks described in our filings with the Securities and Exchange Commission, which are available on the SEC's website or the SEC Filings section of our website. We do not undertake any obligation to update or correct any forward-looking statements.

With that, I would like to turn the presentation over to our Chairman and Chief Executive Officer, Sean Downes.

Sean P. Downes
Chairman and Chief Executive Officer

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

We are pleased to report another profitable quarter with strong top line growth. For the first quarter, we delivered a 6.3% increase in total revenues and a 6% increase in net earned premiums. We reported strong underwriting profitability with a solid 78.9% net combined ratio for the quarter.

Although the quarter included some unexpected weather events, our claims handling team once again performed up to our high expectations. And these events had a minimal impact on our quarterly earnings with only $3 million of pretax net losses and LAE as a result. We reported net income of $31.2 million and diluted EPS of $0.86, which equates to a return on average common equity of 31.4%.

We believe we've positioned Universal for the future by pursuing various organic growth avenues. These include further growth in our home state of Florida, expanding our footprint into new states; strategic initiatives, such as Universal Direct; and new business lines, such as a Commercial Residential product.

These initiatives have resulted in a more stable, diversified and balanced business that is well positioned to drive growth and long-term shareholder value. Our core Florida market continues to produce solid top line growth, with policies in force, premiums and total insured value, each increasing by roughly 5% in the first quarter. While we are certainly a large part of the Florida marketplace, we continue to believe that we have the opportunity to continue to grow organically, given our tremendous agency network and Universal Direct.

Geographic expansion remains a core element of our growth strategy, and we continue to see an increase in policy count, premiums in force and total insured value for states outside of Florida in the first quarter, with each showing growth of more than 40% from the comparable quarter last year. Of note, during the first quarter, we received our Certificate of Authority from Iowa. Currently, Universal is running business in 14 states and is now licensed in additional 5 states.

Universal Direct, our direct-to-consumer online platform for homeowners insurance, is now available in all of our active states. Since launch, we've over 3,000 policies in force for more than $3.5 million in premium. We continue to receive positive feedback from customers who appreciate the flexibility and convenience of purchasing homeowners insurance online.

We've recently partnered with BBMC, a national mortgage company, who offers a complete line of residential mortgage, refinance and specialty loans. Universal Direct will provide real-time quotes to BBMC customers during the mortgage qualification process. This partnership is the first to be rolled out under the Universal Direct affiliate program, which we hope to expand in the future to include other businesses and the home purchasing arena for utilizing the proprietary B2B tool that we have created.

We are confident in our business model, coupled with our commitment to providing best-in-class product offerings and service to our policyholders, which we believe positions Universal for profitable growth in 2017 and beyond.

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

Jon W. Springer
President, Chief Risk Officer and Director

Thanks, Sean. I think the most relevant current topic to discuss would be an update on the status of our reinsurance placement to be effective June 1, 2017. Over the course of the past 2 months, we've met face-to-face with vast majority of our reinsurance partners to discuss this upcoming renewal. As of late yesterday, after receiving and evaluating quotes from our lead reinsurers, we entered the market with firm order terms on the core all states catastrophe tower per UPCIC, and authorizations have already started to arrive this morning. When you take into account the coverage provided by the Florida Hurricane Catastrophe Fund, the coverage we previously negotiated within multi-year transactions and the pricing levels released yesterday, we have now established the cost of over 90% of our desired catastrophe capacity.

At this point, the 2017 renewal is shaping up to be a year where we'll be keeping our catastrophe retention at the same level on a growing book of business, buying catastrophe coverage to a higher level and spending less as a percent of earned premium to do so.

With that, I'll turn it over to Frank.

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer

Thank you, Jon. For the first quarter of 2017, net income totaled $31.2 million, an increase of 23.7% compared to 2016. Diluted EPS was $0.86, up from $0.71 for the first quarter of 2016 due to the increase in net income, partially offset by a modest increase in diluted shares outstanding.

During the quarter, we continued to experience top line growth with increases in every major category of revenue compared to the prior year's quarter. Direct premiums earned of $236.4 million, offset by ceded premiums earned of $74.8 million, generated $161.6 million of net earned premiums for Q1 of '17 compared to $152.4 million in Q1 of '16. The increase was the result of organic growth from both Florida and other state growth initiatives. Ceded premiums earned as a percentage of direct premiums earned was 32% and 31%, respectively, during Q1 '17 and Q1 '16.

Commissioned revenue of $4.6 million for the quarter grew 11.8% compared to the same quarter in 2016, reflecting the differences in our reinsurance programs in effect during those periods, including an increase in our exposures covered by reinsurance. Policy fees of $4.5 million for the quarter grew 9% year-over-year from an increase in the number of policies written during the first quarter of 2017 compared to the prior year quarter. Other revenues of $1.6 million, which is comprised primarily of financing fees and charges, grew 6.1% from prior year's quarter, reflecting both growth and consumer behaviors underlying the policies written during the periods being compared.

Net investment income for the quarter was $2.7 million, growth of 68% from Q1 of '16. This reflects both an increase in our invested assets and actions taken to maximize yields, while maintaining high credit quality as securities mature. We realized $63,000 in losses from the sale of investment securities during the quarter compared to $667,000 in realized gains in Q1 of 2016.

We continue to maintain a high quality investment portfolio comprised of 90% fixed maturity securities, of which 98.6% are investment-grade securities, and we take a conservative approach to managing our investments.

Total invested assets reached $666.1 million as of March 31, 2017, compared to $541 million 1 year prior, an increase of 23%. The weighted average duration of the fixed maturity investments in our available for sale portfolio at March 31, 2007, was 3.4 years, while the book yield of this portfolio was 1.79% for the first quarter of '17 versus 1.25% in the first quarter of '16.

We generated a net combined ratio of 78.9% for the first quarter of 2017 compared to 80.8% for the first quarter of 2016. The net loss in LAE ratio was 43.7% compared to 43.4% in the prior year's quarter. We recorded $3 million or 1.9 points of losses in LAE related to weather events beyond plan in the first quarter of '17, compared to $8.5 million or 5.6 points during the first quarter of 2016. While there was 3.7 loss ratio points less than impact from weather events beyond plan in the first quarter of '17 versus '16, this was offset by an increase in the underlying net loss ratio of 4%.

Our net expense ratio for the quarter of 2017 was 35.2% compared to 37.5% for the same period in 2016. Our net acquisition cost ratio increased slightly to 20.1% from 19.4%, largely reflecting increased acquisition cost related to our other state expansion. This was more than made up for by a decline in other operating expense ratio, which was 15.1% in the first quarter of 2017 versus 18% in the prior year's quarter. The primary factors behind this decrease were reduction in executive compensation and economies of scale.

The effective income tax rate was 34.1% in the first quarter of 2017 compared to 38.6% for the same quarter in 2016. The first quarter of 2017 reflects 2 discrete items. The first was a credit to income tax expense of $0.8 million for excess tax benefits resulting from stock-based awards divested and/or were exercised during the first quarter of 2017.

This credit to income tax expense represents the application of a new accounting pronouncement. Prior to this quarter, excess benefits were reflected in stockholders' equity. The other discrete item is a credit to income tax expense of $1.3 million, resulting from anticipated recoveries of income taxes paid for the years 2013 through 2015. Collectively, these discrete items lowered our effective tax rate by 4.3%, leaving our underlying effective tax rate for Q1 of '17 in line with the expectations.

Our balance sheet continues to strengthen with stockholders' equity and book value per common share of $398.8 million and $11.37 per share as of March 31, 2017, an annual growth of 26.9% and 25.9%, respectively.

Consolidated unrestricted cash and cash equivalents were $160.4 million and combined surplus for insurance subsidiaries was $350 million as of March 31, 2017, respectively.

We are committed to actively managing our capital position and took several actions on that front in the first quarter of '17. We repurchased over 100,000 shares for $2.5 million or an average cost of $25.46 per share. We believe these repurchases represented a tremendous value in light of our current return on equity. $15.4 million remains on our current repurchase authorization.

We paid dividends of $0.14 per share in the first quarter, equating to an annualized dividend yield of 2.4% at current share price levels. Return on equity was 31.4% in the first quarter of 2017 compared to 32.6% in the first quarter of 2016. We remain dedicated to providing value to our shareholders and believe this 31.4% return on equity coupled with our 2.4% dividend yield is an excellent result.
At this point, I'd like to turn the call back to the operator.

Question and Answer

Operator

[Operator Instructions] And the first question is from Adam Davidson, private investor.

Unknown Attendee

I know on the last call you mentioned potential expansion into New York and New Jersey. Could you just provide an update on how that's progressing?

Sean P. Downes
Chairman and Chief Executive Officer

Yes, thanks for your question. We have our rates and forms filed in New York and hope for an approval sometime this year. Last week, we actually received an approval in New Jersey. And as of today, we are live in New Jersey writing business. I'm pleased to say that we actually wrote our first policy this morning. We've had our folks in New Jersey for the last few months, getting agencies appointed, and basically, just replicating the same model that we've used in other states. We'll have our Fast Track folks in New Jersey to handle claims as they arise. So we're happy and pleased to be a part of the New Jersey marketplace.

Operator

And the next question is from Arash Soleimani of KBW.

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

Can you talk about what you're seeing in terms of frequency of AOB lawsuits year-over-year, and also, relative to the fourth quarter?

Sean P. Downes
Chairman and Chief Executive Officer

No, we're not really seeing a large spike in lawsuits, Arash. I'm sure you're referring to the CaseGlide form. Any moment in time, you see how that goes up and down. I think it's a seasonal thing to be honest with you. We have seen somewhat of increase as it relates to some plaintiffs' attorneys being a little bit more aggressive. But one thing that we've done, really that's different than first quarter of '16, is that all of our AOB claims that are in a litigious environment are being handled by our internal law firm of more than 20 attorneys. So we're not really having to deal with outside attorneys. We're not having that extra cost that you would if you're using a third-party law firm. So we believe that, that is going to pay dividends to us down the road. And as far as the frequency is concerned from a lawsuit perspective, we're seeing that, that's up a little bit. We're seeing the overall AOB frequency relatively flat or down by a tick or so. But I do want to make it clear that the AOB issue is an issue for our company the same way it is everybody else's. I just think that what we put into place over the last 3 years, as it relates to our own legal law firm, if you will, in-house, our Fast Track division, our subrogation division, when you couple all those things together, it's lessening the severity, when you compare us to some others. But it is an issue, and we're doing everything that we can to lessen the severity.

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

So basically, you're saying the frequency is up a bit, but the -- all the stuff you're doing is kind of offsetting that from a severity perspective?

Sean P. Downes
Chairman and Chief Executive Officer

I would say, as a percentage of AOB frequency related to plaintiffs' attorneys, that is up. Overall, AOB is relatively flat or down a tick or 2.

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

Okay. And also, are you seeing any spread outside of tri-county with AOB?

Sean P. Downes
Chairman and Chief Executive Officer

Yes. More than 50% of our AOB claims are outside of the tri-county area.

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

Okay. But is it becoming more prevalent outside of tri-county than it was, maybe a year ago or so?

Sean P. Downes
Chairman and Chief Executive Officer

No, the ratios are basically in line with what they were a year ago, as far as the spread of the overall AOB claims.

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

Okay. And the other question I was going to ask. Have you filed for rate increases yet this year in Florida, and if so, what are you expecting and then when do you expect to implement it?

Sean P. Downes
Chairman and Chief Executive Officer

We're just about at the end right now of our rate indication process. I'm sure, as you're aware, '14, we had a minus reduction of roughly 2.4. In '15, we had an increase of about 2.2. Last year, we were flat. And this year, we're looking at probably somewhere, I'm guessing right now, some things to change here the last week or 2, but I believe we'll be filing for some midrange single-digit increase sometime next month.

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

Okay. And when would -- when do you think you'll be able to implement that, if approved?

Sean P. Downes
Chairman and Chief Executive Officer

Probably, September 1, give or take.

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

Okay. The other question I had was around the liability for unpaid losses. So I know you guys have some subrogation efforts and Fast Track that help. But I saw that drop quite a bit again in the first quarter, so just wanted to get understanding of what was driving that.

Jon W. Springer
President, Chief Risk Officer and Director

Yes, I think -- Arash, this is Jon. I think as I've said in the past, you really need to take a holistic view of loss reserves. It -- looking at the number of remaining open claims, and in turn, how many claims have closed in whatever period of time you're looking at. So when you take into account what our Fast Track team is doing in terms of new claims and how quickly we're getting to those claims and closing them, in addition to what we've been able to do with the "legacy claims," what you would see occurring during the first quarter is that we closed nearly 50% of the open claims that existed on the books as of 12/31/16. In addition to closing nearly half of those, we also paid out over $50 million of partial payments on those remaining open claims. So after you take into account all the claims closed and all the partial payments on the remaining opens, then lastly, you would look at the IBNR, and of course, take into account the amount of anticipated subrogation recoveries to be included on top of the IBNR.

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

Okay. And is Fast Track -- is the Fast Track program, I guess, is it more robust than it sounds than it was a quarter ago? Is it -- are you seeing major strides with that program? Or -- I'm just trying to think of what caused Fast Track to contribute that much more this time.

Sean P. Downes
Chairman and Chief Executive Officer

More bodies on the ground bolstering that division, creating some time lines that are even more stringent than they were in the past. And basically, handling 80% of all of our claims through the Fast Track division, which is, obviously, contributing to lesser cost as it relates to LAE. Then, again, when claims are in litigious arena, we're having our own internal law firm handle the claims. All first-party lawsuits, AOB claims are all being handled by our internal law firm.

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

Yes. The 80% you mentioned for Fast Track, can you just for comparison what would that have been about a year ago?

Sean P. Downes
Chairman and Chief Executive Officer

I believe, right now, when I talked about claims, these are claims that are eligible for Fast Track. So almost look at it as a triage when we're going into a hospital. Claims that we can get to, we can pay immediately and settle within a few days. I believe that number probably in early '16, up on top of my head, was more like 60 something. Early 60s. When you compare that to where we're at now, it's a big difference.

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

Okay. And from a prior period development perspective, I guess, question for Frank, was there any development in the quarter?

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer

There was, Arash. It was negligible, 96,000, less than 1%.

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

And was that favorable or unfavorable?

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer

That was unfavorable.

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

Okay. And when you mentioned the plan you have for storms, what you guys assume as, I guess, normal or expected?

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer

Well, we set aside embedded within the loss ratio that we booked to an amount for Florida and a separate amount for outside of Florida for weather events. So if you look at the loss ratio we booked to, we break that into 2 pieces, and we have a portion of it for weather, a portion of it for all other perils.

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

Okay. And my last question on the expense ratio improvement. How much of that came from economies of scale improving versus executive compensation declining?

Sean P. Downes
Chairman and Chief Executive Officer

Each benefited us by about 1.5%.

Operator

The next question is from Samir Khare of Capital Returns Management.

Samir Khare
Capital Returns Management, LLC

Just on the claims storms. Do you have the numbers of the loss ratio for Florida of expected weather losses?

Sean P. Downes
Chairman and Chief Executive Officer

Samir, could you just say that a little bit -- we lost you a little bit there at the end.

Samir Khare
Capital Returns Management, LLC

Yes, so I'm just asking to quantify the expected loss ratio for poor weather on an expected basis.

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer

Let me tell you the whole picture in terms of first quarter 2017. So we booked to a 29.5% loss ratio overall. Specific to Florida, that would be a 27% loss ratio within Florida. Approximately a 50% loss ratio outside of Florida. Then breaking down that 27% for Florida, approximately 24.5% would be for all other perils and approximately 2.5% for Florida weather losses.

Samir Khare
Capital Returns Management, LLC

Got it. Okay. So it sounds like there were some considerable weather losses outside of Florida. Is that correct?

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer

Yes. So I guess, the number I didn't give you is the approximately 50% loss ratio outside of Florida is broken down roughly 40 for all other perils and 10 for expected weather losses. The activity outside of Florida in the first quarter, including 5 different PCS events, totaled a loss amount beyond what we had planned for. The largest of which was PCS 17 13 happening in mid-January. We had over 700 claims from that. Second would have been PCS 17 21 happening in late March. We picked up over 150 claims from that event.

Samir Khare

Capital Returns Management, LLC

Okay. And just a few other questions on the subrogation. And specifically, on the GAAP prior period development, any particular accident year losses that produced any noteworthy favorable or unfavorable period development?

Sean P. Downes
Chairman and Chief Executive Officer

No, nothing that stands out.

Samir Khare
Capital Returns Management, LLC

Okay. And just to make sure I understand the subrogation. On a GAAP basis, that's considered in the incurred loss and the reserve numbers, but in stats, it's not, is that right?

Sean P. Downes
Chairman and Chief Executive Officer

In Schedule B, it's presented gross.

Samir Khare
Capital Returns Management, LLC

In Schedule, okay. But on the reserve numbers on the balance sheet, it's -- it is incorporated on the stat, is that correct?

Sean P. Downes
Chairman and Chief Executive Officer

Yes. Yes.

Samir Khare
Capital Returns Management, LLC

Okay. And then how often are you guys doing reserve reviews versus -- a fully blown versus actual versus expected analysis?

Sean P. Downes
Chairman and Chief Executive Officer

In terms of our outside actuary?

Samir Khare
Capital Returns Management, LLC

Yes. Or internally.

Sean P. Downes
Chairman and Chief Executive Officer

Well, I mean, internally, we're looking at it regularly as you might imagine. In terms of our outside actuaries, we will continue to do 2 separate analyses a year.

Samir Khare
Capital Returns Management, LLC

Okay. And that will include an analysis of the subrogation reserves as well?

Frank C. Wilcox
Chief Financial Officer and Principal Accounting Officer

Absolutely.

Samir Khare
Capital Returns Management, LLC

Okay. And was there any material increase or decrease to the subrogation reserve from year-end 2016 and prior?

Sean P. Downes
Chairman and Chief Executive Officer

No.

Samir Khare
Capital Returns Management, LLC

Okay. And then just on the subrogation, you guys take credit for it as you see the opportunities within your claims files? Or are you guys incorporating some allowance for it in returns in your loss ratio pick?

Sean P. Downes
Chairman and Chief Executive Officer

It's within the go-forward loss ratio pick. So the actuarial study that was done provided a predictable salvage in subro rate, which then, of course, was incorporated into the loss reserves and in turn incorporated into future loss picks.

Samir Khare
Capital Returns Management, LLC

Okay. And can you quantify how many points it is?

Sean P. Downes
Chairman and Chief Executive Officer

No, now I can't, not off the top of my head.

Samir Khare
Capital Returns Management, LLC

Okay. And just in light of your stock price, any share repurchases quarter-to-date?

Sean P. Downes
Chairman and Chief Executive Officer

We've not done any since the first quarter.

Operator

And at this time, I'd like to turn the call back over to Sean Downes for closing remarks.

Sean P. Downes
Chairman and Chief Executive Officer

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

Operator
Thank you. Ladies and gentlemen, this concludes today's conference. You may now disconnect. Good day.