S&P Global
Market Intelligence

Intact Financial Corporation TSX:IFC

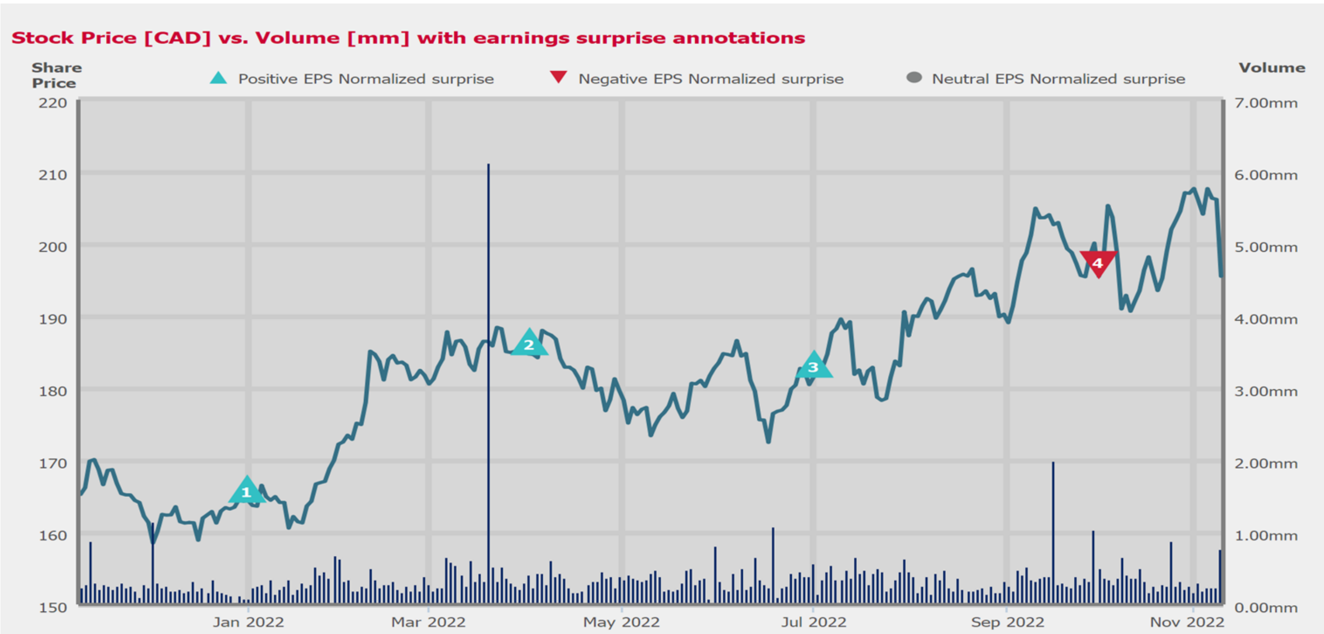
FQ3 2022 Earnings Call Transcripts

Wednesday, November 9, 2022 4:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2022-			-FQ4 2022-	-FY 2022-	-FY 2023-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	2.74	2.70	(1.46 %)	3.16	11.79	NA
Revenue (mm)	5080.17	4945.00	(2.66 %)	5082.25	19464.78	NA

Currency: CAD
Consensus as of Nov-10-2022 11:55 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2021	2.52	3.78	1 50.00 %
FQ1 2022	2.43	2.70	2 11.11 %
FQ2 2022	2.73	3.14	3 15.02 %
FQ3 2022	2.74	2.70	4 (1.46 %)

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Call Participants

EXECUTIVES

Charles J. G. Brindamour
CEO & Director

Darren Christopher Godfrey
Executive Vice President of Global Specialty Lines

Kenneth Anderson
Executive Vice President & CFO of UK and International

Louis Marcotte
Executive VP & CFO

Patrick Barbeau
Executive VP & COO

Shubha Rahman Khan
Vice President of Investor Relations

ANALYSTS

Brian Robert Meredith
UBS Investment Bank, Research Division

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RBC Capital Markets, Research Division

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TD Securities Equity Research

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CIBC Capital Markets, Research Division

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Presentation

Operator

Good morning, ladies and gentlemen, and welcome to the Intact Financial Corporation Q3 2022 results. [Operator Instructions] I would like to remind everyone that this call is being recorded on Wednesday, November 9, 2022.

I would now like to turn the conference over to Shubha Khan, Vice President of Investor Relations. Please go ahead.

Shubha Rahman Khan
Vice President of Investor Relations

Thank you, Joanna. Good morning, everyone, and thank you for joining the call today. A link to our live webcast and published information for this call is posted on our website at intactfc.com under the Investors tab.

As usual, before we start, please refer to Slide 2 for cautionary language regarding the use of forward-looking statements, which form part of this morning's remarks, and Slide 3 for a note on the use of non-GAAP financial measures and important notes on adjustments, terms and definitions used in this presentation.

With me today, we have our CEO, Charles Brindamour; our CFO, Louis Marcotte; Patrick Barbeau, Executive Vice President and Chief Operating Officer; Darren Godfrey, Executive Vice President, Global Specialty Lines; and Ken Anderson, Executive Vice President and CFO, U.K. and I. We will begin with prepared remarks followed by Q&A.

With that, I will turn the call to Charles.

Charles J. G. Brindamour
CEO & Director

Good morning, everyone, and thank you for joining us today. In late September, Hurricanes Fiona and Ian caused widespread devastation in Atlantic Canada and the Southern U.S. We acted quickly and decisively. Fiona, the strongest hurricane in Canadian history, deserved a robust response given our deep presence in the Atlantic. We've mobilized, beyond our people in the region, over 100 distribution and claims staff in other parts of Canada to ensure service remains very strong as we come to help our customers. Drone operators were brought in from Western Canada for damage appraisal and On Side added one of their staff to their local team to help with emergency repairs.

Overall, we're better equipped than ever before to deliver on our purpose to help people, businesses and society do well in good times and be resilient in bad times. Despite severe weather events, inflation headwinds and capital markets volatility, we delivered solid results. Yesterday evening, we announced net operating income per share of $2.70 for the third quarter. Underlying topline growth was 4% after adjusting for the impact of exited lines. The overall combined ratio was 92.6%, reflecting cost pressures in personal lines and very strong underwriting performance in commercial and specialty lines.

Let's look at each of our lines of business, starting with Canada. In personal auto, premiums were largely flat year-over-year. Less policy shopping by customers in a muted rate environment as well as our rate increases ahead of our competitors weighed on new business volumes. We expect our competitive position to improve as the market reflects inflation in its pricing. Our focus on profitability resulted in a combined ratio of 93%. We achieved this despite 13% claims inflation in the quarter. This is a testament to our pricing strategy, our supply chain actions, our prudence in reserving, and the fact that frequency remains below historical average.

I'm also encouraged by early signs that inflationary pressures are actually easing. Car prices were flat to down in September relative to August. The cost of OEM parts was stable quarter-over-quarter, and improved parts availability is reducing gradually repair times, resulting in less upward pressure on rental costs. As I've said on previous calls, we've been proactively managing cost pressures for some time now. Rates have been moving higher since early Q2. In aggregate, written rates and insured values increased close to 6 points by September, and this will increase to around 9 points by the end of the year. We expect premium increases to cover the loss cost inflation we're anticipating.

There's also a good degree of caution embedded in our reserves for both short and longtail claims. This has been true of past years and continues to be true for the current year. That's why I very much look at the underlying performance and prior year development in aggregate. With the actions taken so far, I expect our personal auto business to run at a sub-95% combined ratio over the next 12 months.

Meanwhile, the environment is evolving as we anticipated. We expect industry premium growth to climb to the mid-single-digit range due to inflation and changing driving patterns.

In Personal Property, premiums grew 7% against the backdrop of firm market conditions. The combined ratio of 98.4% included 16 points of CATs, mostly due to the impact of Hurricane Fiona. Weather and inflation are continuing to support rate increases at a high single-digit level. As a result, our expectation continues to be that even in bad times, this business will operate at a sub-95% level on a full year basis.

In Commercial Lines, premiums grew 4%. Strong rate momentum in a hard market was partially offset by lower new business volumes in non-specialty lines. A very healthy combined ratio of 87.9% reflected continued rate increases and profitability actions. We expect market conditions to remain favorable due to the elevated CAT losses, inflation pressures and reinsurance costs. As a result, our Commercial Lines of business remains well placed to sustain low 90s or better performance.

Moving to our UK&I business, which delivered a combined ratio of 93.5%. In Personal Lines, premiums decreased by 13%, mainly due to the sale of RSA's Middle East business. The combined ratio of 105.5% included 7 points of reserve strengthening. This was primarily for elevated subsidence claims after an unusually dry U.K. summer as well as inflation pressure. The underlying performance of this business remains in the high 90s after allowing for seasonality. We continue to prioritize bottom line performance and are maintaining pricing discipline in a competitive market. We expect market conditions to begin firming due to inflation. This remains our most difficult marketplace. That said, we have less than 8% of our business in this segment.

In Commercial Lines, premium growth was roughly 9% after adjusting for the impact of our Middle East exit and actions to optimize our delegated business in the U.K. We continue to benefit from hard market conditions, which are supporting high single-digit rate increases. The combined ratio was very strong at 85%, reflecting our continued profitability action. The business continues to perform well with rates tracking ahead of loss cost trends. I'm pleased with the overall performance of the UK&I business, but we remain very focused on taking actions required to drive a sustainable outperformance in Personal Lines.

Our U.S. Commercial business once again grew at a double-digit pace, thanks to continued focus on expanding profitable lines and favorable market conditions. The combined ratio of 90.5% reflected solid rate increases over the past 12 months as well as our exit from the public entities business. We remain well placed to deliver low 90s or better performance in the U.S.

Turning to our strategic initiatives. I'm pleased that the RSA integration remains very much on track. In Canada, more than 95% of policies outside of Affinity and Specialty Businesses have been converted to Intact systems and products. All RSA claims are now being handled by Intact adjusters and increasingly within our supply chain. Close to 70% of legal files are being handled by the in-house legal team. In addition to driving part of our combined ratio performance, this ensures a consistent customer experience. And it's no surprise, therefore, that retention levels continue to be consistent with or better than RSA's historical experience.

On the distribution side, we completed 6 broker acquisitions across the country in Q3. This helped BrokerLink surpass $3 billion of premiums early in the quarter. As we said at Investor Day in September, our ambition is to grow this business to $5 billion by 2025. There's a lot of room for us to consolidate in a highly fragmented market through disciplined capital deployment.

And finally, we further enhanced our supply chain capabilities. During the quarter, we opened 6 new partner-operated Intact service centers, expanding our network to 13 locations. Increased volume to our growing network of dedicated service centers is reducing cycle times and containing repair costs.

As we set our sights to 2023 and beyond, there is really strong momentum right across our business. Despite inflation pressures, we've delivered low 90s underwriting performance so far this year, and growth continues to be solid, particularly in Commercial Lines. With a robust balance sheet, disciplined underwriting, and the RSA integration firmly on track, we're well positioned to grow net operating income per share by 10% per year and outperform the industry ROE by at least 500 basis points.

And with that, I'll turn the call over to our CFO, Louis Marcotte.

Louis Marcotte
Executive VP & CFO

Thanks, Charles, and good morning, everyone. We reported solid results this quarter, with all segments delivering combined ratios in the low to mid-90s despite inflationary pressures and significant weather events. Investment and distribution income remained strong and operating ROE for the last 12 months is 15%. Given the challenging environment we are in, I'm quite happy with these results.

The overall combined ratio of 92.6% was 1.3 points higher than last year, with improved performances across all of our Commercial Lines tempered by the impact of weather and inflation on our Personal Lines results. CAT losses in the quarter were $229 million, driven largely by Hurricanes Fiona and Ian. In aggregate, this level of losses is broadly in line with our expectations for a third quarter. I will provide an update at year-end on our annual CAT guidance, taking into consideration the outcome of our January 1 reinsurance renewals.

Favorable prior year development was broadly unchanged from last year and remained healthy at 2.9%. This is in line with our current guidance of 1% to 3% over the long term and towards the upper end of this range in the short term. Net investment income increased by 21% year-over-year, reflecting higher yields captured in a rising interest rate environment. I now expect investment income for the full year to be approximately $885 million, $20 million higher than our guidance in the prior quarter due to higher yields on our fixed income portfolio.

Distribution income grew 6% to $111 million, which includes a contribution from Highland Insurance, our newly acquired U.S. based NGA. Otherwise, growth was somewhat muted due to lower variable commissions relative to last year's elevated levels. On a full year basis, we expect distribution income for 2022 to be around $435 million, an increase of 20% over last year.

Now let's turn to our underwriting results, starting with Canada. In personal auto, the underlying loss ratio increased by 9.6 points compared to a very strong 62.5% last year. Though up modestly from the prior year, frequency remains below pre-pandemic levels. However, we continue to price for higher frequency than we observe today, as society is still adjusting to new driving patterns. The significant increase in severity is not a surprise given inflationary pressures. A combined ratio of 93% demonstrate that our pricing and claims actions are working. The results also include close to 5 points of favorable prior year development, which reflects our reserving prudence. This prudence in reserving will penalize our current accident year results, which is why it's important to look at our underwriting results in aggregate, including prior year development. Now given our prudence in pricing and reserving, I am confident we will be able to operate this business at sub-95% combined ratio over the next 12 months, adjusting for seasonality.

In Personal Property, the 98.4% combined ratio reflected 15.6 points of CAT losses. That's almost 5 points higher than expected. The underlying loss ratio increased in the quarter by 7.1 points compared to a benign Q3 2021, primarily driven by higher weather-related losses. That being said, the business has delivered 94.6% year-to-date with most of the CAT season normally being behind us, which suggests we are on track to perform at a sub-95% for the full year.

In Commercial Lines, the combined ratio was strong at 87.9% despite 2 points of CATs higher than expected in the quarter, mainly in respect to Hurricane Fiona. While we are seeing inflation in this line of business, this is more than offset by higher rates. The overall expense ratio in Canada improved by 1.6 points, driven mainly by lower variable commissions across all lines of business. At around 30% year-to-date, the expense ratio was broadly in line with expectations.

Turning now to the UK&I, which delivered an overall result of 93.5%. In Personal Lines, the combined ratio of 105.5% reflects what was a challenging quarter for the industry. Underlying losses were elevated due to a weather-related phenomenon in the U.K. known as subsidence. This can occur in certain parts of the country following unusually hot and dry summers. It can lead to land movements under homes potentially leading to cracks or other damage to parts of the structure. Subsidence added around 4.5 points to our Q3 loss ratio. In addition to this, and as expected, inflation pressures put around 2.5 points of strain on the results as we move to update our current year reserves to reflect recent trends.

In Commercial Lines, the combined ratio was very strong at 85%, reflecting the line large losses in U.K. and solid prior year developments. CAT losses of 3.5 points were in line with expectations. Overall, I'm pleased with the progress being made on our profitability action plan, which is showing in the results.

In our U.S. business, the combined ratio was strong at 90.5%. This included 3 points of CAT losses primarily related to Hurricane Ian. The underlying loss ratio improved by 2.1 points as we benefited from a more favorable business mix, including our exit from Public Entities. Overall, the U.S. is running in the right zone as we continue to see the benefits of our profitability actions.

Our Global Specialty Lines business is performing well across all regions. Year-to-date premiums are up 13% at $4.2 billion with a combined ratio of 85.9%. With such momentum, we are confident we have the platform to achieve our ambitions of growing this business to $10 billion in premiums by 2030 and running at a sub-90% combined ratio. A quick word on the RSA integration. I announced at our recent Investor Day that we now expect to achieve at least $350 million in annual synergies by mid-2024, $100 million more than our initial guidance. This reflects a mix of expense synergies, additional value created through investment and tax optimization as well as the impact of our loss ratio improvement actions. Our annualized run rate currently stands at around $235 million.

Moving now to the balance sheet, it was another volatile quarter for capital markets as equity suffered further losses and interest rates continued to rise amid global economic uncertainty. That being said, our balance sheet is well positioned to absorb these impacts and our book value per share was down only 2% since last quarter. This reflects the high-quality nature of our portfolio as well as a gradual de-risking of our investment portfolio and pension plans. In the current environment, we remain underweight equities compared to our long-term target asset allocation.

Our total capital margin at Q3 remained strong at $2.5 billion. This includes capital that will be used to repay in part our U.S. senior notes of USD 275 million maturing today. Our adjusted debt to total capital ratio at quarter end, after allowing for the net impact of today's debt repayment, is 21%, slightly higher than at Q2 and our long-term target, but it reflects the impact of recent market movements. Shortly after quarter end, we further de-risked our Canadian pension plans by purchasing annuities in respect of approximately $400 million of liabilities. We now have annuities covering over 1/3 of our Canadian defined benefit obligations, removing all market and longevity risks from these liabilities.

In the U.K., our pension plans have fared well against -- fared well during the significant market volatility seen recently. At Q3, there remained a healthy accounting surplus of close to $900 million on our balance sheet. The significant increase in interest rates provide an opportunity for us to continue our pension de-risking journey. We are currently evaluating all options, including purchasing annuities.

The strength of our performance over the last 12 months, despite market volatility and elevated CAT losses, has led to an adjusted ROE of 22.5%. When I look at our performance relative to the industry over the first half of 2022, I can see we are well on our way to achieving our outperformance objective of 500 basis points. But the hard work doesn't stop here. We remain focused on continuing to deliver for the remainder of the year and beyond. With the teams and the platform we have in place and the resilience of our earnings potential economic headwinds, I am confident we can continue to create value for our shareholders.

With that, I'll give it back to Shubha.

Shubha Rahman Khan
Vice President of Investor Relations

Thank you, Louis. In order to give everyone a chance to participate in the Q&A, we would ask you to kindly limit yourselves to 2 questions per person. And of course, if there's time at the end, you can certainly requeue for follow-ups.
Joanna, we're ready to take questions now.

Question and Answer

Operator

[Operator Instructions] First question comes from Geoff Kwan at RBC Capital Markets.

Geoffrey Kwan
RBC Capital Markets, Research Division

My first question was, just given what's going with the economic environment and high interest rate, high inflation and whatnot, I get P&C and pretty much most of your business lines are remaining in hard market conditions. Are you seeing any early signs of things like customers reducing insurance coverages or increasing deductibles to lower premiums? Or even from regulators in auto pushing back on rate increase requests?

Charles J. G. Brindamour
CEO & Director

Geoff, thanks for your question. I'd say no, we don't see that. In fact, what we've observed in the past 24 months is little shopping, very strong retention, little shopping. I think the first thing we're looking for here is the new business pipeline driven by traffic and shopping to replenish a bit. And that's the first sign we're looking for. When it comes to coverage at this stage or regulatory behavior, no change in that regard. Very strong relationships with regulators. It's fact-based and not concerned about that at this stage.

Geoffrey Kwan
RBC Capital Markets, Research Division

And just my second question, just the comments you had around auto and the sub-95% combined ratio over the next 12 months. Just wanted to clarify, is that less than 95% adjusting for seasonality over the entire period? Or is it also you expect that for every quarter over that time period? And if I can kind of sneak in a related question, kind of what gives you comfort that you can get that sort of combined ratio performance and not have it be like the kind of roughly 100% combined ratios you had back in 2017/2018 when the physical damage was a key issue?

Charles J. G. Brindamour
CEO & Director

Yes. Part of the answer, Geoff, is that we've been trying to tackle inflation and physical damage since then, and so there's a number of trends that we've been focused on in that regard. But to answer your question directly, sub-95% is the level at which we'll operate the business in the coming 12 months. Seasonality is uneven by quarter. I'd point out that the first quarter tends to be the higher seasonality quarter by roughly 4 points. But the underlying performance in our mind is sub-95%. Why am I confident? Our pricing position is one.

I think we've been on inflation for a number of quarters. Our rate segmentation strategy, same thing. Very robust action from a supply chain point of view, not only based on the practices that we've had historically from a supply chain management, but also because we've cranked up supply chain management initiatives as you might have picked up in our remarks. Then I'd add the fact that we've been very cautious in reserving in the past, for a very long period of time, but in particular in the past 2, 3 years because there were lots of moving pieces.

Our position relative to the industry is very, very clear. The degree of caution is higher. And that gives me very good confidence that we'll operate in that zone for the foreseeable future. Now Patrick, I think you have a very specific lens also on inflation, maybe you can see what you're seeing these days from an inflation point of view and how it feeds into the outlook that we've laid out.

Patrick Barbeau
Executive VP & COO

Sure. And maybe I can give an update on what created the acceleration during Q3 and why, and some of the signs we're seeing that it is tempering in the more recent months. As you'll recall, in prior quarters, we're splitting the claims cost in personal auto in 3 big categories. There's 40% coming from injuries and liability, 30% on car repairs, and 30% of total losses, including death. On the first 40% of injuries, no change from prior quarters. We've seen no inflation on that part, and that's one of the main areas where we're prudent in reserving and we continue to do so on the current accident year. No change on the long tail.

The next bucket, representing another 30% of the claims cost, is repairables. There, the rate of inflation in Q3 was similar to Q2, in the mid-teens. There are a couple of moving pieces. In the remarks we've mentioned the fact that the parts, the availability of parts is now better. That allowed us to catch up on the delayed repairs. It's reduced the pressure on rental on one side, but added a little bit of pressure on labor. Overall, similar rates on that 30%. The main acceleration we've seen in Q3 actually came from the last 30%, which is the settlement of total losses. In this area, the market values were up significantly in Q3 and reached close to 30% compared to Q3 last year.

That being said, when we look at it month-to-month, September and October, we've seen 2 months in a row of sequential decrease in market values in Canada, evidenced both by CPI as well as our internal results. It's very consistent with what we've observed in the U.S. for now 5 months in a row. Overall, no inflation on long tail, mid-teens on repairs, close to 30% on total losses. That's what gives 13% overall impact in Q3. But the signs of decrease in market values, the cost of parts that are stabilizing, and the availability of parts that is improving suggests that inflation has peaked in Q3 but could remain high for a few more quarters.

Charles J. G. Brindamour
CEO & Director

Thanks, Patrick. And I think, Geoff, you want to take a holistic picture here. It's important to keep in mind that frequency is still below long-term levels. And that's why -- that's also why you're seeing that sort of performance. And that reinforces the outlook that we've given for auto. If you step back, I mean for me, there's 4 things that I'm looking at to capitalize on because of inflation. Now inflation is tough for everyone, I get that. I think our job is to make sure that we have a good value prop for our customers and then we protect the business, but then turn our eyes towards the opportunities that this environment drives.

I can point just from an insurance or underwriting point of view towards 4 things. First, this is driving competitors to move on rates and move closer to our rate position, which should improve our ability to grow the business. And we're comfortable growing, because quite frankly, if you look at the underwriting performance of the organization, I think we want more of that. Second, I think that as rate moves, you will likely see shopping increase.

And as our relative market position improves, we should be doing well, and we should leverage the 2 best known brands in the Canadian marketplace, which are Intact Insurance and Belair. Third of all, I expect distribution income to be very healthy because inflation flows through premium. And finally, I do think that this helps support hard market conditions for longer would be my perspective. And these are all factors that in both relative and absolute terms work for us.

If you move away from the underwriting business and the distribution business, this is fueling interest rates moving up. You're seeing what it means from a P&L point of view. Louis I think has been very clear. And this has created de-risking opportunities. Tough environment, no doubt about it, lots of pressure points. If you generate mid-teens operating ROE in this environment, I think it says a lot about the resilience of the platform.

[Technical Difficulty]

I think there are no more questions? Shubha, there must be more questions.

Shubha Rahman Khan
Vice President of Investor Relations

There are. Operator? Operator, we are ready for the next question. Bear with us while we move to the next. Geoff, are you still on the line?

Geoffrey Kwan
RBC Capital Markets, Research Division

Yes. Can you hear me, or…

Charles J. G. Brindamour
CEO & Director

Yes. Good. We're just looking for the operator.

Shubha Rahman Khan
Vice President of Investor Relations

Geoff, if you have a follow-up question, you can ask it now while we wait for the next caller.

Geoffrey Kwan
RBC Capital Markets, Research Division

I did have a question on the subsidence, but I don't know if that's going to get too boring.

Shubha Rahman Khan
Vice President of Investor Relations

Please. It might be better than no sound at all, Geoff.

Geoffrey Kwan
RBC Capital Markets, Research Division

Okay. I guess if there's no questions right now, maybe if I can ask another one just on the subsidence. Just trying to I guess better understand how that kind of gets factored in on pricing. Is it a separate coverage that policyholders have to pay for? And how is the nature of in terms of when you get those claims coming in, how significant could those costs be? Just trying to think about framing it going forward in terms of expectations of how common this is and the potential impact.

Charles J. G. Brindamour
CEO & Director

Ken, maybe you want to pick this up quickly?

Kenneth Anderson
Executive Vice President & CFO of UK and International

Yes, sure. Well, in terms of coverage, Geoff, this is something that is included as part of home coverage. It's not an optional up in cover and not one that can be removed from a regulatory perspective. In terms of its being common or not, I would say it's not common. As Louis outlined, it's really driven by extremely hot and dry conditions that impact on just certain parts of the country in the U.K. And indeed, it was quite a dry and hot summer in the U.K. this year. That leads to that drying out of the soil, which will impact, potentially impact on foundations causing cracks in walls and in foundations potentially as well. In terms of average cost, you're looking at between GBP 10,000 and GBP 20,000 on average in terms of claims cost associated with it.

Charles J. G. Brindamour
CEO & Director

In the meantime, Shubha, I don't know if you, if the Operator is back, but my advice would be to keep the flow going, is that the sell side analysts e-mail questions to Shubha and we will repeat the questions and take them on that basis.

Operator

Your next question will be from Brian Meredith at UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

Great. What's your cyber insurance policy like? No. I guess a couple of questions here. The first, I'm just curious, Charles, going back to personal auto insurance, when you talked about the kind of pricing environment right now, what you're pushing through, what is your assumption going forward from a severity perspective? Are you assuming that the severities are going to stay at these pretty high elevated levels? I mean you're saying that inflation is already starting to come down, or are you assuming there's going to be a moderation in inflation? And perhaps is that one of the reasons you are kind of seeing some elevated underlying loss ratios is because you really hadn't anticipated the level of inflation that we were going to see?

Charles J. G. Brindamour
CEO & Director

Patrick, maybe you want to give your perspective on that. I don't want to unpack every assumption we're making in pricing, but to provide a bit of context, it would be helpful for Brian.

Patrick Barbeau
Executive VP & COO

Yes, Brian. I think Q3 was -- the acceleration in Q3 was higher than what we were anticipating. We had seen at the end of Q2 an acceleration starting in the month of June in particular, so we knew it would be slightly higher in Q3 than it was in Q2. I guess the extra inflation we've seen compared to our expectation in Q3 was largely offset by we were anticipating more increase in frequency during the quarter. And that, in fact, it is stabilizing pretty much over the last 3 quarters.

Going forward, there's a couple of things there. There is the signals we've seen so far on market values, the price of OEM, the availability that should reduce the quarter-over-quarter inflation we get from here. But also, as we get into Q1 and into next year, this is over, the inflation will be measured over the period that is accelerated this year as well. When you compare the rates that are flowing through, the expectation on some continued increase in frequency and our projection overall, we're confident in the sub-95% going forward for the 12 months.

Charles J. G. Brindamour
CEO & Director

Exactly right. I think, Brian, a couple of points that I would like to make. The first thing is, the loss cost assumptions reflected in pricing are indeed loss cost, so as a function of severity, it's one thing. Frequency is the other thing, and then how your mix is actually shifting. All that go into the result. And despite the bump in Q3, I feel like our pricing assumptions are in very good shape given the current environment. The second thing I want to point out, and I made that point in my remarks, and I think it's an important point, is there is caution when we look at the current accident year.

In other words, we're not reflecting the full benefit of the drop in frequency in longtail lines of business. Why? Because we want to be very prudent in relationship with the loss cost in longtail lines of business. So far, so good. The environment has been quite muted, thanks to in part the work we've been doing on this front, thanks to the in-house legal work, but also thanks to the reforms that regulators have put in place in the past few years. Now we're prudent.

That's how we operate. It is baked into current accident year performance. In my mind, one should not look at our results, ignore PYD, because PYD is a reflection of the prudence we've had in the past few years. And as a result, I think you need to look at both together. Well, you can do what you want, but I'm certainly looking at the combination of both when I look at the underlying performance at the moment.

Brian Robert Meredith
UBS Investment Bank, Research Division

Makes sense. And then, Charles, my second question is, given the hard market we're seeing in commercial insurance in Global Specialty, in Canadian Commercial Lines, and given the level of profitability you are running out, I'm a little surprised at that your premium growth is as low as it is in Canada. And I'm assuming some global specialties going into that. I would have thought that you would see double-digit premium growth, particularly with the economic activity and pricing going on.

Charles J. G. Brindamour
CEO & Director

Yes. I think Darren will give you a perspective of topline and flow. I would say just one thing to keep in mind, Brian, is that we're in year 2 of an integration. And it's normal that in year 2, you have a bit of pressure from your, the second year of the integration. But beyond that, let's talk about the market dynamics and what we're seeing, Darren.

Darren Christopher Godfrey
Executive Vice President of Global Specialty Lines

Thanks, Charles. Brian, when we look at the topline, and I look at it from both the retention and from a new business standpoint, retention is holding relatively strong at very high levels. When I look at the Intact portfolio, roughly around 90%. And same with on the new business side, our buying ratios remain high. Even as we continue to adjust rates relative to the market conditions, the buying ratios remain high. Similar to what we talked about from a personal lines' standpoint, our unit growth is flat. And that's primarily driven through a decrease in completed quotes compared to last year.

As I said, our buying ratios are holding strong. It's very much driven by a lower number of submissions, and it's roughly 30% lower than the pre-pandemic levels. An additional drag I would say in the quarter, and this talks to Charles' point about the integration work that we're doing on the RSA portfolio, we do have a number of profitability actions in play as we integrate the portfolio. While the premium retention on the RSA portfolio is very consistent with historical levels, it is sort of 3 to 4 points lower than what we anticipated when we look at the Intact portfolio.

And I'd highlight 3 things that is impacting that retention. One is, on the SME portfolio, we're taking some very strong rating action due to underlying profitability challenge, so the retention is taking a bit of a hit there. As you well know, our management of earthquake PMLs has been quite evident across the years. And we're applying that same rigor to the mid-market portfolio and really driving higher earthquake deductibles in BC. And then lastly, we exited quite a large program in specialty lines due to some underlying profitability concerns. Each of those 3 things is contributing to a little bit of that topline pressure.

Now as Charles said, from a commercial line standpoint, we are at the tail end of the integration, so we do expect in the coming quarters that we probably will remain largely rate driven in the short term. And then lastly, I would say even though we have some of these short-term pressures, we're really looking to bolster our service levels to make sure that we do capture all the opportunities that are available to us and to making sure that we stay diligent from a rating and from a risk selection. From a market environment standpoint, these comments would apply both across all of our geographies.

Market continues to be quite hard, both in commercial and specialty lines. We are keeping pace and maintaining that strong momentum from a rate standpoint. And in fact, from a Canadian standpoint, we'll look to see probably rates move a little bit higher in Q4, given some of the pressures that we're seeing there. No abatement in terms of the market environment and it's a good market to operate in, and we're comfortable in terms of our expectations of low 90s or better moving forward.

Operator

Next question will be from Jaeme Gloyn at National Bank.

Jaeme Gloyn
National Bank Financial, Inc., Research Division

I wanted to just get a little bit more color on what you're seeing from the reinsurance renewal. Louis, you talked about holding back on CAT guidance as a result of the Jan 1 renewal season. And I just wanted to get a little bit of color or perspective on what you're seeing, what you're thinking perhaps on rates, on capacity for your upcoming year?

Louis Marcotte
Executive VP & CFO

Sure. Well, maybe I'll ask Darren if he wants, he's very close to the file. Darren, do you want to give your perspective?

Darren Christopher Godfrey
Executive Vice President of Global Specialty Lines

Yes. Thanks, Louis. Jaeme, as you well know, the reinsurance market, we're already in a hard market environment in reinsurance, and that very much played out through the first half of this year, primarily driven to the continued reduction in the property CAT capacity. Obviously, reinsurers continue to focus on their own underwriting profitability and ultimately, concerns about trends, including climate.

Now obviously, Hurricane Ian changes that dynamic even further. We believe that the market will harden further in 1/1. From an Intact standpoint, it's too early to say to properly evaluate what that will mean both in terms of reinsurer appetite, pricing and retention impacts. However, we're more than comfortable offsetting any potential increase and/or lack of capacity by optimizing our retention and co-participation while remaining obviously within our own risk appetite. I would, however, highlight 3 things that we think that we're well positioned to navigate through, which will be a tough 1/1 renewal.

First of all, our actions in managing our BC earthquake exposures, obviously including the runoff of CNS. This will reduce our 2023 limit requirements in Canada greatly. Our U.S. CAT limit, where the market pressure actually is the greatest at the moment is in the U.S., and it's relatively small relative to our Canadian and U.K. European limit requirements. And that's very much evident by also if you look at our exposure to Hurricane Ian, which is quite minimal at best.

And then lastly, our CAT program in its entirety has been quite profitable for reinsurers over the years, unlike many cedents in a number of other territories. I think the thing to remember here though, is this just is one of many factors that will continue to drive the hard market well into 2023. And as I talked about on the question there from Brian before, gives us very strong momentum on the rate standpoint into '23.

Charles J. G. Brindamour
CEO & Director

Thanks, Darren. And I think, Jaeme, important to keep in mind also that ceded premium to direct premium here is roughly 10%. I feel like our dependence on reinsurance is, in relative terms, less than many of our peers. And I think given the underlying performance of the business, the exposure management, we're looking at this environment and looking forward to see what the outcome. But in relative terms, we should do well.

Jaeme Gloyn
National Bank Financial, Inc., Research Division

Great. And second question, just on the ROE outlook for the industry. In the slides, you're suggesting high single digits for your industry across all geographies, weighted average. And recent performance has been, or outperformance has been in the 6.5%, 7% plus range on that against the industry. Just your perspectives, thoughts on sustaining that 7% outperformance, or is it something that we should think of more in the traditional 500 basis points range? Where do you land in your comfort of guiding to greater outperformance?

Charles J. G. Brindamour
CEO & Director

Well, Louis, I don't know if you want to provide your perspective, happy to do it as well, but why don't you start?

Louis Marcotte
Executive VP & CFO

Sure. Obviously, we're doing extremely well so far this year. Our performance has been very, very strong. When we look out in the future, there are opportunities, but there are challenges as well. And we do see this reversion towards the high single digits in the overall industry that we try to track. Obviously, we feel confident that 500 we can exceed, but going or committing much higher than that at this point, I think, would be a bit too ambitious, honestly.

For us, maintaining that $500 million in the future is really what we're focused on and eliminating all the elements or obstacles that would impede that kind of outperformance is our key focus. When you hear us talking about some elements that drag ROE and trying to get them removed is really what we're focused on, and that obviously includes the performance of the business.

Charles J. G. Brindamour
CEO & Director

Just to be clear, Louis is right, we're not changing the guidance or the objective on ROE outperformance. Now keep in mind that prudence in reserving from a combined ratio outperformance point of view has been a headwind in the last 2 years. And we're entering in a phase of the market where I do expect combined ratio outperformance to improve. If you're ahead of others from a pricing point of view, if you're ahead of others from a reserving point of view, I do expect that combined ratio outperformance will improve, and that should flow to ROE outperformance.

Operator

Next question will be from Tom MacKinnon at BMO Capital.

Tom MacKinnon
BMO Capital Markets Equity Research

Just to ask another question on personal auto, the 28% of your business that consumes about 95% of the questions. Just in terms of -- for people who say that -- I agree with you that we should be looking at the underwriting loss ratio and adding back any favorable prior year development. But for those who say, things are going to revert with respect to your personal auto book back to 2018, 2019 levels, just as frequency gets back to normal, I guess. If I look back then, you had combined ratios of 198 in personal auto.

And you had, even if you look at the underlying loss ratio and you add back any favorable reserve development, you're at -- that number is like in the 75%, 76% range. And now you're running like lower than that. I think you're running at about 65% to 67% over the last couple of quarters, and you've got a better combined ratio. What is different between now and 2018 and 2019? And what would you tell investors that are concerned that you're going to move back to where you were in 2018 and 2019 with respect to personal auto underwriting profitability?

Charles J. G. Brindamour
CEO & Director

Yes. I think, Tom, the first thing I would say is that if you look at 2018 and 2019, and like those 2, 3 years post 2016, you're looking pretty much at the worst years of the track record. And you will remember, at that time, these were tough moments from a personal automobile performance point of view because in late 2016, early 2017, we realized that there was a steep trend in longtail lines of business. We took at that time a very sharp turn from both a pricing and from a reserving point of view.

And you'll see that in 2018 for instance, we shrank our portfolio by 4% because we moved way ahead of the market and took corrective measures. That's why you've seen that very rarely in our history, but a couple of years of adverse development. This was a very rapid reaction to what we were observing. Things have changed. There have been reforms. There was catchup at that time. We're not pricing at the upper 90s. I think we're just looking at 2 years that were years where inflation had picked up. That led to reforms and pricing actions, et cetera.

I don't think this is a good reference point. Further, we're not pricing at these levels. Obviously, we're trying to be in the zone that we're operating at the moment. And therefore, if one wants to take a look at history, I don't think 2018 and '19 is the reference. I think 2018 and 2019 to me is the exception. And I would say the prudence you've seen on longtail lines in the past 2, 3 years, is precisely to avoid having to react the way we did in '17 and '18.

Tom MacKinnon
BMO Capital Markets Equity Research

That's good. And so you would anticipate that if we were to look at the trend of underlying loss ratio, just adding back the PYD, which is basically coming back to close to the loss ratio, that that trend should continue because you're talking about sub-95 over the next 12 months. And just like you had in the third quarter. Is that the...

Charles J. G. Brindamour
CEO & Director

Yes. I think if you take an underlying performance and you make abstraction of the seasonality you might see in Q1, I'd say that the guidance we've given, which is sub-95, which to me, 93 is very much smack in that. We expect to be in that zone for the next 12 months. Keep in mind, there's seasonality in Q1.

Tom MacKinnon
BMO Capital Markets Equity Research

Okay. And as a follow-up question, there seemed to be some elevated other operating expenses in the quarter, corporate costs and others or something like that. This number seems to be running maybe around 25 or 30 and it was like maybe 45 in the quarter. Is there some sort of anomaly there that happened in the quarter? And how should we be thinking about that number going forward?

Charles J. G. Brindamour
CEO & Director

Louis, why don't you tackle this one?

Louis Marcotte
Executive VP & CFO

Yes, I will. Included in this line in our results now are the central costs. Those are the costs of group individuals who are managing the entire company. We group them together. They are not recharged out to all the businesses. And I would expect those to run in the 20 to 25 quarterly run rate, $1 million quarterly run rate basis. Other than that, there are intercompany adjustments that are booked in that line as well, which basically neutralizes intercompany transactions between the underwriting business and the distribution business. That's purely I will say accounting adjustments, but they do tend to bring a bit of noise to that line quarter-over-quarter.

In this specific quarter, above the run rate that I just mentioned, 2 elements. One is an adjustment for long-term compensation, which is driven by the share price. And so that's been booked in this quarter for about $10-ish million. Those will happen once in a while, and the philosophy behind it for us is the underwriting results should not be penalized if you want because the share price is actually creating a bit of additional comp expense. That's one item here. And the other one is intercompany eliminations. There's a bump-up around $10 million there too for just timing of profit recognition between the underwriting and the distribution business. I think those are 2. One is clearly a one-off, and the other one is something that neutralizes over the year, but they have increased the amount for this quarter.

Tom MacKinnon
BMO Capital Markets Equity Research

Okay, so net-net, it was probably about $10 million or $15 million higher in the quarter than the normal run rate? And that's, I don't know, $0.06 or $0.07. Okay, that's great.

Operator

Next question will be from Paul Holden at CIBC.

Paul David Holden
CIBC Capital Markets, Research Division

I'll just limit myself to one question in the interest of time. Just wondering, given all the dislocations we're seeing in the bond market, if that's opening up some opportunities to accelerate reinvestment of your portfolio, either into higher yielding sovereign or maybe there's some interesting opportunities with credit spreads blowing out as well? Any thoughts there would be helpful.

Charles J. G. Brindamour
CEO & Director

Thanks, Paul. I'll ask Louis to share his perspective, but I understand the interest of time is important. That being said, we had a coverage gap at the start of this call, so I'm happy to take the questions so that we have a proper earnings call. Louis, why don't you pick up that question?

Louis Marcotte
Executive VP & CFO

Yes, absolutely. Of course, there are opportunities with rising rates. What I would take into consideration here, the current reinvestment yield is roughly 200 basis points higher than the book yield. That is something that can be captured. If I were to make an assumption here, because we would not turn the entire portfolio at once, it turns generally over 7 or 8 years. I think a reasonable assumption is 1/8 of the portfolio turning over and then adding it to the current run rate would be one way to see the upside.

If there are opportunities, and here we're careful between the balance of the nonoperating impact of gains and losses from selling a bond at a loss to capture more yield, if we balance that out, the investment team will try to capture as much as they can and they've been very successful in the past here at capturing some of those yields. There is upside clearly in investment income going forward given the conditions we're in right now. And the gap, that 200-basis points gap is very significant. It was reversed at the end of last year you might remember. Clearly, there is tailwind in the investment income line.

Charles J. G. Brindamour
CEO & Director

Yes. But I think to be clear, Paul, we're at the bottom end of our risk appetite, and we're not reaching out for risk in this environment. Even though there might be opportunities there, I think we're running the asset side beyond our long-term asset mix policy. I think we -- it's important for us to protect the capital margin and seek the de-risking opportunities as opposed to reaching for risk on the asset side in this environment.

Paul David Holden
CIBC Capital Markets, Research Division

That's helpful. Charles, you convinced me to ask a second one, so I will. I just want to get a better understanding with the change in premium mix over the last few years, what extent if any let's call it economic sensitivity to your business has changed at all? Sort of throughout surety as an example of a business line that I think is more procyclical and you've, through acquisitions, grown in that line. Maybe address the surety specifically, and if there's any other kind of specialty lines that you would also similarly characterize?

Charles J. G. Brindamour
CEO & Director

Paul, we're out of time. No, just kidding. Darren, do you want to take Paul's question in terms of mix of business?

Darren Christopher Godfrey
Executive Vice President of Global Specialty Lines

Yes, absolutely. Thanks for the question, Paul. One of the things that we've done recently is really look back at the recession in 2008 and look to see both how our portfolio performed, but also how the industry performed. And at that time, we had quite a bit of resilience in our portfolio. And if I compare our portfolio today to back then, it's even further diversified relative to 2008. When we look at topline during the last recession, really wasn't a lot of movement either from a retention or from a new business standpoint.

And similar to the bottom line as well, too. Even with the slower economic activity, we really didn't see a dramatic shift in terms of bottom-line performance. Obviously, from a surety standpoint, there's 2 things at play at the moment. One is very much benefiting from the inflationary environment from a topline standpoint. But obviously, from a reserve and in terms of our current loss ratio picks, consistent with our other lines of business, we're taking a very prudent position, reflecting a little bit of economic headwinds there as well, too.

Generally, I mean the team is an overly conservative group, both north and south of the border, which is exactly what we want to see in our surety team. Managing the economics extremely well. We're quite comfortable in terms of the position that that portfolio is in. Obviously, looking to take advantage of any opportunities that avail themselves, but continue to be quite prudent in terms of the way we're managing our surety book. Beyond surety, not a lot of economic potential headwinds there. You got to think through, obviously, lower economic activity can also turn to lower exposure risk as well too from a casualty standpoint.

There are some pluses and minuses through some economic stresses. But generally, the book is well diversified from a geographic standpoint, well diversified from a product mix and short-term longtail as well too. We're quite comfortable moving forward even if we do feel a little bit of headwind into 2023.

Charles J. G. Brindamour
CEO & Director

Paul, a couple of points. Darren is right. I think that from a CL/SL point of view, very good diversification footprint. But our philosophy, and if you were to look under the hood, we're pushing the mix changes where we feel rate adequacy is the greatest. That's how we manage the business. We know risk-by-risk the extent of the adequacy. Not -- of course, we know the adequacy at the line level, but we manage the business with adequacy in mind at the risk level. And that's where we're focusing to shift the mix within a line of business. In PL, I would say same thing. I mean, we've been managing the mix based on the expected profit per customer.

That is the number one tool that shifts the mix as opposed to one segment versus another. In aggregate, if you look at the home insurance business, which has been transformed in the last decade, this is where the bulk of the PL growth has been coming from. And the performance there has been really strong. We obviously want more of that. In a world where cost of living is going up, we have an offer, Insurance Simplified, through Belair Direct. That's where I do expect to see outsized growth in this environment. Because as shopping picks up, Belair is superbly well positioned to capitalize on this environment. But bottom line, mix for us is one customer at a time, and that's driven by expected profitability, which is measured and used in the field as it is embedded in our systems.

Operator

Next question will be from Lemar Persaud at Cormark.

Lemar Persaud
Cormark Securities Inc., Research Division

Charles, you mentioned that frequency in personal auto is below long-term levels. Can you give us an update on trends and frequency? How far are we from those long-term levels? And do you think we'll ever go back to that long-term average?

Charles J. G. Brindamour
CEO & Director

Patrick, do you want to give your perspective? I think you have your finger on the pulse there, and maybe share your view.

Patrick Barbeau
Executive VP & COO

Sure. The driving levels have been quite stable over now 2 or 3 quarters compared to pre-pandemic. It's pretty much at the pre-pandemic level in terms of amount of driving, number of kilometers. Just slightly below, but fairly stable. Frequency is still below that level, though when we observe -- when we look at behaviors from our telematics tool, we can point to 2 main things that I think we have mentioned to some extent in the past. First, the amount of driving or how it's distributed over time during the week is different than pre-pandemic.

We have less driving being done during morning rush hour, in particular, and more spread throughout the day in particular as well. More driving during the weekend. The other element that might be helping the fact that the frequency is lower than the actual driving level is within our telematics tool, there's 2 big indicators of potential accidents that we measure. One is harsh braking, the other one is fast acceleration. We've seen that both the frequency and the intensity of these indicators have gone down since pre-pandemic, both during rush hour and outside of rush hours. Is that a new norm? Well, it has been quite stable now for a number of months. And in our pricing, we expect that this will probably continue to migrate more towards pre-pandemic level, but we haven't seen much movement over the past 6 months at this point in these behaviors.

Charles J. G. Brindamour
CEO & Director

The stability has been surprising in the past 6 to 9 months. We expected more change let's just say come September or October, and we're just not seeing it. Taking advantage of that for now.

Lemar Persaud
Cormark Securities Inc., Research Division

Great. And then my second question, just sticking with personal auto, I think you guys talked about premium growth benefiting when policy shopping resumes, but I also see in your MD&A here that you're expecting to progress to high single-digit rate increases by year-end. Whereas the industry is only going to move up to the mid-single digits. Then wouldn't premium growth at Intact remain muted under that scenario where you guys are high single-digit increases and the industry is at the mid?

Charles J. G. Brindamour
CEO & Director

Patrick, do you want to give your perspective on that?

Patrick Barbeau
Executive VP & COO

Yes. Well, what we're seeing so far is really the shopping behavior that's hitting our units. Retention is strong. Closing ratio on the quotes we receive is actually quite good. And if we're taking rates at or ahead of the competition, it's really the quote volume that is low at the moment. We think that with the rate increases we're just starting to see and even the rates approved and published in some of our markets that will take effect in the coming months, this should increase the shopping behavior. We will be able to quote more of these clients. We think that we're very well positioned, both from an overall rate level and from a segmentation perspective, to be able to capture that opportunity. And on top of it, our own rate increases will be favorable to topline.

Charles J. G. Brindamour
CEO & Director

Yes. And I think the other phenomenon, if you unpack how to grow business here, is that the marketing team basically earlier in 2021 said, look, there's -- the traffic and the shopping we're seeing is very muted. And as a result, the cost of driving traffic per click and new business is going up in a way where we recommend slowing down our investment. Not a function I think of what the competitivity is today, but I think as traffic picks up, we will increase the marketing machine. And we think that the combination of that and a better competitive position will translate into movement from a topline point of view.

Operator

Next question will be from Mario Mendonca at TD Securities.

Mario Mendonca
TD Securities Equity Research

Charles, in the past -- well, normally, the company talks about ROE performance in the context of relative to the industry. Do you keep or do you have a sort of absolute number in mind as well? I sort of remember you're referring to 15% plus in prior years. Is that still a reasonable number?

Charles J. G. Brindamour
CEO & Director

I think this is. Look, Mario, it's 500 basis points in good time and in bad time, minimum. That's what we're trying to achieve. I think we're operating in a zone where we should be in the mid-teens. I think that's what we're printing at the moment. The AROE is even higher than that. And frankly, I don't see that being meaningfully different. But there are lots of external forces in our industry. And that's why I think maintaining a relative outperformance guidance is the right approach because I don't want to disappoint next year because there's an external force that hits everybody.

The thing though that's important to keep in mind is, we have shown historically that when there's a lot of headwinds in the industry, we're better positioned to absorb the headwind, and we tend to expand the outperformance. When you've seen the industry sub-mid-single digit, we were not in the single-digit zone. We were in the low teens. And for me, I don't want to operate sub that zone even in really, really hard times. But I think the sort of mid-teen performance in the environment in which we operate is definitely where this business should run.

Mario Mendonca
TD Securities Equity Research

Let me try -- let me ask it a slightly different way. And I appreciate your comments, and I understand them. If the company, because of external factors as you say, started to see the ROE drift into the low teens or maybe like 12% or 13%, would you try to manage that ROE higher with capital decisions like buybacks or something else? Or would you just stay…

Charles J. G. Brindamour
CEO & Director

We are ROE driven, Mario. 12%, 13% is not a zone we're comfortable in.

Mario Mendonca
TD Securities Equity Research

You would take action then to address that?

Charles J. G. Brindamour
CEO & Director

Yes, definitely.

Operator

Next question will be from Nigel DeSouza at Veritas Investment Research. I'm sorry, Nigel disconnected. Please proceed.

Charles J. G. Brindamour
CEO & Director

Proceed with? Thank you very much.

Shubha Rahman Khan
Vice President of Investor Relations

Yes. Thank you, everyone, for joining us today. Following the call, a telephone replay will be available for 1 week, and the webcast will be archived on our website for 1 year. A transcript will also be available on our website in the Financial Reports and Filings section. Our 2022 fourth quarter and full year results are scheduled to be released after market close on Tuesday, February 7, with the earnings call starting at 11:00 a.m. Eastern Time on Wednesday, February 8. Thank you again, and this concludes our call for today.

Operator
Thank you. Ladies and gentlemen, this does indeed conclude your conference for today. Once again, thank you for attending. And at this time, we do ask that you please disconnect your lines. Enjoy the rest of your day.