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Earnings Call

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Presentation

Operator

Good morning, ladies and gentlemen. Welcome to the second quarter results teleconference for Travelers. [Operator Instructions] As a reminder, this conference is being recorded on July 20, 2023. At this time, I would like to turn the conference over to Ms. Abbe Goldstein, Senior Vice President of Investor Relations. Ms. Goldstein, you may begin.

Abbe F. Goldstein

Senior Vice President of Investor Relations

Thank you. Good morning, and welcome to Travelers' discussion of our second quarter 2023 results. We released our press release, financial supplement and webcast presentation earlier this morning. All of these materials can be found on our website at travelers.com under the Investors section.

Speaking today will be Alan Schnitzer, Chairman and CEO; Dan Frey, CFO; and our 3 segment Presidents, Greg Toczydlowski of Business Insurance; Jeff Klenk of Bond & Specialty Insurance; and Michael Klein of Personal Insurance. They will discuss the financial results of our business and the current market environment. They will refer to the webcast presentation as they go through prepared remarks, and then we will take questions.

Before I turn the call over to Alan, I'd like to draw your attention to the explanatory note included at the end of the webcast presentation. Our presentation today includes forward-looking statements. The company cautions investors that any forward-looking statement involves risks and uncertainties and is not a guarantee of future performance. Actual results may differ materially from those expressed or implied in the forward-looking statements due to a variety of factors. These factors are described under forward-looking statements in our earnings press release and in our most recent 10-Q and 10-K filed with the SEC. We do not undertake any obligation to update forward-looking statements.

Also in our remarks or responses to questions, we may mention some non-GAAP financial measures. Reconciliations are included in our recent earnings press release, financial supplement and other materials available in the Investors section on our website. And now I'd like to turn the call over to Alan.

Alan David Schnitzer

Chairman & CEO

Thank you, Abbe. Good morning, everyone, and thank you for joining us today. In the face of an historic cat quarter, our top and bottom-line results demonstrate the strength of our franchise and the resilience of our business model.

This quarter, we reported strong underlying results and investment returns as well as net favorable prior year reserve development, which were essentially offset by an historic level of industry-wide catastrophe losses. There were PCS-designated catastrophe events taking place on 88 of the 91 days of the quarter.

Despite pretax catastrophe losses of \$1.5 billion, we generated slightly positive core income for the quarter. We are very pleased with the underlying fundamentals of our business. Pretax underlying underwriting income of \$781 million for the quarter was up nearly 40%, driven by record net earned premiums of \$9.2 billion and a consolidated underlying combined ratio, which improved 1.7 points to an excellent 91.1%. Earned premiums were higher in all 3 of our business segments.

Underlying profitability in our Business Insurance segment was particularly strong. The underlying combined ratio improved by 3 points to an excellent 89.4%. The underlying combined ratio in our Bond & Specialty business was higher year-over-year, but at 87.8%, still generated a very attractive return. In our Personal Insurance segment, the underlying combined ratio improved by 2 points, reflecting the actions we have taken to improve profitability.

Turning to investments. Our high-quality investment portfolio generated net investment income of \$594 million after tax for the quarter, reflecting stronger and reliable returns from our fixed income portfolio, and solid returns from our nonfixed income portfolio. Given our confidence in the strength of our business, we returned \$633 million of excess capital to shareholders during the quarter, including \$400 million of share repurchases.

Turning to production. Thanks once again to excellent execution by our colleagues in the field, we grew net written premiums by \$1.3 billion or 14% to a record \$10.3 billion. In Business Insurance, we grew net written premiums by 18% to \$5.2 billion. Renewal premium change in the segment was a record high at 12.8%, driven by renewal rate change, which accelerated 2.5 points sequentially to 7.2%. The renewal premium change we achieved this quarter was broad-based. RPC was double-digit or near double-digit in every line other than workers' compensation, and it was higher sequentially in every line, including workers' compensation. Even with strong pricing, retention, an important indicator of marketplace stability, remained very strong at 88%. New business increased 36% to \$671 million led by the property line.

In Bond & Specialty Insurance, record net written premiums were about even with the prior year quarter. Retention in our management liability business was an excellent 91% and new business increased 11%. Surety net written premiums were also once again strong. Given the attractive returns, we are very pleased with the strong production results in both of our commercial business segments. The growth we're putting on the books is from geographies, products and distribution partners that we know well.

In Personal Insurance, top line growth of 13% was driven by higher pricing. Renewal premium change was 19.2% in our homeowners and other business and increased to a record high 16.1% in our auto business.

Another quarter of terrific production across the board positions us well for the rest of the year and into 2024. We'll hear more shortly from Greg, Jeff and Michael about our segment results.

Before I turn the call over to Dan, I'd like to spend a few minutes on what Travelers is doing in an important area for us, artificial intelligence. We subscribe to the view that over time, the impact of AI across the economy is going to be profound. So is the opportunity for Travelers. With our perform and transform mindset and our disciplined framework for assessing our investment priorities, we've been focused for years on responsibly developing differentiating AI capabilities across our 3 innovation priorities, extending our lead in risk expertise, providing great experiences for our customers, agents, brokers and employees and optimizing productivity and efficiency.

Between our colleagues who are dedicated to AI specifically and others in enabling disciplines, we have a very significant number of our employees engaged on the objective of making sure that we're leading when it comes to AI.

As we've shared before, and as you can see on Slide 23 of the webcast presentation, for some time, we've been steadily increasing our technology spend. This year, we'll spend more than \$1.5 billion on technology. As the slide demonstrates, we've also been improving the strategic mix of our tech spend. That includes a meaningful increase in investments to develop or acquire cutting-edge AI capabilities built on modern cloud technology. Importantly, we've done all that while significantly improving our expense ratio in no small part, thanks to the success of our technology investments.

The quantity and quality of data are key differentiators when it comes to AI. For more than a decade, we've been investing in data sets, data quality and data accessibility. Between submissions in our commercial businesses and quotes in PI, we intake millions of business opportunities each year. We also take in, adjust and adjudicate millions of claims. As one of the largest risk control organizations in the industry, we provide risk mitigation to our commercial customers, completing more than 100,000 risk control consultations annually. We capture valuable data from virtually all of those interactions.

Our data also include decades of curated institutional knowledge in the forms of policies, procedures, guidelines, forensic investigations and so on. All of that creates an excellent foundation for the next iteration of generative AI.

In addition to our extensive proprietary data, we've been assembling actionable third-party data for years. In fact, we have more than 2,000 data sets from hundreds of third parties. All in, we believe that we have a significant and hard to replicate data advantage. Given the competitive advantages that will come from deploying AI across the insurance value chain, and the expertise, resources and data required to get there, scale will increasingly be a differentiator in our industry as will the ability to execute complex initiatives effectively and efficiently. Expertise, resources, data, scale and execution excellence, all favor Travelers.

The potential use cases for AI and our industry are many and varied. We pursue very focused opportunities that are consistent with our innovation priorities and will create meaningful and sustainable competitive advantages, all with an eye towards leveraging strategic capabilities across our organization.

AI capabilities that we currently have in production span the spectrum from those driving efficiency through automation to more advanced generative AI and large language models. More advanced models augment various aspects of our underwriting, claim handling, service delivery and other work. We use intelligent process automation broadly throughout our business to handle hundreds of routine workflows. Automation and AI have been meaningful drivers of our expense ratio improvement over the past 7 years or so.

A key success driver in insurance is segmenting risk as finely as possible to achieve pricing that is accurately calibrated to the risk. Deep learning models have significantly improved our ability to classify and segment risk in our flow businesses.

For example, in Personal Insurance, we leverage proprietary AI and aerial imagery to assess roof and other site-related conditions at the parcel level. Parcel level risk assessment at scale was practically unimaginable until several years ago. And that type of information is very difficult to obtain from the insured with a reliable degree of accuracy.

In our Select Accounts business, we estimate that AI has improved business classification, a critical underwriting input by more than 30%. In our Middle Market business, we've developed a suite of sophisticated AI models, which facilitate targeted cross-selling, supporting our effort to sell more products to more customers. We're also using AI to better understand our customers and their needs. With this improved customer segmentation, we can better align new product development and generate insights that improve the customer experience, enhancing our industry-leading analytics using machine learning models to deliver sophisticated actuarial insights and to loss cost trends in development, which improve our already strong pricing and product monitoring capabilities.

On the most advanced end, we're leveraging generative AI in large language models, and we've been doing so for several years. For example, in our Bond & Specialty business, our proprietary large language models have processed hundreds of thousands of broker submissions as we work toward improving intake time from hours to minutes. This will improve our responsiveness to our customers and distribution partners and contribute to our productivity.

In our claim organization, a proprietary large language model ingests legal complaints filed against our insureds and then highlights key liability and coverage issues, assist in routing the cases to the best suited defense counsel and provides risk-related insights that can be incorporated back into our underwriting process.

We've also developed and are piloting a Traveler's claim knowledge assistant, a generative AI tool trained on many thousands of pages of proprietary technical source material that was previously only accessible through thousands of different documents. The model provides claim professionals with the ability to easily access accurate actionable information on technical and procedural claim matters, increasing speed, accuracy and consistency in various workflows, including in interactions with our customers and distribution partners.

So in terms of AI, we're investing with speed and strategic direction, consistent with our stated objective of delivering industry-leading returns. I've only shared some of what's in flight, and the capabilities that

we've developed are in various phases of adoption. The full impact of the capabilities we're developing and others on our road map are still ahead of us.

To sum things up, we are very confident in the outlook for our business. We have terrific underlying fundamentals in our commercial businesses, improving underlying results in our Personal Insurance business and steadily rising investment returns in our fixed income portfolio.

As you've heard, we're also investing in impactful new capabilities to advance our ambitious innovation agenda. With that momentum and the best talent in the industry, we are well positioned to continue to deliver meaningful shareholder value over time. And with that, I'm pleased to turn the call over to Dan.

Daniel Stephen Frey

Executive VP & CFO

Thank you, Alan. We're pleased to have generated record levels of earned premium this quarter and an underlying combined ratio of 91.1% and a 170 basis point improvement from last year's strong results. This led to a very strong underlying underwriting gain of \$615 million after tax, up \$171 million or 39% from the prior year quarter.

The expense ratio for the second quarter improved 40 basis points from last year to 28.6%. Once again, benefiting from the combination of our focus on productivity and efficiency, coupled with strong top line growth.

As Alan mentioned, the industry experienced a very active cat quarter and our second quarter results include \$1.5 billion of pretax catastrophe losses, our second largest ever cat amount for a second quarter. As disclosed in the significant events table in our 10-Q, we had 6 events surpass the \$100 million mark in Q2, the most ever for a single quarter since we began disclosing the table in 2013.

Turning to prior year reserve development, we had total net favorable development of \$60 million pretax. In Business Insurance, net unfavorable PYD of \$101 million was the result of better-than-expected loss experience in workers' comp across a number of accident years, being more than offset by an increase in some of our other casualty reserves as well as for runoff operations.

In Bond & Specialty, net favorable PYD of \$119 million was driven by better-than-expected results in management liability and surety. Personal Insurance had \$42 million of net favorable PYD driven by homeowners and other. After-tax net investment income of \$594 million was in line with the prior year quarter. Fixed maturity NII was again higher than the prior year quarter reflecting both the benefit of higher average yields and higher invested assets.

Returns in the nonfixed income portfolio were solid, but as expected, were not as strong as the double-digit yield we experienced in the prior year quarter.

With interest rates having moved higher during the second quarter, we are raising our outlook for fixed income NII, including earnings from short-term securities by \$35 million after tax for the back half of the year. We now expect approximately \$570 million after tax in the third quarter and \$595 million after tax in the fourth quarter. New money rates as of June 30 are about 140 basis points higher than what's embedded in the portfolio, so fixed income NII should continue to improve as the portfolio gradually turns over and continues to grow.

Turning to capital management. Operating cash flows for the quarter of \$1.5 billion were again very strong. All our capital ratios were at or better than target levels, and we ended the quarter with holding company liquidity of approximately \$2 billion. In late May, we issued \$750 million of 30-year debt in order to maintain the debt-to-capital ratio in line with our target range as our premium volume has continued to grow.

Interest rates increased and spreads widened during the quarter, and as a result, our net unrealized investment loss increased from \$3.9 billion after tax at March 31 to \$4.6 billion after tax at June 30. As we've discussed in prior quarters, the changes in unrealized investment gains and losses generally do not impact how we manage our investment portfolio. We generally hold fixed income investments to maturity,

the quality of our fixed income portfolio remains very high and changes in unrealized gains and losses have little impact on our cash flows, statutory surplus or regulatory capital requirements.

Adjusted book value per share, which excludes net unrealized investment gains and losses was \$115.45 at quarter end, up 1% from year-end and up 3% from a year ago. We returned \$633 million of capital to our shareholders this quarter, comprising share repurchases of \$400 million and dividends of \$233 million. We have approximately \$6.2 billion of capacity remaining under the share repurchase authorization from our Board of Directors.

Since the significant level of cat losses in late June resulted in lower earnings for the quarter than we had anticipated, we expect the level of share repurchases over the back half of the year to be lower than the level of share repurchases in the first half of the year.

Turning to the topic of reinsurance. Page 20 of the webcast presentation shows a summary of our July 1 reinsurance placements. While we did see some meaningful price increases on our reinsurance renewals, those increases were broadly in line with the price increases we are obtaining on the direct property premiums we're writing. So there's little or no impact expected on margins.

Let me take another moment to highlight a few items on Page 20. First, we renewed our main cat reinsurance program at terms that were generally consistent with the expiring program. Second, we increased the coverage under our Northeast Property Treaty by fully placing the \$850 million layer above the attachment point of \$2.5 billion. A year ago, we placed \$750 million of that \$850 million layer and the attachment point was \$2.25 billion. This treaty remains pretty far out on the tail for us.

Finally, as part of our ongoing management of tail-risk exposure for the enterprise and in response to inflation-driven growth and insured values in our Personal Insurance property book, we added a new hurricane cat excess-of-loss reinsurance program specific to Personal Insurance coastal exposure, providing 50% coverage for the \$1 billion layer above an attachment point of \$1.75 billion, again, far out on the tail. Any margin impact from this new program will be de minimis, given both the size of our PI property book and the level of price increases we are obtaining on that book.

To sum up the quarter, our ability to absorb \$1.5 billion of pretax cat losses and still report slightly positive core income for the quarter is a testament to the overall strength of our franchise and the underlying fundamentals of our business. Q2 was another quarter of double-digit premium growth, improved underlying profitability and further improvement in our outlook for fixed income NII, all of which bodes well for our future returns. With that, I'll turn the call over to Greg for a discussion of Business Insurance.

Gregory Cheshire Toczydlowski

Executive VP & President of Business Insurance

Thanks, Dan. Business Insurance produced \$402 million of segment income for the second quarter, down from the prior year quarter driven by prior year reserve development and higher cats, as Dan mentioned. Underlying underwriting results continue to be exceptional with underlying underwriting income up more than 50% from the prior year quarter.

We're once again particularly pleased with the quarter's underlying combined ratio of 89.4% which improved by 3 points from the prior year quarter. The loss ratio benefited from property losses that were about 1.5 points better than our expectations for the current year quarter. The loss ratio also improved due to earned pricing. The expense ratio remained strong at 30.1%.

Net written premiums increased 18% to a quarterly record of \$5.2 billion, driven by renewal premium change of 12.8%, retention of 88% and new business of \$671 million, all record highs. Underneath RPC, renewal rate change accelerated sequentially from the first quarter by 2.5 points to 7.2%. We're thrilled with these production results and the superior execution by our field team in the marketplace.

In terms of pricing, we're pleased with our response to the persistent environmental headwinds in both the property and liability lines. In each of our product lines, renewal premium change was higher than the first quarter. And beyond pricing, we continue to improve terms and conditions to ensure we're achieving an appropriate risk/reward trade-off on the business we write.

As we always say, we execute in a granular manner, deal by deal, class by class. And to that point, we're thrilled with our execution demonstrated by a record retention of 88% on our very high-quality book of business and a rate that is thoughtfully segmented by return profile.

New business as a percentage of the book returned to pre-pandemic levels, led by the property line. We're pleased with new business dollars at an all-time high. And as always, when it comes to new business, we remain focused on risk selection, underwriting, terms and conditions and pricing. We're also very pleased with the impact that our strategic investments are having on our production results.

As for the individual businesses, in select, renewal premium change was up 1 point from the first quarter to a strong 10.6% while retention also remained historically high at 84%. New business increased \$30 million or 28% from the prior year quarter driven by the continued success of our BOP 2.0 product.

In Middle Market, renewal premium change was up more than 2 points sequentially from the first quarter to a historically high 10.5% with renewal rate change increasing sequentially by 1.5% to 5.9% and continued strong exposure growth. Retention was once again exceptional at 90% while new business was up 32% from the prior year quarter with increases across all account sizes in most markets.

To sum up, Business Insurance had another strong quarter and continue to execute on the fundamentals to drive profitable growth. With that, I'll turn the call over to Jeff.

Jeffrey Peter Klenk

Executive VP and President of Bond & Specialty Insurance

Thanks, Greg. Bond & Specialty posted strong top and bottom-line results for the quarter. Segment income of \$230 million was up slightly from the very strong prior year quarter. The combined ratio was a terrific 77.1%. The underlying combined ratio was a solid 87.8% for the quarter. A small number of surety losses drove the roughly 4-point increase in the underlying loss ratio year-over-year.

As we've said before, surety losses can be a bit lumpy. Even with the incremental losses this quarter, our returns in the surety line remain excellent.

Turning to the top line. We delivered record net written premiums this quarter. In domestic management liability, we are pleased that we drove record retention of 91% in the quarter, up 2 points sequentially and 3 points from the second quarter of 2022 while continuing to achieve solid renewal premium change. This result reflects our team's deliberate execution to retain our high-quality book of business in light of the very strong returns.

We're also pleased that we increased new business 11% from the prior year quarter. That's a reflection of the strong franchise value we offer to our customers and distribution partners and a lot of hard work by our team in the field. Additionally, we're pleased to report record surety net written premiums in the quarter.

So both top and bottom-line results for Bond & Specialty were once again strong this quarter, driven by our continued underwriting and risk management diligence, excellent execution by our field organization and the benefits from our ongoing strategic investments to extend our market-leading competitive advantages. And now I'll turn the call over to Michael.

Michael Frederick Klein

Executive VP & President of Personal Insurance

Thanks, Jeff, and good morning, everyone. In Personal Insurance, the second quarter segment loss of \$538 million and a combined ratio of 122% were significantly impacted by catastrophes. While it's not unusual for us to have a loss in the second quarter, given it's typically the quarter with the highest weather-related losses, catastrophe losses this quarter for both us and the industry were significantly elevated compared to historical results.

Net written premiums for the quarter grew 13%, driven by double-digit renewal premium change in both domestic automobile and homeowners and other. The underlying combined ratio of 94.1% improved

2 points from the prior year quarter, reflecting an improvement in the underlying combined ratio in homeowners and other, partially offset by an increase in automobile.

In automobile, the second quarter combined ratio was 108.4% with an underlying combined ratio of 103.5%. The underlying combined ratio increased 1.7 points from the prior year quarter due to higher severity driven by increased vehicle replacement and repair costs, and a mix shift from collision only claims towards claims with bodily injury and third-party property damage, which is more consistent with more cars on the road, leading to more multicar accidents. These increases were partially offset by the growing benefit of earned pricing and a lower expense ratio.

While some of the inflationary pressures in auto are beginning to show signs of easing, they are not improving at the rate we expected. Consequently, we're not yet achieving the written rate adequacy levels we had anticipated. While we continue to make progress and expect to get there in the coming quarters, exactly when will depend on a few things. For example, how quickly inflation comes down, how quickly we can get additional rate through the regulatory process and our actual loss experience.

In homeowners and other, the second quarter combined ratio of 135.1% increased 17.1 points due to significantly higher catastrophe losses. The underlying combined ratio of 85.2% improved 5.1 points, primarily driven by non-cat weather losses that were lower than in the prior year quarter. Non-cat weather losses in the quarter were also better than our expectations as more events reached our catastrophe threshold.

Turning to production. Our results continue to demonstrate disciplined market execution of rate and non-rate actions in both lines as we remain focused on improving profitability and managing growth in response to continued inflationary pressures in the environment. In domestic automobile, renewal premium change of 16.1% increased 2.1 points from the first quarter of 2023. We expect renewal premium change to continue to increase from current levels throughout the second half of this year.

In domestic homeowners and other, renewal premium change of 19.2% was broadly consistent with the first quarter. We expect renewal premium change to remain in the high teens through the end of the year.

Before I conclude, I just want to take a minute to thank our claim partners for responding to our customers when it matters most. Behind the aggregate statistics of catastrophe events occurring virtually every day of the quarter, are tens of thousands of individual customers whose homes and vehicles are damaged or destroyed and whose lives are disrupted. In each case, our claim team is responding, helping those customers get their homes repaired and their cars back on the road, continuing to deliver high-quality customer service despite the high volume of claims.

Both the loss environment and the Personal Insurance marketplace remain dynamic. We continue to respond to the changing environment with a steadfast focus on execution, quickly addressing changes in loss experience with targeted pricing, underwriting and other non-rate actions, remaining disciplined in writing business that is consistent with our appetite and making thoughtful and impactful investments for the future. We're confident that the actions we've taken and will continue to take will improve profitability as we move through 2023 and beyond. Now I'll turn the call back over to Abbe.

Abbe F. Goldstein

Senior Vice President of Investor Relations

Thanks, Michael. We're ready to open up for questions.

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Greg Peters of Raymond James.

Charles Gregory Peters

Raymond James & Associates, Inc., Research Division

I guess notwithstanding Michael's comments, I -- just curious about if there's going to be any shift in the strategy on property considering what's going on with catastrophe losses. And I'm also trying to triangulate or bridge the difference between personal lines, which clearly was a negative surprise. And I think, Greg, in your comments, you said property actually was a better -- a net gain for you guys relative to expectations. So any broad comments on your views on property in light of the cats and in the different segments, too, please?

Michael Frederick Klein

Executive VP & President of Personal Insurance

Sure. So I can start on the property side, Greg. Certainly, the catastrophe experience in the quarter was significantly worse than prior year and worse than our expectations. In terms of a shift in strategy, what I would say is we continue to execute a series of actions in the property line to manage growth and improve profitability. And again, first and foremost, you see that in the pricing, in the production statistics that we shared with you on the webcast. But beyond that, we're managing terms and conditions, think deductibles, think roof age eligibility, think coverage levels on roof replacement in a variety of actions that we look at very granularly state by state, market by market, account by account.

And then one of the other things we're really encouraged by, Alan mentioned in his discussion around artificial intelligence, is our aerial imagery and artificial intelligence-enabled capability we have there to refine our underwriting and our risk selection. So less a shift in strategy and more a continuation of a really broad array of profit management and profit improvement efforts in the personal lines' property space.

Gregory Cheshire Toczydlowski

Executive VP & President of Business Insurance

And Greg, this is Greg. Just to follow up on the commercial side. So many times, the catastrophes, the split between personal and commercial can be -- that really depends on the concentration of where the catastrophes hit in terms of where commercial businesses are. In terms of your comment, I think your reference in my prepared comments when I was explaining the underlying combined ratio. And I mentioned that property was better than expectation, and that really was non-cat property.

Charles Gregory Peters

Raymond James & Associates, Inc., Research Division

Got it. All right. And then I guess I'll pivot, Greg also during your comments, you talked about reserve development. Maybe spend a minute, don't really touch upon workers' comp, but the adverse development in the other lines.

Daniel Stephen Frey

Executive VP & CFO

Greg, it's Dan Frey. I'll take the PYD comment. So in the quarter for Business Insurance, as we said, overall unfavorable \$101 million. Comp continues to be favorable. The comp favorable was very strong this quarter, more than \$250 million of good news. So that leaves us with the other liability lines, including runoff being unfavorable. And that's really led by umbrella, which is sort of the poster child for perpetual core levels of inflation, just compounding and pushing more claims up into the umbrella layer.

But a couple of things to put that in context, I guess, we're making a relatively small adjustment to those liability lines, given the fact that there are more than \$15 billion worth of reserves in those lines. The returns in BI continue to remain excellent. And across the company, I'd just remind us, including the good news coming out of Bond & Specialty, which is also liability-type coverage, we had a net favorable \$60 million for the quarter.

Operator

Your next question comes from the line of David Motemaden of Evercore ISI.

David Kenneth Motemaden

Evercore ISI Institutional Equities, Research Division

I had just a follow-up question just on the adverse prior year development. I guess, what does that do to your view of future loss cost trends. It sounds like some of it is runoff, but also some of it is more business that you're obviously still writing. So I'd be interested in how you've changed your 5.5% to 6% loss trend assumption.

Alan David Schnitzer

Chairman & CEO

Yes. David, it's Alan. Thank you. Two things in response to that. One, I would say that -- I would just point you to the combined ratio and underlying combined in BI in a quarter. And obviously, we think about how prior year development influences that through base year changes, and you can see a pretty solid result. And as we've shared with you before, I always want to just preface this by saying it's a very blunt instrument to try to capture what's going on across billions of dollars of premiums in a single loss trend metric. Every line has its own dynamics and the question usually comes in, in terms of loss trend, but of course, there's base year changes, there's exposure changes. There's other adjustments to loss activity. So always puts and takes in all those measures, but all in, I'd say there really hasn't been much significant change.

And I would go back to a comment that Dan made on \$15-odd billion of reserves, this is a relatively small adjustment, and we're always every quarter looking at all our reserves and sometimes they go up, sometimes they go down, but relatively small. And as Dan said, the returns in BI continue to be exceptional.

David Kenneth Motemaden

Evercore ISI Institutional Equities, Research Division

Got it. And then I guess I should just take that. I mean, it's obviously a very fluid environment. But I guess it would -- fluid macro environment. It would seem that just given the re-acceleration in renewal rate change, the gap between written rate and loss trend has been expanding. I guess, is that the right take? Or is there anything else that I'm missing there? Obviously, we have to take catastrophes into account. But there -- I know Fidelis has come in. I'm just wondering if there's anything else I'm missing on the underlying loss ratio.

Alan David Schnitzer

Chairman & CEO

No. I mean other than -- Greg mentioned in his script that the non-cat property losses came in a little better than we thought. But for the most part, I think the way you size it up is about right.

Daniel Stephen Frey

Executive VP & CFO

Yes. And David, it's Dan. I'll just -- you mentioned Fidelis. I mean we said at the beginning of the year that Fidelis was not going to be big enough to have a meaningful impact on the underlying combined ratio, and that's still the case, including Q2.

Alan David Schnitzer

Chairman & CEO

But I think you got it right, David.

Operator

Your next question comes from the line of Ryan Tunis of Autonomous Research.

Ryan James Tunis

Autonomous Research US LP

So yes, Alan, I hear you that you got \$15 billion of reserves, sometimes they go up, sometimes they go down. But I guess I'd say they don't usually go up by this much in a given quarter, especially when there's so much workers' comp reserve releases. And I mean there's also like a pretty sharp acceleration of pricing. So it does look from the outside, like, I don't know, maybe you guys are seeing something new or you've identified something from a trend perspective. I guess just anything in this review, what have you learned this year that I guess you might not have known a year ago.

Alan David Schnitzer

Chairman & CEO

Let me start, Ryan and then I'll turn it over to Dan but we're squaring triangles and we're doing -- we're applying actuarial analytics to a series of triangles in historical losses and that's really how we're coming up with this. I mean the overwhelming thing that all of us are looking at is higher levels of economic inflation. And so that is no doubt a contributor here.

Daniel Stephen Frey

Executive VP & CFO

Yes, Ryan, the only thing I think I'd add to Alan's comments, which I agree with, we've said, as people have asked over the last several quarters and pricing has continued to be strong for quite a while now, is that sustainable? And here you see it ticking up. And I think we just keep going through the litany of pricing is going to be a reaction to what's your return target and what's happening in the loss environment. So we talk about continued increased frequency and severity of weather losses and you see that certainly this quarter. Headline inflation, social inflation that we said never went away and an uncertain overall macro environment. And so those things continue to factor into our pricing. Those things also get evaluated every quarter and every year in terms of our view of loss trend in prior year reserve development.

So what you're seeing here again across the place, net favorable prior year reserve development, I get the focus on the liability lines. So -- but really, what you're seeing there is a degree of difference as opposed to some surprise. We've been talking about inflation for a long time, and we were the first people to be talking about social inflation and never thought that one anywhere. So directionally, it's not a surprise. It's just an adjustment to the order of magnitude.

Ryan James Tunis

Autonomous Research US LP

Got it. And then for Michael and maybe, Greg, I guess on the cat front, I mean you guys were highlighting frequency of events, but it seems like to me that severity must be at least as big of a contributor. Maybe, I guess, talk about -- yes, in other words, I don't think I would have ever expected \$1 billion of personal lines [indiscernible] with 6 PCS events. So from a severity perspective, like how -- what's weighing on is here? Is it like the size of the hail, in other words, like the nature of the weather? Or how much of it is elevated repair cost, demand surge like that type of thing?

Michael Frederick Klein

Executive VP & President of Personal Insurance

Sure, Ryan, it's Michael. Yes, all of that. So I think your point is a good one. So if you look at the quarter, I think the number of events, PCS-designated events was 19, that is above the long-term average. So

there's a frequency of events that's higher. And that's a relatively high number for Q2. But actually, the majority of it really is severity.

Now some of that severity, to your point, is the underlying weather activity itself. I think on average, the events in this second quarter impacted about 8 states a piece as opposed to 6 states a piece. So they were a little broader and more all-encompassing than again, historical averages. So you've got the number of events and then the size and magnitude.

There certainly are -- there's anecdotal evidence of more severe larger hail, those types of things. But the other item that you mentioned, it really is as big, if not a bigger factor than sort of the frequency and the magnitude of the events, and that's just insured values and cost to repair and the severity pressures that we've been talking about across both auto and property and frankly, any first-party coverage is that, that we offer as an organization, really exacerbating that.

So I think it's all of those things, but it's at least as much a severity issue and at least as much driven by economic inflation as it is the weather activity itself.

Gregory Cheshire Toczydlowski

Executive VP & President of Business Insurance

And Ryan, from a Business Insurance or a commercial point of view, we weren't immune from some of the same dynamics that Michael just articulated. I think we just have a broader array of products that you get a little more diversification when you add the workers' comp to GL and all the other products on top of that.

Operator

Your next question comes from the line of Alex Scott of Goldman Sachs.

Taylor Alexander Scott

Goldman Sachs Group, Inc., Research Division

First one I had for you is on the Business Insurance underlying loss ratio improvement. I was hoping you could help us unpack it a little in terms of workers' comp versus maybe the other products, certainly, the reserve development is sort of a good indication about healthy things there are on workers' comp, but pricing is down. I mean is that a business line that's helping the underlying improvement year-over-year? Or is it detracting from it? Could you kind of dimension that and help us think through some of the underlying drivers?

Daniel Stephen Frey

Executive VP & CFO

Yes, Alex, it's Dan. We're really -- we don't do profitability by line. We're not going to go into that level of detail. You call out comp, it has been a good line for us. It continues to be a good line for us. But really, the way to think about BI is the blend of the products, and that's the level at which we'll talk about the underlying.

Taylor Alexander Scott

Goldman Sachs Group, Inc., Research Division

Okay. The second question I had is on pricing. There was, I'd say, more re-acceleration in your pricing than we're hearing from, I guess, Marsh earlier today in some of the barometers that are out there and so forth. Anything that's unique around the way you're approaching the market there and could you help dimension at all how much of that re-acceleration of pricing is necessary for the reinsurance costs you mentioned. It sounds like maybe loss cost trend hasn't moved that much. But help us think a little bit about how much of that can help you tread water versus allow more underlying improvement?

Alan David Schnitzer

Chairman & CEO

I think we're going to try to stay away from forecasting margins. And I think it may have been David, who went to this question earlier and just said, renewal premium change is close to 13% and you're saying there's not a lot of movement in loss trend is -- should we take it on face value. I think broadly, the answer is yes. But really, I think what's going on here is there are some headwinds. There's -- reinsurance costs are higher, inflation is higher. We're in a tight labor market, there's weather and so on. So we're reacting to all those things. And on the other hand, after years of pretty good pricing, returns are in a pretty good place. And so hats off to our field organization, they are threading that needle incredibly well. And returns are -- were excellent. And we're pricing to continue to maintain and maybe even improve the returns.

Operator

Your next question comes from the line of Elyse Greenspan of Wells Fargo.

Elyse Beth Greenspan

Wells Fargo Securities, LLC, Research Division

My first question, within BI, the underlying loss ratio improved. When we look at the quarter, right, the improvement year-over-year was about [300] basis points. And I know you guys said that there was 150 basis points from better property results. I think that was 1 point negative last year. So if we're looking year-over-year, is it right to say it was 2.5 points better on property and then the remainder, like 50 basis points is earned rate over trend? Or is there something else going on? And I know that's just kind of looking all in, but something else going on with the margins in the quarter?

Daniel Stephen Frey

Executive VP & CFO

Yes, Elyse, it's Dan. So I think you're thinking about the property piece the right way. And then there's 50 basis points left over and Greg mentioned the continued benefit of earned pricing. That's not the only thing going on in there. As always, there are pluses and minuses. We're trying to call out the main drivers for you. And those are the 2 main drivers. If there was anything else of real significance, I think we do a pretty good job of trying to make sure we include that in the commentary.

Elyse Beth Greenspan

Wells Fargo Securities, LLC, Research Division

And then my second question, the RRC improved a good amount sequentially. It sounds like that was broad-based in property and liability lines. I know this is obviously a bigger quarter for property in terms of business mix. I just want to get a sense of -- just confirm that I'm thinking about that right, that it was more than just property that drove the improvement in the RRC. And how should we think about -- any color you could just give in terms of that RRC as we think about the Q3 and beyond?

Alan David Schnitzer

Chairman & CEO

Are you talking about renewal price change, Elyse? Is that...

Elyse Beth Greenspan

Wells Fargo Securities, LLC, Research Division

Well, I was talking about the renewal rate, but -- renewal rate yes, in BI.

Gregory Cheshire Toczydlowski

Executive VP & President of Business Insurance

Yes, Elyse, you're right. I mean clearly, we had a real strong quarter in terms of both rate and exposure in property, but we also had significant movement across the rest of the portfolio also, again, in both rate and exposure.

Alan David Schnitzer

Chairman & CEO

I'd say, Elyse, if you're asking whether it was broad-based or narrow, I think the answer to that, it was broad-based.

Operator

Your next question comes from the line of Brian Meredith of UBS.

Brian Robert Meredith

UBS Investment Bank, Research Division

A couple here. First for Jeff, I know you talked about the surety losses just being a couple and they can be lumpy. But are we seeing any signs of maybe some pressures in that line from a loss cost perspective, given what's going on with commercial real estate and other things that are happening right now?

Jeffrey Peter Klenk

Executive VP and President of Bond & Specialty Insurance

Brian, it's Jeff. Thanks. I would say that we're watching inflation in materials and labor costs relative to construction. But honestly, really, I think the prepared remarks really summed it up for you, right? We had a couple of losses that drove the underlying loss ratio change. And ultimately, this can be a lumpy line, and we feel really good about our market-leading surety book.

Brian Robert Meredith

UBS Investment Bank, Research Division

The higher interest rates matter also? I mean when you get a big cut -- big jump in financing costs, right, first for contractors and stuff?

Jeffrey Peter Klenk

Executive VP and President of Bond & Specialty Insurance

Sure. The credit availability for our contractors is absolutely an issue. We take that into account with our high credit quality book of business, the way we underwrite this book. We've got a high-quality book of contractors that we focus on there. And so your point is well taken. It's a part of the underwriting process. That's where I'd leave it. Thanks for the question.

Brian Robert Meredith

UBS Investment Bank, Research Division

And then, Michael, I'm just curious, can you talk a little bit about kind of the regulatory environment right now in personal lines. Obviously, some states are getting a little more kind of an even rate, but are we seeing any pushback kind of starting to emerge from certain states as far as the level of rate going through?

Michael Frederick Klein

Executive VP & President of Personal Insurance

Yes, Brian. Thanks for the question. And I think it's an astute observation. As we talk about pretty consistently, we feel pretty good about our relationships with the departments of insurance, we really endeavor to make sure they have all the information necessary to evaluate and improve our rate increase requests. And starting with us, we continue to file for increases that align with our most recent experience and our indicated rate needs. That said, and we're seeing and you're seeing in the headlines, some news about increased scrutiny and/or states considering or proposing changes to the way that they regulate pricing in response to the continued parade of increases necessary to keep up with loss costs and so I'd say on the margins, there's a couple of places where it's getting a little more challenging. But broadly speaking, we have still been able to file and get approved the rate we think we need in response to increased costs.

Operator

Your next question comes from the line of Josh Shanker of Bank of America.

Joshua David Shanker*BofA Securities, Research Division*

Alan, you began the conference call with a preempt on artificial intelligence and analytics. It's been an unusual 3 years in terms of interpreting loss cost trends with the courts being opened and closed during COVID and very wildly changing conditions under loss trend. Is the data quality that you are looking at right now, any less reliable in your mind than you think it normally is? Are we in a state where extra caution needs to be placed on being comfortable with those numbers that you're using for reserving practices?

Alan David Schnitzer*Chairman & CEO*

I would say the answer to that, Josh, is yes. And I think we've said pretty consistently over the last few years that we have been cautious in reflecting that level of uncertainty into the way we think about loss cost and reserves. So I think the answer is yes, and we've been doing exactly that.

Joshua David Shanker*BofA Securities, Research Division*

And I mean, look we're all just throwing shells from the cheap seats a little bit. Can you talk a little bit about some of that -- how you get more conservative or how you -- in a time of uncertainty, how you get better or what you're doing in order to offset the risks associated around with bad data and whatnot?

Alan David Schnitzer*Chairman & CEO*

Yes. It's probably a longer conversation, Josh, we can follow up, but let me just give you one example, and I think we've said this over the last couple of years, if you were just looking at the data, you might have assumed that some aspects of loss trend had improved over the last couple of years and whether that's true in Personal Insurance and you see the lack of negative PYD in personal auto, for example. Or if you look at social inflation, we said as the courts were closed, that data could have been misinterpreted to mean things were getting better. You look at that data and you say, "I don't believe it." And we understand that it's distorted and that there are other things that could be impacting it. And so we're going to do the best we can to try to understand where the uncertainty is coming from and to make sure that we're reflecting our view of uncertainty as we're thinking about either our prior year reserves or managing our current loss pace.

Operator

Your next question comes from the line of Meyer Shields of KBW.

Meyer Shields*Keefe, Bruyette, & Woods, Inc., Research Division*

I want to start with a question on personal lines. Michael mentioned that the deceleration in claim cost inflation wasn't as strong as anticipated. And I was hoping you could give us some color on what I guess, the indicators that you've previously used, what they're suggesting for personal loss cost inflation for the back half of the year?

Michael Frederick Klein*Executive VP & President of Personal Insurance*

Sure, Meyer. I don't know that, that the external indicators that we look at are significantly different than the ones you look at or do have available. What I can say is auto severity has sort of remained stubbornly in the low double digits, and we had not anticipated that it would remain in double-digit territory for this long.

I think the other thing I commented on in my prepared remarks was that we are seeing some signs of easing. The predominant thing I'm talking about there is the Manheim wholesale index. And again, an

update just came out this week on that. And I believe Manheim's estimate now is that used car prices will end 2023 below 2022 levels. But importantly, that's just one element of our loss costs, right? So wholesale car prices impact, retail car prices, which impact our total loss settlement values, which is a portion of our loss costs. I think one of the reasons you continue to see double-digit pressure on severity is continued elevation in repair costs, labor materials, et cetera.

And then again, we've talked about just broad-based severity pressure. I think what we are seeing is some of the potential good news that we're starting to see in the physical damage coverages is being offset a little bit by this shift in mix to more claims with bodily injury and property damage. And so on a mix -- that mix impact impacts those loss costs as well. But again, the short answer is we're still seeing low double-digit trends in auto severity, and we hadn't anticipated that they would last this long.

Meyer Shields

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

Okay. Perfect. That's helpful. A broader question, when we look at, I guess, whether it's possibly changing weather patterns or the mix shift within BI slightly towards property or just inflation pushing more weather losses above the cat threshold. How do you think about sort of the magnitude of coming years, catastrophe load compared to where you've been recently.

Alan David Schnitzer

Chairman & CEO

I'm not sure we're quite ready to talk about that or to certainly give an outlook for that. Obviously, as we start to put our views together for 2024 and beyond, we'll think about the experience that we've had this year and in recent years and other factors, whether that's changes in exposure in our book or other things, and we'll come up with a view that we hope will be sort of thoughtful and appropriate.

Operator

We have time for one more question. Your next question comes from the line of Tracy Benguigui of Barclays.

Tracy Dolin-Benguigui

Barclays Bank PLC, Research Division

My focus these days is on latent liabilities and I appreciate your legal perspective given your background, Alan, and I'm not sure if A.J. is on the call or not. The last quarter, you indulged me by talking about this. And this quarter, I'm wondering if you can indulge me again and talk about PFAS. Sorry, in advance my question is quite meaty. Is PFAS a chemical explicitly excluded from GL like included in a pollution exclusion? And for pre-1986 exposure, does the statute of limitations apply?

Alan David Schnitzer

Chairman & CEO

Tracy, it's hard to answer a question like that without a claim and a policy. So I'm going to avoid that. And we're happy to take this offline with you and talk a little bit more about it if we can do that consistent with Reg FD.

About PFAS, what I would say about that is this issue has now been around for a while. What we know about it is reflected in our reserves. And I'm not sure there's a lot more to say about it at this point.

Tracy Dolin-Benguigui

Barclays Bank PLC, Research Division

Okay. So you said reflecting reserves. So the adverse development you took in the quarter didn't reflect an update to PFAS.

Daniel Stephen Frey

Executive VP & CFO

Didn't say that, Tracy, but we're not going to really go into the drivers. We gave you the big drivers of PYD. We're not going to go into specific coverage issues in PYD.

Operator

There are no further questions at this time. I would like to turn the call over to Ms. Abbe Goldstein.

Abbe F. Goldstein

Senior Vice President of Investor Relations

Thank you very much. We appreciate everyone's time. And as always, if there's any follow-up, please feel free to reach out directly. Thank you.

Operator

This concludes today's conference call. You may now disconnect.

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