S&P Global
Market Intelligence

James River Group Holdings, Ltd. NasdaqGS:JRVR

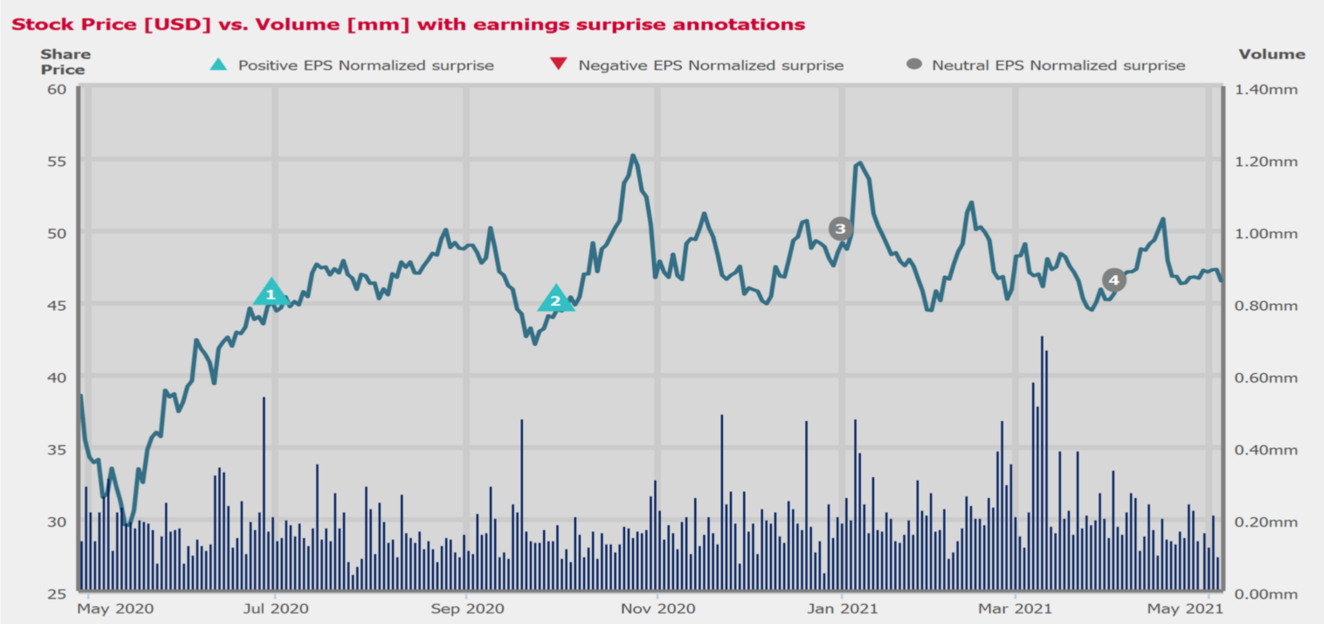
FQ1 2021 Pre Recorded Earnings Call Transcripts

Wednesday, May 05, 2021 8:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ1 2021-			-FQ2 2021-	-FY 2021-	-FY 2022-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.59	(3.54)	NM	0.63	2.56	NA
Revenue (mm)	183.25	182.98	▼(0.15 %)	188.28	765.02	NA

Currency: USD
Consensus as of Apr-16-2021 6:18 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2020	0.46	0.56	▲21.74 %
FQ3 2020	0.50	0.56	▲12.00 %
FQ4 2020	(0.50)	(0.95)	NM
FQ1 2021	0.59	(3.54)	NM

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Call Participants

EXECUTIVES

Frank N. D'Orazio
CEO & Director

Sarah Casey Doran
Chief Financial Officer

Presentation

Operator

Welcome to the James River Group Q1 2021 Earnings Call. My name is John, and I'll be your operator for today's call. [Operator Instructions] Please note, the conference is being recorded.

And I will now turn the call over to Sarah Doran, Chief Financial Officer. Sarah, you may begin.

Sarah Casey Doran
Chief Financial Officer

Thank you, John. Good morning, everyone, and welcome to the James River Group First Quarter 2021 Earnings Conference Call.

During the call, we will be making forward-looking statements. These statements are based on current beliefs, intentions, expectations and assumptions that are subject to various risks and uncertainties, which may cause actual results to differ materially. For a discussion of such risks and uncertainties, please see the cautionary language regarding forward-looking statements in the earnings release and Risk Factors section of our most recent Form 10-K, Form 10-Qs and other reports and filings we made with the Securities and Exchange Commission. We do not undertake any duty to update any forward-looking statements.

I will now turn the call over to Frank D'Orazio, Chief Executive Officer of James River Group.

Frank N. D’Orazio
CEO & Director

Welcome to everyone joining us today, and thank you for listening to our prerecorded earnings call for the first quarter of 2021.

I'm joined today by our CFO, Sarah Doran, who will cover our financial performance for the quarter. But before I hand it over to Sarah, I'd like to share some commentary with you regarding significant actions we've taken during the quarter.

Since joining James River in November of 2020, my primary objectives have been: first, to ensure that the company remains fully focused on the market opportunity we have in front of us, as we continue to strengthen our position as a best-in-class E&S carrier with an expanding fronting and fee income business; and secondly, I've made it my personal goal to be able to eliminate the overhang surrounding our Commercial Auto runoff portfolio. While I intend to share commentary with you in just a few moments about my first objective and the significant accomplishments our underwriting segments have been able to achieve in the first quarter, it's more appropriate that I start with a major step the company took in the quarter to put the concerns with our Commercial Auto runoff portfolio behind us for good.

During the first quarter, we strengthened our prior year reserves by $170 million in our Commercial Auto runoff portfolio. As you might imagine, this decision wasn't taken lightly. We came with the full support of our Board of Directors, so that James River can focus on our thriving prospective business. Admittedly, it is a disappointing outcome after taking a reserve charge for the portfolio in Q4 after we saw emergence in that quarter. The reported losses on this terminated Commercial Auto account meaningfully exceeded our expectations for the 3 months ending March 31, 2021. We had expected that reported losses would decline as the account moved further into runoff, with a continued heavy reported loss emergence in Q1 2021 indicated more inherent severity in the book than anticipated.

In response, we meaningfully adjusted our actuarial methodology, resulting in a significant strengthening of reserves for this account at March 31, 2021. In prior quarters, our actuarial work for this terminated Commercial Auto account have been based on industry data, pricing data, experience data, average claim severity data and blended methodologies. However, the continuation of highly elevated reported losses in the first quarter of 2021 led us to conclude that using only our own loss experience and our paid and incurred reserve projections rather than the array of inputs that we had used in prior quarters and giving greater weight to incurred methods would give us a better and more conservative estimate of ultimate losses on this account.

The result in the changed methodology is significant and also an acknowledgment that our recent loss emergence on the portfolio was likely more than what was originally thought to be a COVID-19-impacted catch-up. Our reserves in the portfolio are now stronger than they've been and a proactive step to close this chapter of the company's history. Our total reserves on Commercial Auto are now more significant than when the account went into runoff at 12/31/2019.

Our held reserves today consist of 42% IBNR, with 60% of the claims in the runoff portfolio that existed at the end of 2019 now closed. Our current net Commercial Auto reserves per open claim have now increased to 150% since the account went into runoff. Additionally, our current net commercial reserve per open claim is more than 40% greater than our average net paid claim on this portfolio in 2021.

As you may recall from our Q4 call, I previously voiced an interest in exploring the potential to reduce tail risk and move to a higher end of the range of outcomes on this portfolio. I believe that many of the structures potentially available on the legacy reinsurance marketplace could require a meaningful risk sharing or co-participation feature, frictional costs and additional premium features as well as a defined limit. I feel very comfortable that our new ultimate reserve levels are likely at similar levels as the legacy market may view.

Before discussing some highlights and metrics from the quarter, I'd like to remind our listeners on the call today that unlike other carriers, the runoff portfolio of James River does not consist of numerous failed underwriting ventures. It consists of one very large account, which has now been in runoff for over 16 months.

Several years ago, we were at the vanguard of underwriting a new sector of the Commercial Auto industry without the benefit of past loss history, promulgated rates or loss triangles, and we got it wrong. My point in all this is that this experience should not define James River, a company with a rich underwriting culture and commitment to excellence. And I look forward to working with the management team to continue to make the company larger, stronger and more profitable in the years to come, my primary objective that I noted at the onset of this call.

And so let me now share with you some of the very positive fundamentals that we experienced in Q1 underlying our ongoing business that demonstrates the company's ability to maximize the current favorable market conditions.

In E&S, the segment's core GWP grew by 35.6% for the quarter. Just as importantly, we also recorded our 17th consecutive quarter of positive rate change at 14.6%, bringing our cumulative compounded rate change to 36.4% since Q1 of 2017. Rate for the quarter eclipsed both our Q4 2020 and full year 2020 figures, a positive sign that the current market conditions have not yet begun to moderate in the markets we serve.

Our submission activity remains robust, and the quote-to-buying ratio in core E&S improved 20% over Q1 2020. The core E&S calendar year reported loss ratio for the quarter remained very attractive at 31.7%, which is very similar to the excellent 30% calendar year reported loss ratio we experienced in all of 2020.

We also continued to benefit from a significant decline in the frequency of claims in this segment. For the last 12 months through to the end of Q1 2021, we've seen an exposure adjusted decline in claims frequency of between 21% and 33%, depending on the exposure metric.

Remember also that our excess property portfolio is managed very conservatively for both tail risk and attritional losses. And as a result, we've had virtually no impact from Winter Storm Uri.

On a combined ratio basis, core E&S produced an 83% for the quarter. This is a reminder of what our overall E&S segment is capable of from an earnings perspective now that our runoff portfolio has been addressed with certainty. Our core E&S division, which has grown by 86% over the last 2 years, enjoys an industry leadership position in its space and should be approaching a $1 billion segment by the end of 2022, a major milestone for the company.

Our fee-based fronting specialty -- our fee-based fronting business in our Specialty Admitted segment is also beginning to gain significant traction, with 23.6% GWP growth over prior, for the quarter, demonstrating the company's stated commitment to gaining scale in this segment as several of the new programs onboard in 2020 are beginning to get traction. The segment's pipeline remains active as we mine relationships and industry contacts throughout the organization and have begun making conscious efforts to better leverage the significant relationships that wholesale distribution partners already have with our E&S segment.

The segment submission activity increased 39% over Q1 2020, and we also just signed a very significant new fronting opportunity and is forecast to have meaningful positive impact on the segment's 2021 plan. Also notable is the fact that several of our existing programs are starting to show signs of growth, as Workers' Compensation payrolls, revenues and other exposure basis increased as the U.S. economy continues to recover and expand in the wake of COVID-19.

In addition to growing fee income by 21.8% for the quarter, the segment has done an excellent job of navigating COVID dynamics as well as Q1 cat activity and is producing a very attractive 92.3% combined ratio for the quarter.

And finally, our Casualty Reinsurance unit will show growth over the quarter over prior. Much of this is due to an effective date change of a large renewal that moved out of the fourth quarter. The segment continues to focus on margin expansion, and its Q1 positive rate change of 16%, inclusive of underlying primary pricing, is well ahead of the effective rate assumption embedded in its 2021 plan, a very good sign for the health of the current accident year.

Collectively, I believe the company is navigating the current market prudently, growing wisely, capturing rate, syndicating risk where appropriate in servicing our distribution partners and insurers. It is our employee base who capably performs these actions, and our 19-year track record as a top-quartile performer that define James River, not our runoff portfolio.

Our plans for 2021 call for us to continue to profitably grow the company, renewing the commitment to our underwriting culture while continuing to invest in our people, our processes and our technology in an effort to create a larger, more profitable specialty carrier, consistently producing top-tier returns.

With that, I'll turn the call over to Sarah Doran.

Sarah Casey Doran
Chief Financial Officer

Thanks, Frank.

Let me highlight a few of the financial points from the quarter. We reported a net loss of $103.5 million for the quarter, and we had a $108.9 million operating loss for the quarter given the reserve charges previously mentioned.

As we turn the page on our large Commercial Auto account and runoff, our performance for the quarter on a go-forward basis continues to reflect accelerating renewal rate pricing, attractive growth and prudent reserving for the E&S segment, significant scale and acceleration of fee income growth in the Specialty Admitted segment and meaningful expense savings and scale uplift throughout the organization. Market conditions remain very attractive for our business.

Let me highlight a few figures of the profitability and strength of our ongoing franchise. The accident year loss ratio was 64.4% this quarter, slightly down from that of the first quarter of 2020. This is higher than the 63.7% accident year loss ratio we reported for the full year 2020, despite E&S renewal rate increases of 13.7% in 2020 and 14.6% year-to-date. Said a different way, we continue to feel that we are building strength in our largest business and largest block of reserves, core E&S. About 69% of the $684 million of net reserves we have in core E&S is in incurred but not reported reserves. The core block also represents about 45% of the $1.5 billion of the company's full net reserve block.

Moving on to expenses. Our group expense ratio decreased to 28.9% this quarter as compared to 34.2% in the first quarter of last year. The absolute dollar amount of operating expenses was down in each of the 4 segments and decreased about 8% or $4.3 million across the group. We have been working over the last 1.5 years to reduce expenses and gain efficiency.

The expense ratio also benefited from strong growth in lines where we see a significant premium for attractive ceding commissions, such as Excess Casualty in our E&S segment. It also benefited meaningfully from the scale we continue to build in our Specialty Admitted segment. We expect that our expense ratio for the full year to be close to our first quarter results. Bringing the accident year loss and expense ratios together, the accident year combined ratio across the company was 93.3% in the quarter, down from 100% in the first quarter of last year.

Gross premiums written in Excess Casualty continued to increase meaningfully and have increased over 100% year-to-date, as rate increases in that line have either been the highest or amongst the highest across our E&S book. As it is our largest line of business in E&S, it has also pushed the net-to-gross retention ratio in that segment down to about 60% this quarter, which is where it was in the fourth quarter of 2020. That is meaningfully down from the first quarter of last year. We expect the retention ratio in E&S to generally be between 60% to 70%, depending on where throughout the 13 underwriting divisions we experience growth.

And finally, on investments. Net investment income for the quarter was $15 million, roughly on par with NII in the second and third quarters of last year as compared to the first quarter 2020 result of $22.8 million. The decline is due to the reduction in short-term interest rates and the sale of a meaningful portion of our bank loan portfolio during the second quarter of 2020. This quarter, our gross yield was 3%, on par with last quarter.

And with that, I'll hand it back to Frank.

Frank N. D'Orazio
CEO & Director
Thank you, Sarah. And again, many thanks to everyone listening to our prerecorded Q1 2021 earnings call. We will look forward to reporting to you again next quarter. Enjoy the rest of your day.