S&P Capital IQ

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Assurant, Inc. NYSE:AIZ

FQ1 2017 Earnings Call Transcripts

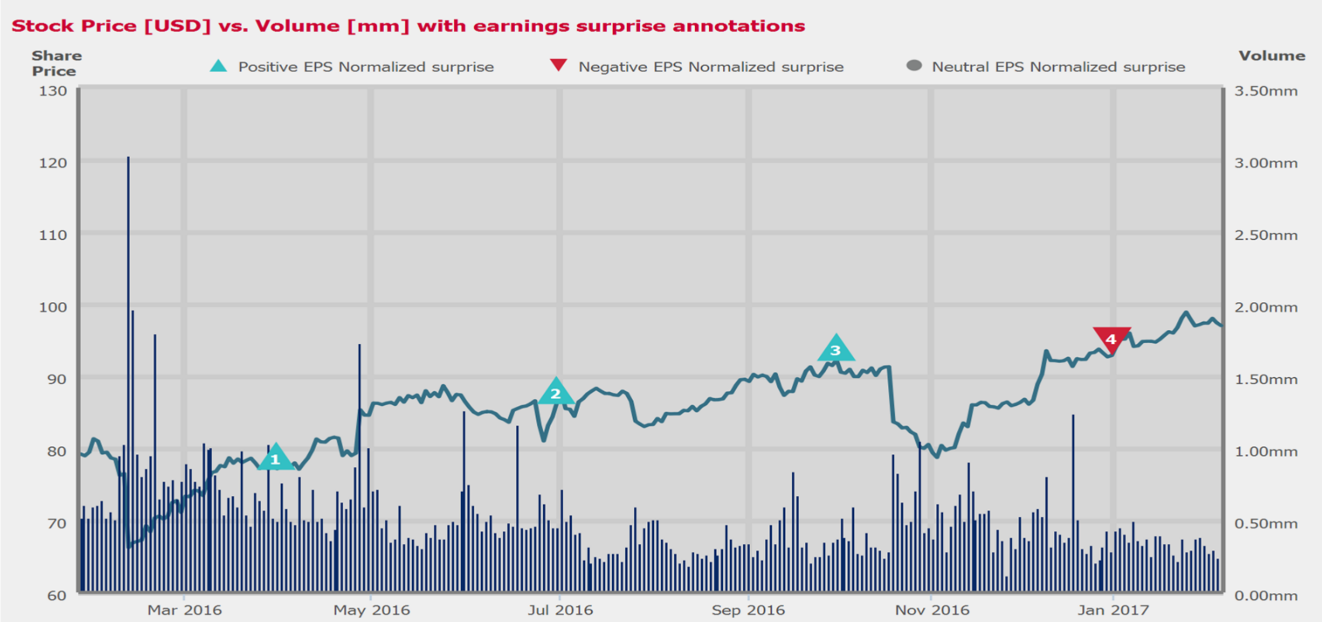
Wednesday, May 03, 2017 12:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2017-			-FQ2 2017-	-FY 2017-	-FY 2018-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.53	1.87	▲22.22	1.58	6.52	7.23
Revenue (mm)	1623.08	1551.50	▼(4.41 %)	1578.87	6391.94	6494.05

Currency: USD

Consensus as of May-03-2017 11:12 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2016	1.21	1.52	▲25.62 %
FQ2 2016	1.35	1.42	▲5.19 %
FQ3 2016	0.98	1.00	▲2.04 %
FQ4 2016	0.53	0.46	▼(13.21 %)

Call Participants

EXECUTIVES

Alan B. Colberg
President, CEO & Director

Francesca Luthi
Executive VP and Chief Communication & Marketing Officer

Richard S. Dziadzio
Executive VP, CFO & Treasurer

ANALYSTS

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

John Matthew Nadel
Crédit Suisse AG, Research Division

Seth M. Weiss
BofA Merrill Lynch, Research Division

Presentation

Operator

Welcome to Assurant's First Quarter 2017 Earnings Conference Call and Webcast. [Operator Instructions] It is now my pleasure to turn the floor over to Francesca Luthi, Chief Communications Officer and Marketing Officer. You may begin.

Francesca Luthi
Executive VP and Chief Communication & Marketing Officer

Thank you, Dan, and good morning, everyone. We look forward to discussing our first quarter 2017 results with you today. Joining me for Assurant's conference call are Alan Colberg, our President and Chief Executive Officer; and Richard Dziadzio, our Chief Financial Officer and Treasurer. Yesterday, after the market closed, we issued a news release announcing our first quarter 2017 results. The release and corresponding financial supplement are available at assurant.com.

As a reminder, beginning in the fourth quarter of 2016, we revised our reportable segments to align with the company's new global operating model. As a result, our reportable segments now comprise Global Housing, Global Lifestyle, Global Preneed and Corporate. Net operating income includes contributions from these 4 reportable segments as well as interest expense. Operating results exclude Health runoff operations, the divested employee benefits and amortization of deferred gains from dispositions and other items that do not represent the ongoing operations of the company. Related prior period results in the financial supplement and in the news release have been revised to conform with the new presentation.

On today's call, we will also refer to other non-GAAP financial measures, which we believe are important in evaluating the company's performance. For more details on these measures, the most comparable GAAP measures and a reconciliation of the 2, please refer to the news release and financial supplement available on assurant.com.

We'll begin the call this morning with prepared remarks before moving to Q&A. Some of the statements made today may be forward-looking and actual results may differ materially from those projected in these statements. Additional information on factors that could cause actual results to differ from those projected can be found in yesterday's news release as well as in our SEC reports, including our Form 10-K.

I will now turn the call over to Alan.

Alan B. Colberg
President, CEO & Director

Thanks, Francesca. Good morning, everyone. Overall, we delivered solid results in the first quarter of this year. Global Lifestyle reported strong earnings, better than we had expected. While segment results were helped by some one-time items in the quarter, we were pleased with our underlying performance. Overall, for Assurant this year, we continue to believe that our total operating earnings, excluding catastrophe losses, will be generally level with 2016 and that operating earnings per share will increase double digits. As we move through 2017, we expect to see continued growth across our targeted areas as well as in vehicle protection.

Our success has been largely driven by our ability to adapt to evolving client and consumer expectations. Extending our competitive advantage will require ongoing investments in our technology infrastructure and other capabilities. Across Assurant, expense management efforts are ongoing and remain central to our culture of continuous improvement. We've identified savings to fund our technology enhancements and moderate the impact from expected declines in lender-placed and legacy businesses.

Overall, though results may vary by quarter, we're confident that growth in our targeted areas, together with expense efficiencies, will enable us to deliver on our commitments for 2017. And importantly, we believe our transformation is solidifying a foundation for profitable growth and ongoing cash flow in 2018 and beyond.

Let me now offer a few updates from the first quarter. In Global Housing, we completed the first client beta implementation of our new lender-placed platform. This represents a milestone for the business. Work began several years ago in partnership with our clients when we saw the opportunity to create greater standardization while providing an even better customer experience. During the course of this year and next, we'll be transferring other clients onto this new platform, enabling us to deliver efficiencies long term as we work to mitigate the impact of lender-placed normalization.

Mortgage solutions posted weaker results for the quarter, driven by softer-than-expected demand. We took action in the quarter to reduce variable expenses and are implementing a number of technology enhancements to strengthen the business and support growth long term. In multifamily housing, year-over-year, we increased our policies enforced by more than 200,000 to nearly 1.6 million.

Turning to Global Lifestyle. First quarter results came in better than anticipated. Overall, we were pleased with the segment's underlying performance, which benefited from higher contributions from service contracts in vehicle protection and Connected Living.

Despite less favorable experience in Europe, our mobile business performed largely as expected. The sustained momentum will continue to focus our efforts on innovation to anticipate both client and consumer needs. As an example, we worked with T-Mobile to launch a new premium device protection plan that now includes AppleCare services. We believe this unique offering makes for a better consumer experience by providing 24/7 priority access to AppleCare services technical support as well as device repair or replacement through Apple. We're proud of our ability to act as a catalyst, bringing together leading companies in the mobile arena to deliver new and compelling offerings.

And as our mobile business continues to ramp up, the wind-down of Assurant Health is now essentially complete. In the first quarter, the runoff of claims was faster than expected, and we collected all outstanding net recoverables related to the 2015 ACA risk mitigation programs. I want to thank the employees and leadership at Health for their tremendous efforts over the last couple of years to ensure a successful wind-down.

Let me now provide an update on our progress as measured by our 3 key financial metrics: net operating income, operating earnings per diluted share and operating return on equity. All metrics exclude reportable catastrophe losses, given the inherent volatility of weather. For the first quarter, net operating income decreased $3 million year-over-year to $106 million, reflecting declines in lender-placed, partially offset by better profitability in extended service contracts and certain one-time items in Global Lifestyle. Operating earnings per diluted share increased 13% to $1.88 for the quarter, driven by share repurchase activity. And finally, annualized operating ROE, excluding AOCI, was 10.8%, up from 10.5% at year-end. Continuing to grow fee-based capital-light offerings will be an important driver of ROE expansion by 2020.

Our balance sheet also remained strong. At the end of March, we had $605 million of holding company capital after returning $135 million to shareholders through dividends and buybacks. Our capital position allows us to continue investing in our businesses, organically and through select acquisitions, while also meeting our commitment to return $1.5 billion to shareholders by the end of this year. Overall, we're encouraged by the progress we are making in our transformation as we build an even stronger Assurant for the future.

I'll now turn the call over to Richard to review segment results for the quarter in greater detail. Richard?

Richard S. Dziadzio
Executive VP, CFO & Treasurer

Thank you, Alan, and good morning. Let's start with a look at Global Housing, which produced earnings of $62 million, down $14 million from the same period last year. The change was primarily driven by declines in lender-placed as well as softer results within mortgage solutions.

The combined ratio for our Global Housing risk-based businesses increased 220 basis points to 82.9%. Lower placement rates in the lender-placed business, as well as higher expenses to onboard new client loans, drove the increase.

The first quarter of 2017 benefited from more favorable loss experience. Reportable catastrophe losses totaled $900,000 pretax, net of $5.2 million of favorable reserve development related to Hurricane Matthew. The pretax margin for our fee-based capital-light businesses decreased 220 basis points to 8.8%. A weaker performance in mortgage solutions coming from softer market conditions, originations and field services, coupled with lower client volumes, contributed to the decline.

As Alan discussed earlier, we are rightsizing expenses in mortgage solutions while, at the same time, implementing technology enhancements to drive additional efficiencies long term. Meanwhile, our multifamily housing business continued to grow profitably, largely through expansion within our affinity channels as well as more favorable loss experience.

Turning to revenue. First quarter net earned premiums and fees in Global Housing decreased 8%, primarily due to lower placement and lower premium rates in our lender-placed insurance business. Our placement rate was 1.96% at the end of the first quarter, down from 2% at year-end. This 4 basis point reduction is consistent with trends seen in prior years.

Now let's move to revenue for our fee-based, capital-light businesses. Multifamily housing increased 11% during the quarter. This reflects double-digit growth in renter's policies sold to our affinity channels and property management network. In mortgage solutions, fee income was down 20%, primarily related to declining volumes in originations and field services discussed earlier.

For 2017, we anticipate continued declines in Global Housing, net earned premiums and earnings, excluding catastrophe losses. The key variables will be the pace of lender-placed normalization and our progress in driving operating efficiencies near term. We expect continued profitable growth in our fee-based, capital-light businesses overall with a focus on improving underlying earnings in mortgage solutions.

Now let's move to Global Lifestyle. The segment's earnings increased by $11 million to $52 million, ahead of our expectations for the quarter. This was largely attributable to $7.5 million after tax of one-time client recoverables within Connected Living and credit and is representative of our ongoing efforts to improve client mix and profitability internationally.

Underlying results were solid across most lines of business. We recorded higher profitability in extended service contracts, resulting from favorable experience, expense savings and a broader shift to OEMs and online channels. Vehicle protection also grew due to prior period sales. Overall earnings growth within Global Lifestyle was partially offset by higher multiple claim costs in Europe, which now have largely been remunerated.

Revenue for the segment decreased by 14%, entirely due to a $137 million reduction in net earned premiums associated with the change in a client program structure implemented late last year. As a reminder, this change also extended our relationship with an important Connected Living client and had no impact on earnings. Excluding this change and the client recoverables, revenues for Global Lifestyle were essentially flat as ongoing declines in legacy businesses were offset by higher volumes of vehicle service contracts and growth in our Canadian credit business. Within mobile, growth in covered devices was offset by lower fee income from mobile repair and logistics services. First quarter of 2016 benefited from strong repair and logistics volumes, driven by the timing of new product launches into the market.

Turning to key performance metrics. The combined ratio for the risk-based businesses, which includes vehicle protection and credit insurance, improved by approximately 240 basis points to 92.2%, driven largely by client recoverables. In addition, we saw favorable loss experience in credit. Going forward, we expect the combined ratio to trend within the long-term range of 96% to 98%.

The pretax margin for the fee-based business, or Connected Living, rose to 7.1% from 4.5% last year, approximately 230 basis points of the increase was driven by client recoverables and change in the client program structure referenced earlier. The balance reflected better underlying results in extended service contracts, partially offset by mobile.

For the full year 2017, we have not changed our expectations for Global Lifestyle overall. We expect segment net operating income to increase from Connected Living, driven primarily by mobile, as we implement new offerings and expand share with existing clients. Higher profitability from the vehicle protection business is also expected to be a driver, along with expense management efforts already underway across Global Lifestyle. All of this is expected to help mitigate declines in legacy businesses. While earnings may fluctuate quarter-to-quarter, depending on volumes, loss experience and other factors, we are confident that the segment will continue to deliver long-term earnings growth of 10% or more on an average annual basis.

Now let's turn to Global Preneed. Earnings increased $4 million to $10 million. But as a reminder, first quarter 2016 results were negatively impacted by $3.9 million coming from an adjustment to reserves and deferred acquisition costs related to an older block of policies. Excluding this adjustment, underlying earnings increased slightly with additional investment income offsetting higher mortality rates. Total revenue for the quarter was up about 3% while new sales increased by 2% year-over-year. In 2017, we continue to expect fee income and earnings to grow in preneed, driven by increased production across North America and operational efficiencies.

Moving to Corporate. The first quarter net operating loss decreased by $4 million to $10 million. This was due in part to reductions in estimated employee-related costs and additional investment income generated from assets transferred to Corporate after the sale of employee benefits. While still early, we continue to expect the Corporate loss to approximate $70 million as we redeploy most savings this year to support our multiyear transformation. These investments include the implementation of a centralized procurement function, along with investments in technology and other key capabilities. Throughout the year, we will update you on our progress as we are committed to reducing Corporate expenses over time.

Moving on to capital. We ended the quarter with approximately $355 million in deployable capital. We upstreamed $43 million of capital to the holding company during the quarter. This included $28 million in dividends from our operating segments and $15 million in capital from Health. For the full year, we continue to expect operating segment dividends to approximate segment earnings and, in addition, to receive approximately $100 million in total from Health and employee benefits as we release residual capital.

During the first quarter, we returned $135 million to shareholders with $105 million returned via share buybacks and the remaining $30 million through common stock dividends. Also, throughout April, we repurchased another $38 million of stock, bringing the total amount returned to shareholders since January 2016 to nearly $1.2 billion.

To summarize, we've continued to make good progress in the first quarter and have delivered solid results. We remain focused on delivering on our commitments to our shareholders for the full year and on driving profitable growth in 2018 and beyond.
And with that, operator, please open the call for questions.

Question and Answer

Operator

[Operator Instructions] Our first question is coming from Seth Weiss with Bank of America Merrill Lynch.

Seth M. Weiss
BofA Merrill Lynch, Research Division

My question is on the mobile business. And if we look at the disclosure around mobile covered devices, it appears flat to year-end. The premium line moves around a little bit because of that program restructure, so I was just curious if you could guide us about the best way to think about top line progression in the mobile business and how we can measure that?

Alan B. Colberg
President, CEO & Director

Yes, certainly, Seth. I mean, first of all, in mobile, I think we felt good about the first quarter. It was in line with what we had expected. As we look to the second quarter and beyond, really 3 things are going on that will continue to drive performance in that business. One is we are expanding with our existing clients. In my prepared remarks, I mentioned the rollout with T-Mobile of AppleCare. We're also in the process of launching premium technical support, which is another fee income service, with some of our clients. Also, later in the year, we expect significant increase in trading activity, both with carrier promotions, but importantly, the new products that are expected -- or is expected later in the year. And then finally, we continue to onboard new clients. Some of which will impact '17. The majority of which are going to impact '18. We actually have a backlog as we implement. And then finally, the mix is shifting. If you think back a few years, traditionally, that business was a premium business, hence, our protection. Now it's heavily also a fee income business, and that just shows up differently in the geography of the P&L. But we feel good about the progress of mobile.

Seth M. Weiss
BofA Merrill Lynch, Research Division

Okay. So the -- we're not going to see a lot of that progression, I guess, within the P&L and the disclosures, if I'm understanding correctly, since only a piece of that comes from onboarding new clients. Is that the right way to think about it?

Alan B. Colberg
President, CEO & Director

What you'll see, we're disclosing a few of the key metrics now, between the number of subscribers, which is more of the premium-based piece of the business and then the number of devices that we process through our facilities. But the important thing to focus on is profit.

Seth M. Weiss
BofA Merrill Lynch, Research Division

Okay, great. And then I'm not sure if you could comment about share buyback. Just considering the amount of excess capital that you have and cash on hand, the first quarter, I guess, was just a little bit light from what I expected. I would expect a little bit more rapid deployment. So if you could just help us think through sort of the pace of bringing that excess capital down.

Richard S. Dziadzio
Executive VP, CFO & Treasurer

Sure. Seth, it's Richard. Just to maybe back up one step. We -- the beginning of 2016, we committed to return $1.5 billion to shareholders by the end of this year. As we get through the end of April, we find ourselves at about -- having returned $1.2 billion, both from share buybacks and dividends. So we're, I would say, sort of well ahead of the -- ahead of the pace that we've put for ourselves. And really, to answer your question more specifically, in terms of the first quarter, typically, in a first quarter, we would be a little bit lighter in things as we see the year evolve and understand how we get through the summer and cat experience at all of that. But we are on track for the $1.5 billion and ahead of the pace.

Operator

[Operator Instructions] Our next question comes from the line of Jimmy Bhullar with JPMorgan.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

So first question on just the mortgage solution business. The results this quarter were weak. Do you view that as an anomaly? Or have your expectations for growth in that business changed at all?

Alan B. Colberg
President, CEO & Director

So let me back up a little context on that business and how we think about it. So we entered these businesses starting about 3 to 4 years ago now, really to leverage our strong client partnerships in the housing space. And our thesis was that we could gain share leveraging our partnerships, and that worked very well in 2015 and into 2016. Really, a couple things happened late last year, early into this year, none of which changed our long-term perspective on the business. One is market demand has gotten softer than anybody had forecasted, really driven by the uncertainty in the economy and uncertainty on interest rate direction. And then as we have been implementing our technology upgrades to really bring these businesses together, we've had some short-term kind of client allocation shifts, but they don't fundamentally change how we think about this. So weaker in the quarter, we're not happy with that. But we took aggressive action as to leadership of that business, and we still feel very good about the longer term for mortgage solutions.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

Okay. And then on the vehicle service business also. You've seen very strong, generally, double-digit growth in that business. This quarter was a little bit of a slowdown. Any color on what happened there?

Richard S. Dziadzio
Executive VP, CFO & Treasurer

Yes -- no, I think from quarter-to-quarter, there could be small movements. But we did have some, as you mentioned, some very strong top line growth. We're attracting new clients and the outlook is still intact for bps to do well for the full year.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

Okay. And just lastly on the share buybacks. I think you have about $540 million remaining in your authorization as of the end of May. Do you expect to complete that this year, by the end of the year because that would put you above your initial targets that you had mentioned for capital deployment?

Alan B. Colberg
President, CEO & Director

Look, Jimmy, let's make sure everyone's clear on what we committed to in capital deployment, which was to return $1.5 billion through both dividends and buybacks. So we have more than enough authorization in place to deliver on our commitment of $1.5 billion.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

So that's what I meant. I was just trying to get a sense if you intend to complete the authorization this year.

Alan B. Colberg
President, CEO & Director

Not going to comment on that. What we do intend to commit is that we will hit that $1.5 billion that we've committed to return to shareholders with authorizations. As appropriate, we'll go back to the Board for additional authorizations. But bottom line, we feel very good about the capital position. We're going to continue to pursue both growth, funding organic growth and select MA, while continuing our long track record of returning capital to shareholders.

Operator

[Operator Instructions] Your next question comes from the line of John Nadel with Crédit Suisse.

John Matthew Nadel
Crédit Suisse AG, Research Division

Just following up on mortgage solutions first. The revenues there were down 20% year-over-year, but I think, if I recall correctly, you actually had an acquisition that should be contributing to that piece of the business, the American Title deal. So if we -- is my recollection, right? And did that contribute this quarter? And if it did, what was the contribution? And how do we think about the revenues on sort of an organic basis there? Because it looks like it slowed down even worse than the 20%.

Richard S. Dziadzio
Executive VP, CFO & Treasurer

John, it's Richard. I'll take that one. Yes, you're referring to the exact -- the acquisition of American Title. And you're right, it added about $10 million to the revenue line. If you could back that out, it would bring down the overall revenues by 33% overall.

John Matthew Nadel
Crédit Suisse AG, Research Division

Okay. And so, Alan, whether it's 20% or 33%, either one sounds very significant. I get that you're saying that nothing that's happened here has really changed your long-term outlook. I guess how do you have that confidence?

Alan B. Colberg
President, CEO & Director

So a couple things. First, we're still bigger than we were when we acquired these companies, even with the disruption that's gone on in the market in the short term, and it really was largely driven in originations, which has been affected by the uncertainty of the economy. I think originations were down in that 33%, 34% type range sequentially. But this business is still small, not material to our overall results and bigger and -- the thesis has worked out until the last couple of quarters, and we don't see anything that would change that. And then as I mentioned in the prepared remarks, we are able to quickly adjust the cost structure in this business so that any problems can be remediated within a quarter or 2.

John Matthew Nadel
Crédit Suisse AG, Research Division

Okay. I mean, that's helpful. So we should be thinking about originations as really, really important driver or data point for this piece of the business.

Alan B. Colberg
President, CEO & Director

Certainly, in part, yes.

John Matthew Nadel
Crédit Suisse AG, Research Division

Yes. And then overall, if I think about the longer-term target, right, fee-based, capital-light within Global Housing, I think you'd indicated at your Investor Day 1.5 years ago or so that that's expected to be about 35% to 40% of the segment's earnings by 2020. It's -- this quarter, and I guess recently, it looks like it sort of a mid-teens contribution. How much in M&A -- when you think about the next couple of years and the driver of the growth in the earnings contribution from this piece, how much in M&A is required to get there versus organic growth?

Alan B. Colberg
President, CEO & Director

We don't assume any M&A is required. We believe we'll achieve it through organic growth in both the multifamily housing and the mortgage solutions businesses.

John Matthew Nadel
Crédit Suisse AG, Research Division

Okay. And then last one, also focusing here in Global Housing. If I do some math on the lender-placed business, it appears -- and I know this isn't perfect, but it appears that the premium rate on the lender-placed is down year-over-year, about 5% to 6%. Is that about right based on what you guys are seeing in the business? And also, as we think about looking forward, how much more pressure should we expect to see on premium rates before you expect that to stabilize, when you think about that normalization of the business?

Alan B. Colberg
President, CEO & Director

So a couple of thoughts there, John. I think the primary driver of our results recently has been the placement rate, and that came down 4 basis points as the housing market continues to recover quarter-on-quarter. What we said on rates, I think, is still very much true, which is we're now normal course. We settled the multistate, and that's behind us. We have some states that approve increases based on our experience, some states that have reductions based on experience, but I wouldn't anticipate any extraordinary trend there.

John Matthew Nadel
Crédit Suisse AG, Research Division

Okay. Is the mid-single-digit decline -- at least on a year-over-year basis, is that about right?

Richard S. Dziadzio
Executive VP, CFO & Treasurer

There're a number of things going on in the lender-placed revenues. As Alan said, its placement rates, which would be the main driver. So it's placement rates, and then obviously, we have some new clients coming in and so forth. So there's offsetting things in there. So it's -- I wouldn't put my finger on one number.

Operator

And we have no further questions in the queue at this time. I will turn the call back to the presenters.

Alan B. Colberg
President, CEO & Director

All right thanks, Dan, and thanks, everyone, for participating in today's call. We look forward to updating you on our progress later this year. Please reach out to Francesca Luthi and Sean Moshier with any follow-up questions.

Thanks, everyone.

Operator

Thank you. This does conclude today's teleconference. Please disconnect your lines at this time, and have a wonderful day.