

The Travelers Companies, Inc.

TRV: Favorable Frequency Helping The Umbrella; Conference Call Round-Up

Equal Weight/\$120

Commercial Lines Insurance

Price Target Change

- Summary.** TRV hosted its Q3 conference call this morning. The call was broad ranging with a focus on commercial lines pricing, loss trends across its segments, and Covid-19 considerations. Our 2020 EPS estimate goes to \$8.85 (from \$9.09) as the Q3 EPS miss and lower NII were partially offset by better Q4 underlying trends. Our 2021 EPS estimate goes to \$9.95 (from \$9.70) and our 2022 EPS estimate goes to \$11.05 (from \$10.45) to reflect more favorable underlying margin trends (mostly in BI) partially offset by lower fixed income NII. Our price target goes to \$120 (from \$115) based on 1.0x our 2021 BV estimate. The TRV shares traded up today (up 5.6% versus the 0.4% rise in the S&P) owing to the favorable pricing and margin outlook relative to expectations.

- Favorable Covid-19 frequency trends in BI and Personal lines.** TRV highlighted that Covid-19 related claims were \$133 million, although favorable frequency trends (mostly in auto and to a lesser extent workers' comp) more than offset the losses and Covid-19 benefitted the overall underlying results by approximately 2 points. TRV also pointed out that YTD frequency trends related to Covid-19 benefited results by approximately 0.5 points, showing that the benefit in the Q3 offset net drags in the earlier quarters of the year. In Business Insurance, TRV saw rate exceed loss trend by around 100 bps and we expect that to continue in Q4 2020 and potentially pick up in 2021 (with rate exceeding 8% and loss trend at 5%). In Bond & Specialty, the underlying loss ratio was elevated for the second consecutive quarter and TRV pointed to loss trends remaining elevated in the Q4. In personal lines, we continue to expect favorable results in auto (although not as strong as Q2/Q3) and are currently modeling 8 points of underlying loss ratio improvement in the Q4 versus 14 points in the Q2 and 12 points in the Q3.

- Pricing getting better in commercial, which is a positive lateral to others.** TRV said that rate is ahead of loss trend but did not want to give a specific pricing outlook given the environment. The company did point to the Covid-19 benefit in BI (a net 50 basis point benefit to the BI margin in the Q3) persisting in the Q4. Further, TRV noted that personal auto results saw lower renewal premium change as it took action around the favorable Covid-19 loss activity. Lastly, TRV said that social inflation in conjunction with elevated cat losses should lead to continued pricing momentum.

- Capital return thoughts unchanged.** When asked about capital return, TRV did not point to a specific level of repurchases but did not close the door on repurchasing shares in the Q4 depending on the economic environment. We are modeling \$150 million of share repurchases in the Q4, down \$300 million estimate previously.

- See inside** for more thoughts from earnings and read-throughs across the space.

Please see page 13 for rating definitions, important disclosures and required analyst certifications. All estimates/forecasts are as of 10/20/20 unless otherwise stated. 10/20/20 19:28:06 ET

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| \$ | 2019A | 2020E | | 2021E | | |
|------------------|--------|-------------|-------|-------------|-------------|-------------|
| EPS | | Curr. | Prior | Curr. | Prior | |
| Q1 (Mar.) | 2.83 | 2.62 | A | NC | 2.94 | 2.75 |
| Q2 (June) | 2.02 | (0.20) | A | NC | 1.64 | 1.47 |
| Q3 (Sep.) | 1.43 | 3.12 | A | NC | 1.96 | 2.10 |
| Q4 (Dec.) | 3.32 | 3.29 | | 3.31 | 3.42 | 3.40 |
| FY | 9.60 | 8.85 | | 9.09 | 9.95 | 9.70 |
| CY | 9.60 | 8.85 | | 9.95 | | |
| FY P/EPS | 12.3x | 13.4x | | 11.9x | | |
| Rev.(MM) | 29,151 | 29,722 | | | 31,291 | |

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile

| Ticker | TRV |
|-------------------------------|---------------------------|
| Price Target/Prior: | \$120/\$115 |
| Price (10/20/2020) | \$118.11 |
| 52-Week Range: | \$76-143 |
| Shares Outstanding: (MM) | 253.2 |
| Market Cap.: (MM) | \$29,905.5 |
| S&P 500: | 3,443.12 |
| Avg. Daily Vol.: | 1,430,180 |
| Dividend/Yield: | \$3.40/2.9% |
| LT Debt: (MM) | \$7,049.0 |
| LT Debt/Total Cap.: | 23.2% |
| ROE: | 5.0% |
| 3-5 Yr. Est. Growth Rate: | 10.0% |
| CY 2020 Est. P/EPS-to-Growth: | 1.3x |
| Last Reporting Date: | 10/20/2020 Before Open |

NC = No Change

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Q3 2020 Earnings And Conference Call Highlights

Summary. The call was broad ranging with a focus on commercial lines pricing, loss trends across its segments, and Covid-19 considerations. TRV highlighted that Covid-19 related claims were \$133 million, although favorable frequency trends (mostly in auto and to a lesser extent workers' comp) more than offset the losses and Covid-19 benefitted the overall underlying results by approximately 2 points. TRV also pointed out that YTD frequency trends related to Covid-19 benefited results by approximately 0.5 points, showing that the benefit in the Q3 offset net drags in the earlier quarters of the year. TRV said that rate is ahead of loss trend but did not want to give a specific pricing outlook, which is not surprising given the fact that they pulled the renewal premium (price plus exposure) guidance earlier this year due to the uncertainty from Covid-19. The company did point to the Covid-19 benefit in BI (a net 50 basis point benefit to the BI margin in the Q3) persisting in the Q4. Our 2020 EPS estimate goes to \$8.85 (from \$9.09) as the Q3 EPS miss and lower NII were partially offset by better Q4 underlying trends. Our 2021 EPS estimate goes to \$9.95 (from \$9.70) and our 2022 EPS estimate goes to \$11.05 (from \$10.45) to reflect more favorable underlying margin trends (mostly in BI) partially offset by lower fixed income NII. Our price target goes to \$120 (from \$115) based on 1.0x our 2021 BV estimate. The TRV shares traded up today (up 5.6% versus the 0.4% rise in the S&P) owing to the favorable pricing and margin outlook relative to expectations.

The Quarter In A Nutshell. This morning (10/20), TRV [reported](#) Q3 core EPS of \$3.12, falling short of our \$3.37, but beating the \$3.03 consensus estimate. TRV's results missed us on higher catastrophe losses and lower prior year reserve development, which offset better investment income and a better underlying margin. NPW rose by 2.7%, better than our estimate for a 0.6% increase, and improving from the 1.4% decline in Q2. TRV did not repurchase shares, in line with our estimate. Net investment income was \$671 million pre-tax, exceeding our \$641 million estimate due to stronger returns from other investments and modestly better results from fixed income portfolio. TRV continues to expect its fixed income investment income to be down \$35-40 million after-tax in Q4, and provided initial guided for a \$420-430 million for each quarter of 2021, versus the \$435-440 million in our model. Book value per share rose by 3.3% and the core ROE was 13.5%. Business Insurance renewal rate change was +8.2%, improving by 80 basis points from +7.4% in the Q2 and +6.0% in the Q1. We had expected about 100 bps of improvement. Exposure growth was -1.9% versus -2.7% in the Q2.

Exhibit 1. Consolidated Results Versus Wells Fargo Securities Estimates

| | Q3 2020 Actual | Q3 2020 Estimate |
|--|----------------|------------------|
| Net premiums written (in millions) | \$7,771 | \$7,613 |
| Growth in net premiums written | 2.7% | 0.6% |
| Growth in net premiums earned | 2.8% | 1.7% |
| Investment income (in millions) | \$671 | \$641 |
| Combined ratio | 94.9% | 93.6% |
| Catastrophe losses (in millions) | \$0 | \$0 |
| Reserve releases (in millions) | \$0 | \$0 |
| Underlying Loss Ratio | 0.0% | 0.0% |
| Expense Ratio | (2.3%) | (0.5%) |
| Underlying combined ratio | (0.2%) | 0.3% |
| Tax rate | 15.9% | 16.5% |
| Operating EPS | \$3.12 | \$3.37 |
| Growth in operating EPS | 117.5% | 135.1% |
| Book value per share | \$109.94 | \$108.93 |
| Segment Underwriting Income (in millions): | | |
| Business Insurance | (\$152) | (\$182) |
| Bond & Specialty Insurance | \$74 | \$72 |
| Personal Insurance | \$363 | \$515 |
| Operating ROE | (0.8%) | 12.5% |

Source: Wells Fargo Securities, LLC estimates and Company reports

2020 Outlook Updated For Lower Investment Income

2020 and 2021 outlook. Exhibit 2 below highlights TRV's commentary and expectations for 2020 and 2021. TRV pulled its outlook in Q1 2020 for renewal premium change and its underlying margins for the remainder of 2020 as a result of the uncertainty associated with the potential impacts associated with Covid-19, but did provide an outlook for net investment income, and also provided helpful color around other line items in the model. TRV's **fixed income** should be down \$35-40 million in the Q4, unchanged from its prior outlook. TRV did not call out any **alternative investment income** trends. Additionally, TRV expects 2021 **fixed income NII** to be in the \$420-430 million range on an after-tax basis in 2021. For **catastrophe losses**, TRV highlighted it exhausted its aggregate cover in the Q3. TRV did not point to a specific level of **share repurchases** but did not close the door on potentially repurchasing shares in the Q4 and we are currently modeling in \$150 million or repurchases. In **Business Insurance**, TRV highlighted about \$91 million of direct covid-19 related losses, although these were more than offset by favorable frequency trends. **Bond and Specialty** saw an elevated loss ratio related to the pandemic and TRV expects the loss trends to remain elevated in the Q4. **Personal lines** results benefited from favorable frequency related to less drivers on the road and we expect this trend to continue in the Q4. TRV said that 8 of the 12 points of improvement in auto was related to favorable frequency. On the **expense ratio**, TRV highlighted that they are comfortable with the expense ratio being around the 30% range, which was the year-to-date level.

Exhibit 2. 2020 And 2021 Outlook Provided By Travelers

| | Provided With Q3 2019 Earnings | 2020 Outlook Provided With Q4 2019 Earnings | Provided With Q1 2020 Earnings | Provided With Q2 2020 Earnings | Provided With Q3 2020 Earnings |
|--|---|--|--|--|--|
| Underlying Margins | | | | | |
| Business Insurance | Margins higher y-o-y for the first three quarters of 2020 | Margins higher for 2020, but weaker in Q1 due to the adjustments taken in Q2-Q4 2019 | | | |
| Bond and Specialty Insurance | Margins broadly consistent y-o-y for the first three quarters of 2020 | Margins broadly consistent over all quarters of 2020 | | | |
| Personal Insurance | Margins higher y-o-y for the first three quarters of 2020 | Underlying combined ratio better in 2020 (in Q2-Q4 due to low non-cat weather) | TRV is not providing an outlook for earned premiums, fee income, claims and claim adjustment expense, and general and administrative expenses for the remainder of 2020 as a result of the uncertainty associated with the potential impacts associated with COVID-19. | | |
| Personal auto | Margins broadly consistent y-o-y for the first three quarters of 2020 | Broadly consistent underlying combined ratio | | | |
| Homeowners' | Margins higher y-o-y for the first three quarters of 2020 | Underlying combined ratio better in 2020 (in Q2-Q4 due to low non-cat weather) | | | |
| Renewal Premium Growth | | | | | |
| Business Insurance | Positive and higher on average y-o-y for first three quarters of 2020 | Positive and higher on average y-o-y for all of 2020 | | | |
| Bond and Specialty Insurance | Management liability: Positive and higher on average y-o-y for first three quarters of 2020 | Management liability: Positive and higher on average y-o-y for all of 2020 | The company expects the decreased economic activity to weigh on premium volumes for 2020. TRV is not providing an outlook for earned premiums, fee income, claims and claim adjustment expense, and general and administrative expenses for the remainder of 2020 as a result of the uncertainty associated with the potential impacts associated with COVID-19. | | |
| Personal auto | Positive but lower on average y-o-y for first three quarters of 2020 | Positive but lower on average y-o-y for all of 2020 | | | |
| Homeowners' | Positive and higher on average y-o-y for first three quarters of 2020 | Positive and higher on average y-o-y for all of 2020 | | | |
| Investment Income (Fixed Income And Short-Term Investments) | | | | | |
| | \$10-\$15 million lower per quarter for the first three quarters of 2020 | \$5-\$10 million lower per quarter for all quarters of 2020 | Approx. \$20 million lower per quarter for the remainder of 2020 and "significantly negative" in Q2 2020. | Approx. \$35-40 million lower per quarter for the remainder of 2020. | Approx. \$35-40 million lower per quarter for the remainder of 2020. For 2021, NII to be between \$420-430 million per quarter |

Source: Wells Fargo Securities, LLC and Company data

Pricing momentum building in commercial lines. In the quarter, Commercial lines pricing continues to firm and picked up with renewal rates up 8.2% in business insurance, improving from 7.4% in the Q2. TRV also noted that it achieved higher rates in all business lines away from workers' comp. Travelers also pointed to higher reinsurance costs as helping to maintain the primary pricing momentum. Further, TRV saw 3% premium growth in the quarter driven by strong new rate change and retention in all three of its segments, with particularly strong growth in homeowners.

Takeaways For The Non-Life Insurance Group

The main takes that stand out from TRV to us and the laterals for the rest of the group are below. Net-net, the biggest take is confirmation in the positive pricing environment and the potential for the P&C group to see a good amount of underlying margin improvement in 2021.

- (1) Commercial lines pricing continues to firm** and picked up in the Q3 with renewal rates up 8.2% in business insurance, improving from 7.4% in the Q2. TRV also noted that it achieved higher rates in all business lines away from workers' comp. Travelers also pointed to higher reinsurance costs as helping to maintain the primary pricing momentum. Further, TRV saw 3% premium growth in the quarter driven by strong new rate change and retention in all three of its segments, with particularly strong growth in homeowners'. **This continued rate firming is positive for the commercial insurers (AIG, CB and HIG) and specifically AIG and CB where workers' comp represent a smaller portion of their book.**
- (2) Underlying margin in Business Insurance benefited from rate exceeding trend.** TRV said that earned rate exceeded loss trend by about one point in Business Insurance, which is positive and a reflection of the strong pricing environment. Further, TRV did not move off of its loss trend assumption of 5%. This could point to strong underlying margins for the group in the Q3, with the potential for greater improvement in 2021 as higher rates are earned in. **This would be a positive as well for the commercial lines insurers, including AIG, CB and HIG.**
- (3) Covid-19 losses were more than offset by favorable frequency trends.** TRV's saw \$133 million of pre-tax losses attributable to Covid-19, of which \$92 million was related to business insurance (driven primarily by workers' com) and \$41 million was related to Bond & Specialty (driven by management liability) this is up from \$114 million in the Q3. However, the company did note that these losses were more than offset by low personal auto losses and from fewer non-Covid-19 related workers' comp and general liability claims due to lower levels of economic activity. The net impact on the underlying margin from Covid-19 was a benefit of 2.0% as compared to 0.5% year-to-date showing the net benefit accelerated in the quarter. **This should also be a benefit to commercial insurers as we expect to see additional Covid-19 related losses for these names but the potential for improved underlying margins from lower claims frequency could help offset ongoing pandemic related losses.**
- (4) Personal auto continues to see favorable benefits from lower miles driven, although the level does appear to be rebounding from Covid-19 lows.** TRV's Personal Auto book saw continued benefits to its margin from lower claims frequency as a result of fewer miles driven. The Personal Auto segment's underlying margin came in at 81%, improving by almost 12 points which primarily reflected favorable frequency in both the current quarter and a catch-up for H1 2020. The company noted that data from its IntelliDrive program indicates that miles driven increased relative to last quarter, but continued to be down from pre-pandemic levels. As such, TRV filed modest rate reductions in a few states during Q3. **This is a positive lateral for the personal auto insurers (ALL and PGR and HIG within its auto business) who should continue to benefit from favorable frequency trends in auto (which is their largest business).**
- (5) Net investment income headwinds should continue into next year, which is included within TRV's guidance.** TRV provided initial commentary on 2021 fixed income related net investment income where it expects to report between \$420-430 million per quarter on an after-tax basis and is below our previous expectation for \$435-440 million per quarter in 2021, which is down around 4% on average when compared to 2020. This guidance is not all that surprising given that 10-year yields remain close to historic lows in the 70-80 basis point range. **We expect the low rate environment to be a headwind to all insurers (life and non-life) as everyone will be impacted by lower interest rates.**
- (6) Repurchases could remain muted for TRV and the group.** TRV did not repurchase shares in either Q3 or Q2, and is continuing to take a more cautious approach around capital management given the impact of the ongoing economic uncertainty. **We expect all insurers, P&C and life, to remain cautious on the buyback front as they look to conservative capital in these uncertain markets.**

Highlights Of Our Estimate Changes

Overview of our estimate changes. Exhibit 4 highlights the changes we made to our earnings model following Q3 2020 earnings. Our 2020 EPS estimate goes to \$8.85 from \$9.09 to reflect the earning miss that was mostly offset by better underlying results in the Q4. Our 2021 EPS estimate goes to \$9.95 from \$9.70 and our 2022 EPS estimate goes to \$11.05 from \$10.45 due to better underlying results that are partially offset by lower fixed income NII. See below for more details on our estimate changes

(1) Weaker net investment income in 2021 and 2022 as TRV guided to fixed income NII being in the \$420-\$430 million range versus our prior estimates that were in the \$435-440 million range.

(2) Loss ratio adjustments in all segments. We lowered our underling loss ratio estimates in Business Insurance to reflect the strong pricing TRV is getting. We raised our underlying loss ratio in Bond and Specialty in Q4 2020 to reflect elevated loss activity associated with the economic slowdown. We lowered our underlying loss ratio in Personal Lines (mainly personal auto) in the Q3 to reflect better frequency trends then we had previously been modeling.

(3) We lowered our share repurchase forecast to \$150 million from \$300 million in the Q4.

Exhibit 4. Summary Of Estimate Changes

| Income Statement | Current | | | Prior Estimates | | | Delta (Absolute) | | |
|---|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|------------------|---------------|----------------|
| | 2020E | 2021E | 2022E | 2020E | 2021E | 2022E | 2020E | 2021E | 2022E |
| Gross premiums written | 31,721.1 | 33,069.0 | 34,554.5 | 31,721.7 | 33,162.2 | 34,647.1 | (0.5) | (93.2) | (92.5) |
| % growth (yr/yr) | 2.1% | 4.2% | 4.5% | 2.1% | 4.5% | 4.5% | (0.0%) | (0.3%) | 0.0% |
| Net premiums written | 29,721.6 | 31,290.7 | 32,825.3 | 29,562.0 | 31,125.3 | 32,654.0 | 159.6 | 165.4 | 171.3 |
| % growth (yr/yr) | 2.0% | 5.3% | 4.9% | 1.4% | 5.3% | 4.9% | 0.5% | (0.0%) | (0.0%) |
| Increase in unearned premiums | (815.6) | (837.4) | (941.0) | (705.0) | (827.7) | (930.8) | (110.6) | (9.7) | (10.2) |
| Net premiums earned | 28,906.0 | 30,453.3 | 31,884.3 | 28,857.0 | 30,297.7 | 31,723.2 | 49.0 | 155.6 | 161.1 |
| % growth (yr/yr) | 2.2% | 5.4% | 4.7% | 2.1% | 5.0% | 4.7% | 0.2% | 0.4% | (0.0%) |
| Net investment income | 2,142.7 | 2,226.9 | 2,229.9 | 2,115.5 | 2,291.9 | 2,317.5 | 27.1 | (65.0) | (87.6) |
| Fee income | 436.0 | 436.0 | 436.0 | 456.0 | 456.0 | 456.0 | (20.0) | (20.0) | (20.0) |
| Other income | 262.0 | 263.0 | 271.0 | 243.0 | 264.0 | 272.0 | 19.0 | (1.0) | (1.0) |
| Total revenue | 31,746.7 | 33,379.2 | 34,821.2 | 31,671.5 | 33,309.6 | 34,768.7 | 75.1 | 69.7 | 52.5 |
| Losses and loss adjustment expenses | 19,492.9 | 20,591.4 | 21,480.8 | 19,349.8 | 20,631.1 | 21,642.3 | 143.1 | (39.7) | (161.5) |
| Amortization of deferred acquisition costs | 4,755.0 | 4,951.5 | 5,184.7 | 4,730.4 | 4,914.8 | 5,146.5 | 24.6 | 36.7 | 38.3 |
| General and administrative expenses | 4,487.0 | 4,568.0 | 4,726.0 | 4,523.0 | 4,625.0 | 4,793.0 | (36.0) | (57.0) | (67.0) |
| Interest expense | 339.8 | 331.3 | 337.3 | 338.9 | 331.3 | 337.3 | 0.8 | 0.0 | 0.0 |
| Total expenses | 29,074.7 | 30,442.1 | 31,728.8 | 28,942.1 | 30,502.1 | 31,919.0 | 132.5 | (60.0) | (190.2) |
| Pretax operating income | 2,672.0 | 2,937.1 | 3,092.4 | 2,729.4 | 2,807.5 | 2,849.7 | (57.4) | 129.6 | 242.6 |
| % growth (yr/yr) | (11.7%) | 9.9% | 5.3% | (9.8%) | 2.9% | 1.5% | (1.9%) | 7.1% | 3.8% |
| Income tax expense/(benefit) | 410.5 | 484.6 | 510.2 | 425.6 | 463.2 | 470.2 | (15.1) | 21.4 | 40.0 |
| After-tax core income | 2,261.5 | 2,452.5 | 2,582.1 | 2,303.9 | 2,344.3 | 2,379.5 | (42.4) | 108.2 | 202.6 |
| % growth (yr/yr) | (10.9%) | 8.4% | 5.3% | (9.2%) | 1.8% | 1.5% | (1.7%) | 6.7% | 3.8% |
| Company income tax rate (%) | 15.4% | 16.5% | 16.5% | 15.6% | 16.5% | 16.5% | (0.2%) | 0.0% | 0.0% |
| Weighted average number of diluted shares | 253.7 | 245.0 | 232.2 | 252.0 | 240.1 | 226.2 | 1.7 | 4.9 | 5.9 |
| Participating share-based awards - allocated income | 15.8 | 16.0 | 16.0 | 14.0 | 16.0 | 16.0 | 1.8 | 0.0 | 0.0 |
| After-tax core income | \$8.85 | \$9.95 | \$11.05 | \$9.09 | \$9.70 | \$10.45 | (\$0.24) | \$0.25 | \$0.61 |
| Profitability Metrics | | | | | | | | | |
| Loss and loss adjustment expense ratio | 66.9% | 67.1% | 66.8% | 66.5% | 67.5% | 67.6% | 0.4% | -0.4% | -0.8% |
| Underwriting expense ratio | 30.0% | 29.3% | 29.1% | 30.1% | 29.5% | 29.3% | -0.1% | -0.2% | -0.2% |
| Combined ratio | 96.9% | 96.4% | 95.9% | 96.5% | 97.0% | 97.0% | 0.3% | -0.6% | -1.1% |
| Points on the combined ratio | 6.2% | 4.4% | 4.4% | 6.0% | 4.4% | 4.4% | 0.2% | 0.0% | 0.0% |
| Points on the combined ratio | -0.7% | 0.4% | 0.2% | -1.6% | -0.1% | -0.1% | 0.9% | 0.5% | 0.3% |
| Current accident year combined ratio | 91.4% | 91.6% | 91.3% | 92.2% | 92.7% | 92.6% | -0.8% | -1.1% | -1.3% |
| Underlying loss ratio | 61.4% | 62.3% | 62.2% | 62.1% | 63.2% | 63.3% | -0.7% | -0.9% | -1.1% |
| Segment Underwriting Income (in millions): | | | | | | | | | |
| Business Insurance | (\$593) | (\$206) | (\$109) | (\$583) | (\$332) | (\$348) | (\$10) | \$126 | \$239 |
| Bond & Specialty Insurance | \$292 | \$449 | \$511 | \$331 | \$471 | \$506 | (\$39) | (\$22) | \$6 |
| Personal Insurance | \$938 | \$569 | \$561 | \$994 | \$478 | \$474 | (\$56) | \$92 | \$87 |
| Book value per share | \$112.38 | \$118.81 | \$126.60 | \$111.39 | \$117.92 | \$125.50 | \$1.00 | \$0.89 | \$1.09 |
| ROE | 8.3% | 8.6% | 9.0% | 8.5% | 8.5% | 8.6% | -0.3% | 0.1% | 0.4% |

Source: Wells Fargo Securities, LLC estimates and Company data

Pricing Accelerating In Commercial Lines

Business Insurance Rating Environment – TRV Rates Increased As Expected, While Exposure Declined

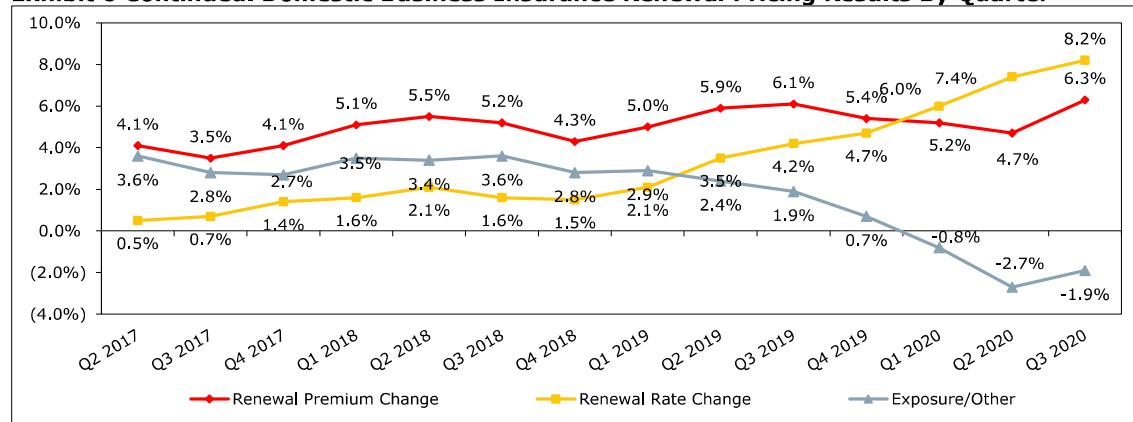
- In the Q3, the *Business Insurance* renewal rate change was +8.2% accelerating 80 bps from the +7.4% in Q2 2020, and the +6.1% in Q1 2020. Exposure growth was -1.9%, better than the -2.7% in Q2 2020 (revised down from -1.8%) and the -0.8% in Q1 (revised up from -1.0%). See Exhibit 5 below, which shows the recent trends in TRV's quarterly domestic Business Insurance (BI) renewal rate change.
- TRV stopped providing forward guidance on its RPC as the company is unsure of how the economy will be impacted from Covid-19. Our assumption is the exposure bucket of the RPC remains negative in the Q4.

Exhibit 5. Domestic Business Insurance Renewal Pricing Results By Quarter

| | Q2 2017 | Q3 2017 | Q4 2017 | Q1 2018 | Q2 2018 | Q3 2018 | Q4 2018 | Q1 2019 | Q2 2019 | Q3 2019 | Q4 2019 | Q1 2020 | Q2 2020 | Q3 2020 |
|------------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| RPC | 4.1% | 3.5% | 4.1% | 5.1% | 5.5% | 5.2% | 4.3% | 5.0% | 5.9% | 6.1% | 5.4% | 5.2% | 4.7% | 6.3% |
| RRC | 0.5% | 0.7% | 1.4% | 1.6% | 2.1% | 1.6% | 1.5% | 2.1% | 3.5% | 4.2% | 4.7% | 6.0% | 7.4% | 8.2% |
| Exposure/other | 3.6% | 2.8% | 2.7% | 3.5% | 3.4% | 3.6% | 2.8% | 2.9% | 2.4% | 1.9% | 0.7% | -0.8% | -2.7% | -1.9% |
| % of BI NPW in Workers' Comp | 26.1% | 26.7% | 25.5% | 29.8% | 24.7% | 24.3% | 23.4% | 28.6% | 23.1% | 23.3% | 22.1% | 26.2% | 20.7% | 20.2% |

Source: Wells Fargo Securities, LLC and Company data

Exhibit 6 Continued. Domestic Business Insurance Renewal Pricing Results By Quarter



Source: Wells Fargo Securities, LLC and Company data

Personal Auto - TRV Continues to Secure Rate, Although The Level Is Slowing

- Within *Personal Insurance*, TRV continues to secure rate increases in auto (but the level is slowing as they pointed to filing for a handful of modest declines in a handful of states during the quarter). The RPC in auto was 1.4% in the Q3 versus 1.7% in Q2, 2.4% in Q1, 3.0% in Q4, 3.8% in Q3, and 4.8% in Q2 2019. Homeowners' pricing did accelerate to 8.2% in the Q3 versus 7.6% in Q2, 7.5% in Q1, 7.3% in Q4 and 6.8% in Q3 2019.
- Travelers saw its new business in auto grow for the ninth consecutive quarter. Auto new business premium was \$257 million in the Q3 versus \$233 million in Q2, \$227 million in Q1, \$224 million in Q4, and \$236 million in the Q3 2019.

Exhibit 7. Personal Insurance Business Statistics

| | Q1 2017 | Q2 2017 | Q3 2017 | Q4 2017 | Q1 2018 | Q2 2018 | Q3 2018 | Q4 2018 | Q1 2019 | Q2 2019 | Q3 2019 | Q4 2019 | Q1 2020 | Q2 2020 | Q3 2020 |
|---------------------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| Agency Automobile | | | | | | | | | | | | | | | |
| Retention | 86% | 86% | 84% | 84% | 83% | 83% | 84% | 84% | 84% | 84% | 84% | 84% | 85% | 85% | 84% |
| Renewal Premium Change | 7.3% | 8.8% | 10.5% | 11.5% | 10.7% | 9.6% | 8.0% | 6.7% | 5.5% | 4.8% | 3.8% | 3.0% | 2.4% | 1.7% | 1.4% |
| Policies-In-Force (PIF, in thousands) | 2,482 | 2,514 | 2,528 | 2,529 | 2,519 | 2,517 | 2,518 | 2,518 | 2,516 | 2,517 | 2,524 | 2,532 | 2,540 | 2,570 | 2,596 |
| PIF Yearly Change | 12% | 11% | 8% | 4% | 1% | 0% | (0%) | (0%) | (0%) | 0% | 0% | 1% | 1% | 2% | 3% |
| PIF Sequential Change | 2% | 1% | 1% | 0% | (0%) | (0%) | 0% | 0% | (0%) | 0% | 0% | 0% | 0% | 1% | 1% |
| New Business (\$ in millions) | \$244 | \$225 | \$214 | \$198 | \$193 | \$212 | \$219 | \$202 | \$206 | \$217 | \$236 | \$224 | \$227 | \$233 | \$257 |
| New Business yearly change | 13% | (3%) | (17%) | (24%) | (21%) | (6%) | 2% | 2% | 7% | 2% | 8% | 11% | 10% | 7% | 9% |
| Agency Homeowners & Other | | | | | | | | | | | | | | | |
| Retention | 87% | 87% | 86% | 87% | 86% | 86% | 86% | 87% | 85% | 86% | 86% | 86% | 87% | 87% | 86% |
| Renewal Premium Change | 2.6% | 2.6% | 2.8% | 3.0% | 3.2% | 3.7% | 3.6% | 3.7% | 5.2% | 6.6% | 6.8% | 7.3% | 7.5% | 7.6% | 8.2% |
| Policies-In-Force (PIF, in thousands) | 4,222 | 4,283 | 4,352 | 4,402 | 4,453 | 4,530 | 4,601 | 4,652 | 4,726 | 4,825 | 4,927 | 5,016 | 5,111 | 5,255 | 5,365 |
| PIF Yearly Change | 4% | 4% | 5% | 4% | 5% | 6% | 6% | 6% | 7% | 7% | 8% | 8% | 9% | 9% | 9% |
| PIF Sequential Change | 1% | 1% | 2% | 0% | 1% | 2% | 1% | 2% | 2% | 2% | 2% | 2% | 3% | 2% | 2% |
| New Business (\$ in millions) | \$118 | \$151 | \$159 | \$125 | \$125 | \$170 | \$173 | \$154 | \$163 | \$215 | \$237 | \$219 | \$212 | \$252 | \$288 |
| New Business yearly change | 17% | 14% | 18% | 9% | 6% | 13% | 9% | 23% | 30% | 26% | 37% | 42% | 30% | 17% | 22% |

Source: Wells Fargo Securities, LLC and Company data

Margins Impacted By Higher Cats And Lower PYD

Underlying Results Beat With Strong Results In Business Insurance And Personal Auto

- The consolidated combined ratio was 94.9%, missing our 93.6% estimate largely reflective of a lower level of favorable reserve releases. Cats of \$397 million were above our \$346 million estimate, while favorable reserve development of \$142 million missed our \$357 million estimate due to a higher level of asbestos strengthening and lower favorable development away from the PG&E benefit. The underlying combined ratio of 91.5% beat our 93.8% estimate, and improved 2.5 bps from last year and included a 2 point benefit from Covid-19. Underlying results beat us in Bond and Specialty and in Business Insurance, but missed us in Personal Insurance.
- Catastrophe losses of \$397 million included the impacts from Hurricane Laura, Tropical Storms Isaias, wind events that impacted the Midwest in August, and several large wildfires in the Western U.S. TRV noted that the increase in cat activity levels was even more pronounced than its catastrophe loss number suggests, as its net results in the Q3 were tempered by recoveries under its aggregate catastrophe XOL treaty. TRV recognized a full recovery under that treaty in its Q3 results with \$233 million pre-tax benefiting the catastrophe line and \$47 million pre-tax benefiting non-cat weather in its underlying results.
- Reserve releases were \$142 million, lower than our \$357 million estimate (which included the previously announced \$403 million of releases due to subrogation benefits from PG&E) due to higher asbestos strengthening (of \$295 million, lower than our \$154 million) and less releases in other lines. Away from PG&E and asbestos there was \$34 million of releases (for personal auto for recent accident years), lower than our \$111 million estimate (due to lack of favorable development within BI away from PG&E).

Exhibit 8. Underlying Combined Ratio – Deterioration In Loss Ratio, But Improvement In Expense Ratio

| | Q3 2017 | Q4 2017 | Q1 2018 | Q2 2018 | Q3 2018 | Q4 2018 | Q1 2019 | Q2 2019 | Q3 2019 | Q4 2019 | Q1 2020 | Q2 2020 | Q3 2020 |
|---|--------------|--------------|--------------|--------------|--------------|---------------|---------------|--------------|--------------|--------------|---------------|---------------|---------------|
| Reported Combined Ratio | 103.2% | 95.5% | 95.5% | 98.1% | 96.6% | 97.5% | 93.7% | 98.4% | 101.5% | 92.4% | 95.5% | 103.7% | 94.9% |
| Catastrophe Losses, net of reinsurance | 10.7% | 7.5% | 5.4% | 7.3% | 3.8% | 8.8% | 2.8% | 5.3% | 3.4% | 1.2% | 4.6% | 12.3% | 5.3% |
| Prior Year Reserve Development (Favorable)/Unfavorable | (0.3%) | (4.4%) | (2.3%) | (2.8%) | (0.2%) | (2.4%) | (0.7%) | (1.8%) | 4.1% | (0.8%) | (0.4%) | (0.0%) | (1.9%) |
| Underlying Combined Ratio | 92.8% | 92.4% | 92.4% | 93.6% | 93.0% | 91.1% | 91.6% | 94.9% | 94.1% | 92.1% | 91.3% | 91.4% | 91.5% |
| Underlying (improvement) deterioration | 0.7% | 0.4% | 0.7% | 0.1% | 0.2% | (1.3%) | (0.8%) | 1.3% | 1.1% | 0.9% | (0.3%) | (3.5%) | (2.5%) |
| Underlying Loss Ratio | 62.4% | 61.7% | 61.8% | 62.9% | 63.3% | 61.6% | 61.9% | 64.7% | 64.5% | 63.0% | 61.3% | 60.4% | 62.2% |
| Change from last year | 2.0% | 0.9% | 0.8% | 0.5% | 0.9% | (0.1%) | 0.1% | 1.8% | 1.3% | 1.3% | (0.6%) | (4.3%) | (2.3%) |
| Underlying Expense Ratio | 30.4% | 30.7% | 30.6% | 30.7% | 29.7% | 29.5% | 29.7% | 30.2% | 29.5% | 29.1% | 30.0% | 31.0% | 29.3% |
| Change from last year | (1.3%) | (0.5%) | (0.1%) | (0.4%) | (0.7%) | (1.2%) | (0.9%) | (0.5%) | (0.2%) | (0.4%) | 0.3% | 0.8% | (0.2%) |

Source: Wells Fargo Securities, LLC and Company data

Exhibit 9. Underlying Combined Ratio By Segment – Deterioration In All Segments

| | Q3 2017 | Q4 2017 | Q1 2018 | Q2 2018 | Q3 2018 | Q4 2018 | Q1 2019 | Q2 2019 | Q3 2019 | Q4 2019 | Q1 2020 | Q2 2020 | Q3 2020 |
|--|--------------|---------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Business Insurance | 96.4% | 93.9% | 95.5% | 96.5% | 95.4% | 95.4% | 95.0% | 97.4% | 95.9% | 96.4% | 97.3% | 97.0% | 94.0% |
| Underlying (improvement) deterioration | 2.3% | 1.1% | 1.1% | 1.7% | (1.0%) | 1.5% | (0.5%) | 0.9% | 0.5% | 1.0% | 2.3% | (0.4%) | (1.8%) |
| Bond & Specialty | 77.7% | 91.1% | 80.7% | 80.5% | 78.3% | 78.1% | 81.1% | 81.0% | 83.6% | 81.3% | 85.7% | 88.1% | 89.0% |
| Underlying (improvement) deterioration | (0.8%) | 9.8% | (1.2%) | (1.5%) | 0.6% | (13.0%) | 0.4% | 0.5% | 5.3% | 3.2% | 4.6% | 7.1% | 5.5% |
| Personal Insurance | 91.0% | 90.4% | 90.5% | 92.6% | 92.9% | 87.8% | 89.1% | 94.6% | 94.0% | 88.4% | 84.0% | 84.0% | 88.7% |
| Underlying (improvement) deterioration | (1.4%) | (3.2%) | 0.4% | (1.9%) | 1.9% | (2.6%) | (1.4%) | 2.0% | 1.1% | 0.5% | (5.1%) | (10.7%) | (5.3%) |
| Personal Insurance: | | | | | | | | | | | | | |
| Agency Automobile | 98.8% | 104.1% | 96.3% | 95.5% | 92.6% | 96.9% | 92.1% | 93.8% | 92.7% | 99.6% | 89.2% | 84.2% | 81.0% |
| Underlying (improvement) deterioration | (2.3%) | (8.1%) | (2.3%) | (6.9%) | (6.2%) | (7.2%) | (4.2%) | (1.7%) | 0.1% | 2.7% | (2.9%) | (9.6%) | (11.7%) |
| Agency Homeowners & Other | 78.1% | 70.2% | 80.2% | 85.2% | 88.5% | 72.5% | 82.6% | 92.9% | 93.5% | 73.6% | 74.9% | 81.4% | 96.4% |
| Underlying (improvement) deterioration | (0.2%) | (0.2%) | 2.6% | 2.4% | 10.4% | 2.3% | 2.4% | 7.7% | 5.0% | 1.1% | (7.7%) | (11.5%) | 3.0% |

Source: Wells Fargo Securities, LLC and Company data

Investment Income And Other

Investment Income Beats Us; Guidance Provided For 2021

- Net investment income was \$671 million pre-tax, better than our \$641 million estimate. Travelers' pre-tax book yield on its investment portfolio was 3.4%, above the 1.4% yield for Q2 2020, due to stronger results from its other investments. Fixed income investments added \$502 million pre-tax, higher than our \$488 million estimate, while alts were \$173 million, also higher than our \$150 million estimate. Short-term investments added \$6 million, just above our \$13 million estimate.
- TRV continues to expect its fixed income investment income to be down \$35-40 million after-tax in Q4, and provided initial guided for \$420-430 million of fixed income investment income after-tax for each quarter of 2021, which represents around a 3% decline when compared to our 2020 estimate.

Capital Management – Likely Muted In The Q4

- TRV did not repurchases shares in the Q3, in line with our estimate. Dividends were \$218 million versus the \$798 million in core earnings. We have lowered our repurchase expectation in the Q4 and now expect TRV to repurchase \$150 million of its shares, down from our previous estimate of \$300 million. Our 2020 capital return estimates have the company returning approximately 61% of its core earnings while our 2021 and 2022 estimates are 99% and 97%, respectively.

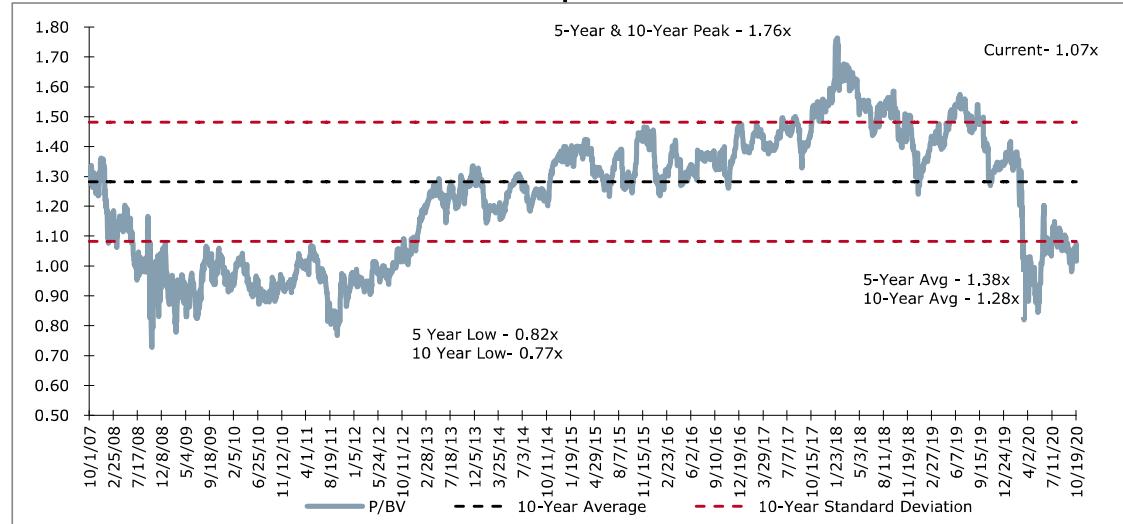
Premium Growth Above Us

- Net premiums rose 2.7% better than our 0.6% estimate and accelerated from -1.4% in Q2. The increase in premiums was due to higher Bond & Specialty and Personal Insurance volume, which more than offset premium declines in Business Insurance. Gross premiums rose by almost an equivalent level as net, rising by 2.8%.
- Business Insurance net premiums declined 1.4% versus our -0.9% estimate and -2.5% in the Q2. Bond and Specialty net premiums were up 3.6% versus our 3.9% estimate and 3.4% in the Q2. Personal Insurance net premiums increased by 7.9% versus our 1.8% estimate and -1.1% in the Q2. Within personal insurance, TRV saw a rise of 4.1% in auto (above -12.2% in Q2 as Q2 was impacted by the premium refunds; excluding the refunds Q2 was 4.4%) and growth of 14.0% in home (versus +12.8% in Q2).

Valuation

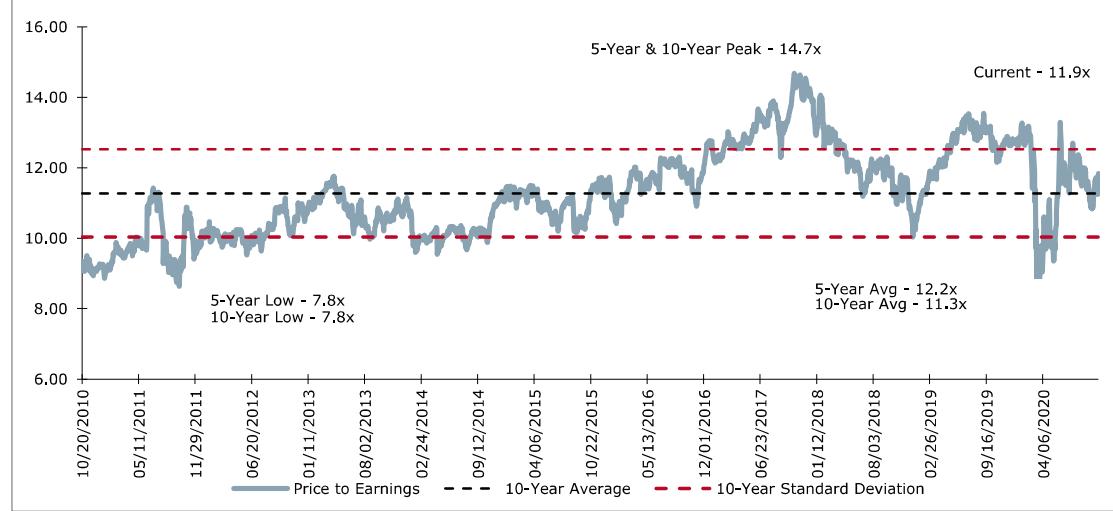
Current Valuation. The TRV shares are now trading at 1.07x book value, below its 5-year (1.38x) average and its 10-year (1.28x) average multiple. The shares are trading below peak levels of 1.76x. On a price-to-earnings basis, the shares are trading at 11.9x our 2020 EPS estimate and 10.7x our 2021 EPS estimate versus the 10-year average of 11.3x and 10-year peak of 14.7x

Exhibit 10. TRV Historical Price-To-Book Multiples



Source: FactSet and Wells Fargo Securities, LLC

Exhibit 11. TRV Historical Price-To-Earnings Multiples



Source: FactSet and Wells Fargo Securities, LLC

Price Target

Price Target: \$120 from \$115

Our price target of \$120 is based on around a 1.0x multiple of our projected 2021 book value estimate of around \$119 and 12.1x our 2021 EPS estimate of \$9.95. Risks to achieving our price target include large catastrophe losses, adverse reserve development, increased competition, a deterioration in loss costs, and a rise in D&O claims.

Investment Thesis

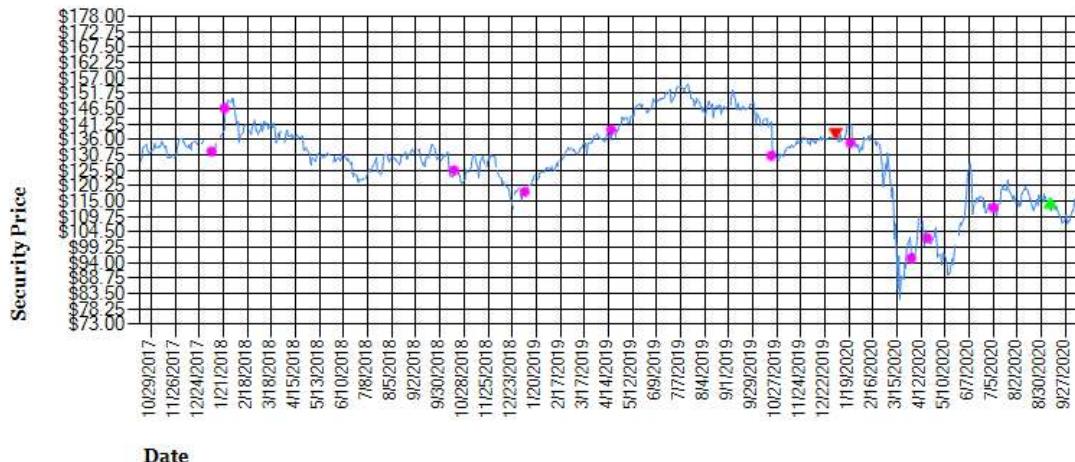
We believe that TRV will benefit from one of the hardest commercial pricing environment since 2003. Although we are positive on the commercial lines space as a whole, we are more cautious on TRV relative to peers due to its smaller account and higher workers' comp focus. We still believe that risk remain around social inflation, lower reserve releases, and Covid-19, but we believe that these risks are adequately reflected in shares with the risk/reward now more neutral.

Company Description

The Travelers Companies, Inc. (TRV) is the second largest writer of commercial lines in the United States and also the second-largest writer of personal insurance through independent agents. The company is organized into three business segments: Business Insurance (54% of 2019 net premiums written); Personal Insurance (37%); and Bond & Specialty Insurance (9%), which sell a wide range of insurance and surety products, as well as risk management services. Products are distributed primarily through independent agents and brokers in all 50 states and in select international markets.

Required Disclosures

The Travelers Companies, Inc. (TRV) 3-yr. Price Performance



| Date | Published Price (\$) | Rating Code* | Price Target | Val. Rng. Low | Val. Rng. High | Close Price (\$) |
|---------------|----------------------|--------------|--------------|---------------|----------------|------------------|
| 10/16/2017 | | Greenspan | | | | |
| 10/16/2017 | NA | 2 | 125 | NE | NE | 128.82 |
| ● 1/8/2018 | 131.45 | 2 | 133 | NE | NE | 131.45 |
| ● 1/23/2018 | 146.26 | 2 | 142 | NE | NE | 146.26 |
| ● 10/18/2018 | 124.80 | 2 | 136 | NE | NE | 125.14 |
| ● 1/8/2019 | 118.30 | 2 | 130 | NE | NE | 117.84 |
| ● 4/18/2019 | 138.93 | 2 | 140 | NE | NE | 138.93 |
| ● 10/22/2019 | 130.15 | 2 | 136 | NE | NE | 130.15 |
| ▼ 1/6/2020 | 137.02 | 3 | 136 | NE | NE | 137.17 |
| ● 1/23/2020 | 134.31 | 3 | 130 | NE | NE | 134.19 |
| ● 4/1/2020 | 99.35 | 3 | 110 | NE | NE | 95.20 |
| ● 4/21/2020 | 102.88 | 3 | 105 | NE | NE | 101.78 |
| ● 7/7/2020 | 114.57 | 3 | 112 | NE | NE | 112.48 |
| ▲ ● 9/11/2020 | 111.80 | 2 | 115 | NE | NE | 113.40 |

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- Price Target/Val Range Change

- ◆ Initiation, Resumption, Drop or Suspend
- Analyst Change
- Split Adjustment

Rating Code Key

- | | | | |
|---|-------------------|----|-------------|
| 1 | Overweight/Buy | SR | Suspended |
| 2 | Equal Weight/Hold | NR | Not Rated |
| 3 | Underweight/Sell | NE | No Estimate |

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